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| **1. Recent Corporate Law and Corporate Governance Developments** |
| **1.1 UK FRC publishes updated Turnbull guidance**  On the 13 October 2005, the UK Financial Reporting Council (FRC) published an updated version of 'Internal Control: Guidance for Directors on the Combined Code', also known as the Turnbull guidance. The new guidance will take effect for financial years beginning on or after 1 January 2006.  Publication of the updated guidance follows two consultation exercises, during the course of which the principles-based approach of the existing guidance was strongly endorsed by listed companies, the investment community and the accountancy profession.  As a result, only limited changes have been made to the guidance itself, while a new preface has been added to emphasise the need for companies to keep their application of the guidance under review and to provide shareholders with meaningful information in their annual report.  A copy of the updated Turnbull guidance is available from the [FRC website](http://www.frc.org.uk/corporate/internalcontrol.cfm" \t "_new).  **1.2 APRA statistics reveal superannuation assets exceed $740 billion**  On 13 October 2005, the Australian Prudential Regulation Authority (APRA) released the June 2005 edition of the Quarterly Superannuation Performance publication.  Total superannuation assets rose during the June 2005 quarter by 4.5 per cent to $741.7 billion. Industry funds showed the strongest growth during the quarter, with assets increasing by 8.2 per cent ($8.6 billion) to $112.9 billion. Retail fund assets grew by 5.4 per cent ($12.7 billion) to $247.7 billion. Public sector fund assets grew by 4.6 per cent ($5.6 billion) to stand at $128.3 billion, while corporate fund assets remained relatively stable, growing by 0.3 per cent ($0.2 billion) during the June quarter.  Over the same period, contributions to funds with at least $50 million in assets were $17.3 billion, with employers contributing $12.0 billion and members contributing $5.0 billion. Other contributions, including spouse contributions and government co-contributions, totalled $0.3 billion. Retail funds received $7.8 billion (45.3 per cent) of total contributions over the quarter. Public sector funds received $4.4 billion (25.3 per cent), industry funds received $4.0 billion (23.4 per cent) and corporate funds $1.0 billon (6.0 per cent).  At the end of June 2005, 28.0 per cent of superannuation assets ($150.3 billion) was invested in wholesale trusts and 25.2 per cent ($135.2 billion) was invested in life insurance companies. Individually managed mandates comprised 22.0 per cent of superannuation assets ($118.3 billion).  The return on assets was 3.0 per cent for the June quarter. The return for public sector funds was 3.4 per cent, industry funds 3.0 per cent, retail funds 2.8 per cent and corporate funds 2.7 per cent.  Copies of the publication are available on the [APRA website](http://www.apra.gov.au/Statistics/Quarterly-Superannuation-Performance.cfm" \t "_new).  **1.3 Taskforce on reducing the regulatory burden on business**  On 12 October 2005, the Australian Prime Minister, the Hon Mr John Howard MP, announced the appointment of a Taskforce to identify practical options for alleviating the compliance burden on business from Commonwealth Government regulation.  The Taskforce will examine and report on areas where regulatory reform can provide significant immediate gains to business.  It will be chaired by Mr Gary Banks, Chairman of the Productivity Commission, and will also include Mr Dick Humphry, the former Managing Director of the Australian Stock Exchange, Mr Rod Halstead, a corporate law expert with Clayton Utz, and Mrs Angela MacRae, a consultant to small business and Chairman of the Independent Contractors Association of Australia. The Taskforce will:   * identify specific areas of Commonwealth Government regulation which are unnecessarily burdensome, complex, redundant or duplicate regulations in other jurisdictions; * indicate those areas in which regulation should be removed or significantly reduced as a matter of priority; * examine non-regulatory options (including business self-regulation) for achieving desired outcomes and how best to reduce duplication and increase harmonisation within existing regulatory frameworks; and * provide practical options for alleviating the Commonwealth's 'red tape' burden on business, including family-run and other small businesses.   The Taskforce will report by 31 January 2006.  While the Taskforce will focus on areas that are predominantly the responsibility of the Commonwealth Government, it is to identify key areas in which the regulatory burden arises from overlaps with State and Territory legislation. The Taskforce will consult closely with business groups and other stakeholders.  The Government also intends to introduce a new annual review process to examine the cumulative stock of Australian Government regulation and identify an annual red tape reduction agenda. Reviews will be undertaken by the Productivity Commission. The Commission will call for public submissions on areas of red tape concern, based on a direction from the Treasurer and will propose an agenda to the Australian Government.  The Taskforce's website address is [www.regulationtaskforce.gov.au](http://www.regulationtaskforce.gov.au" \t "_new)  **1.4 Insolvency reform**  On 12 October 2005, the Parliamentary Secretary to the Australian Treasurer, the Hon Chris Pearce MP, announced an integrated package of reforms to improve the operation of Australia's insolvency laws.  The package proposes a number of reforms, including: improved access to the General Employee Entitlements and Redundancy Scheme (GEERS); enhancing the prospect of payment of employee entitlements and personal injury claims in insolvency; and the establishment of a fund to finance preliminary investigations of 'assetless' companies to curb fraudulent phoenix activity.  The Government will allocate an additional $62 million over four years to enhance the range of entitlements under GEERS. Since the Government introduced employee entitlements assistance in January 2000, over 54,000 Australian workers have received more than $661 million in assistance for their entitlements lost due to the insolvency of their employer.  As recommended by the Parliamentary Joint Committee on Corporations and Financial Services, the Government will retain the existing priority of employee entitlements in insolvency. The Government will also move to prevent this priority being downgraded in deeds of company arrangement without the agreement of employees, and clarify the status and priority of the Superannuation Guarantee Charge in external administrations.  The Government will allocate $23 million over four years to establish an 'asset less administration' fund and complementary enforcement programme by the Australian Securities and Investments Commission (ASIC). The fund will finance preliminary investigations by expert liquidators of companies, selected by ASIC, that have been left insolvent with little or no assets.  Reflecting the findings of the Report of the James Hardie Special Commission of Inquiry, the Government considers there is a strong case for introducing new protections for personal injury claimants, where a company expects a large number of successful personal injury claims arising from its conduct or products. However, the recognition of mass future claims in insolvency has risks that must be carefully addressed. As such, the Government will refer this issue to its expert advisory committee, the Corporations and Markets Advisory Committee (CAMAC), for detailed consideration.  Additionally, the Government will introduce minor reforms to improve the registration of insolvency practitioners, and to fine-tune the voluntary administration process.  The package has been developed after taking into account the recommendations of a number of recent reviews, including the Parliamentary Joint Committee on Corporations and Financial Services Report titled Corporate Insolvency Laws: a Stocktake, the Report of the James Hardie Special Commission of Inquiry, and several reports by the Corporations and Markets Advisory Committee.  Exposure draft legislation will be prepared in consultation with industry groups. It is anticipated that legislation will be circulated for public comment in early 2006 and a bill introduced later that year.  Further details about the reform package are available from the [Treasury website](http://www.treasury.gov.au/contentitem.asp?pageId=&ContentID=1022" \t "_new) and the reference to CAMAC is available on the [CAMAC website](http://www.camac.gov.au/camac/camac.nsf" \t "_new).  **1.5 Agreement reached in European Council on the 8th Company Law Directive on statutory audit**  On 11 October 2005, the European Commission welcomed a political agreement at first reading by the Council of Economic and Finance Ministers on the 8th Company Law Directive on statutory audit of annual accounts and consolidated accounts, which amends Council Directives 78/660/EEC and 83/349/EEC. Its objectives are to restore credibility of financial reporting and to enhance the EU's protection against the type of scandals that occurred in the past at companies such as Parmalat and Ahold. The Commission proposed the Directive on 16 March 2004 (see IP/04/340, MEMO/04/60) and it was approved by the European Parliament on 28 September 2005 in a form to which the Council has now agreed, without the need for a second reading by either the Parliament or the Council.  The new 8th Company Law Directive on statutory audit aims to reinforce and harmonise the statutory audit function throughout the EU. It sets out principles for public supervision in all Member States. It also introduces a requirement for external quality assurance and clarifies the duties of statutory auditors.  Moreover, harmonised principles of independence applicable to all statutory auditors through the EU have been defined. The Directive further improves the independence of auditors by requiring listed companies to set up an audit committee (or a similar body) with clear functions to perform. It also foresees the use of international standards on auditing for all statutory audits conducted in the EU. Adoption of these standards will be subject to strict conditions such as their quality and whether they are conducive to the European public good.  The Directive provides a basis for co-operation between regulators in the EU and regulators in other countries, such as the US Public Company Accounting Oversight Board (PCAOB). It also includes the creation of an Audit Regulatory Committee to complement the revised legislation and allow the speedy adoption of necessary implementing measures.  For further information is available on the [Europa website](http://europa.eu.int/comm/internal_market/auditing/index_en.htm" \t "_new).  **1.6 Draft FSR refinement regulations**  On 11 October 2005, the Parliamentary Secretary to the Australian Treasurer, the Hon Chris Pearce MP, released draft regulations implementing a number of proposed refinements to Financial Services Regulation (FSR).  The refinements, originally outlined in the Refinements to Financial Services Regulation proposals paper released on 2 May 2005, are designed to improve the operation of the FSR framework.  The draft regulations also implement refinement proposals to improve the operation of the legislation in practice and to identify the intent of the legislation by:   * clarifying the retail/wholesale client distinction; * streamlining disclosure where financial services are provided through intermediaries; * fine tuning in general advice definition; * defining the jurisdictional reach of the law; and * simplifying authorisation procedures for representatives.   The draft regulations were developed after several months of public consultations and take account of comments received from consumer and industry representatives on the original refinement proposals.  The Government seeks comment on the package of draft regulations, which is available on the [Treasury website](http://www.treasury.gov.au/contentitem.asp?NavId=037&ContentID=1020" \t "_new).  **1.7 Agreement reached in European Council on the Capital Requirements Directive**  On 11 October 2005, the European Commission welcomed the agreement by the Council of Economic and Finance Ministers to the European Parliament's legislative resolution on the Capital Requirements Directive for credit institutions and investment firms. The Directive, generally known as the Capital Requirements Directive but technically comprising two Directives, will introduce a new supervisory framework in the European Union which reflects the Basel II rules on capital measurement and capital standards agreed at the G-10 level. The Commission proposed the Directive on 14 July 2004 (see IP/04/899, MEMO/04/178) and it was approved by the European Parliament on 28 September 2005 in a form to which the Council has now agreed, without the need for a second reading by either the Parliament or the Council.  The Directive, which is one of the outstanding measures required to complete the EU Financial Services Action Plan, will modernise the existing framework to make it more comprehensive and risk-sensitive and to foster enhanced risk management amongst financial institutions. This will maximise the effectiveness of the framework in ensuring continuing financial stability, maintaining confidence in financial institutions and protecting consumers. Improved risk-sensitivity in the capital requirements will facilitate more effective allocation of capital, contributing to boosting the competitiveness of the EU economy.  A key aspect of the new framework is its flexibility. This provides institutions with the opportunity to adopt the approaches most appropriate to their situation and to the sophistication of their risk management. The new regime is also designed to ensure that the capital requirements for lending to small- and medium-sized enterprises (SMEs) are appropriate and proportionate.  Member States are to apply the Directive from the start of 2007, with the most sophisticated approaches being available from 2008. This is in line with the planned global introduction of the Basel II rules.  Further details on the EU policy on capital requirements are available on the [Europa website](http://europa.eu.int/comm/internal_market/bank/regcapital/index_en.htm" \t "_new).  **1.8 Regulators to share information on international financial reporting standards**  On 4 October 2005, the International Organization of Securities Commissions (IOSCO) announced that it is establishing arrangements for regulators to share decisions on the application of the International Financial Reporting Standards (IFRS).  The adoption of IFRS in many national jurisdictions and their use in numerous cross-border transactions should help to achieve convergence towards high quality global accounting standards that provide transparent and comparable information in general purpose financial reports.  A system will be established for participating IOSCO members and other independent enforcement organizations to share information and consult in order to maximize co-ordination and convergence. While each national regulator will retain the right to deal with an issue in its own right, the system will facilitate consistency.  IOSCO will assist participating regulators in cataloguing in a database, decisions made by regulators concerning application of IFRS. This will provide a reference source for input to future regulatory decisions. Participating regulators will also contact each other to discuss particular decisions.  On an ongoing basis, IOSCO will monitor issues related to the implementation of IFRS for indicators of issues that should be referred to the International Accounting Standards Board or the International Financial Reporting Interpretations Committee for consideration.  IOSCO anticipates that the database will be operational by the second half of 2006. At this stage it is not intended for the catalogue of decisions to be publicly accessible.  Further information is available on the [IOSCO website](http://www.iosco.org/" \t "_new).  **1.9 APRA releases Basel II advanced measurement approaches to operational risk**  On 4 October 2004, the Australian Prudential Regulation Authority (APRA) released its discussion paper and accompanying draft prudential standard on the implementation of the Basel II advanced measurement approaches to operational risk.  The discussion paper follows APRA's release of draft Basel II standards in April and July 2005 which form part of a suite of prudential standards that are expected to be finalised in 2007.  The discussion paper and draft prudential standard are available on [APRA's website](http://www.apra.gov.au/RePEc/RePEcDocs/Archive/discussion_papers/dp0025.pdf" \t "_new).  **1.10 IOSCO issues consultation report on international disclosure principles for cross-border offerings and listing of debt securities by foreign issuers**  On 3 October 2005, the International Organization of Securities Commissions (IOSCO) announced that it has published for public consultation a report on the 'International Disclosure Principles for Cross-Border Offerings and Listings of Debt Securities by Foreign Issuers' (International Debt Disclosure Principles).  The consultation report sets out substantive disclosure principles for documents used in public offerings and listings of "plain vanilla" corporate debt securities. IOSCO believes that the International Debt Disclosure Principles are especially pertinent given the increased volume of public offerings and listings of debt securities in the international capital markets, and the increased participation of retail investors in those markets.  The International Debt Disclosure Principles should provide useful guidance to securities regulators who are developing or reviewing their regulatory disclosure regimes for cross-border offerings and listings of debt securities. The principles-based format for this project is expected to provide maximum flexibility and adaptability, so that the International Debt Disclosure Principles can potentially be applied to a broader range of debt securities.  After the consultation process has concluded and all comments received from the public have been fully considered, IOSCO intends to issue a final version of the International Debt Disclosure Principles.  A copy of the consultation report is available on the [IOSCO website](http://www.iosco.org/" \t "_new).  **1.11 UK FSA publishes proposals for fund disclosures to retail clients**  On 30 September 2005, the UK Financial Services Authority (FSA) published a consultation paper CP05/13 'Bundled Brokerage and Soft Commissions Arrangements for Retail Investment Funds' which addresses the issue of how to ensure that investors in retail funds benefit from the enhanced disclosure regime being introduced for firms for bundled brokerage and soft commissions from 1 January 2006.  The paper examines how the needs and expectations of investors in retail funds can best be met and proposes measures that will support the FSA's aim of ensuring fairness and accountability for those investors.  The overall objective of the FSA's new regime is that investment managers should achieve value for money for any expenditure that is charged through to their customer’s portfolios. The aim is to achieve this through increased transparency and accountability by disclosing this expenditure to clients, thereby subjecting the manager to competitive pressure to ensure clients receive best value.  The FSA recognizes that the majority of retail investors will have little interest in receiving this detailed information as it would be largely meaningless to them or they have limited means of influencing the investment manager's behaviour if they are unhappy with it.  The FSA, in addressing this discrepancy, is proposing that an individual or body should act as a representative of retail investors who will consider the new disclosures on investors' behalf and interact with the manager where necessary.  Any representative will need to have an appropriate degree of expertise, authority and independence and so the FSA has made proposals for who would be suitable to carry out this role for each type of fund:   * for collective investment schemes (CIS), the depositary or trustee; * for with-profits funds, the committee or person appointed to review compliance with the Principles and Practices of Financial Management; * for investment trusts, the directors of the company, in particular those who are independent of the investment manager; * for unit-linked funds, either the with-profits committee if the company has one, or the appointed actuary, or the independent directors of the company.   The consultation paper is available on the [FSA website](http://www.fsa.gov.uk/" \t "_new).  **1.12 Proposals to refine ASIC's audit inspection powers**  On 30 September 2005, the Parliamentary Secretary to the Australian Treasurer, the Hon Chris Pearce MP, released a consultation paper on proposals in relation to the powers of the Australian Securities and Investments Commission (ASIC) to conduct audit inspections.  Discussions between ASIC and the US Public Company Accounting Oversight Board (PCAOB) have identified potential for significant rationalisation of the two regimes applying to the audit inspection process.  The objective of the proposed joint audit regulation programme is to ensure that Australian auditors that are registered with the PCAOB and their Australian audit clients are not required to undergo duplicate audit inspection processes by Australian and US regulators.  The proposals would give ASIC complementary updated powers for use solely in the domestic audit inspection context.  The consultation paper is available from the [Treasury website](http://www.treasury.gov.au/contentitem.asp?NavId=002&ContentID=1017" \t "_new).  **1.13 Global competitiveness report**  On 28 September 2005, the World Economic Forum (WEF) released The Global Competitiveness Report 2005-2006. Finland remains the most competitive economy in the world and tops the rankings for the third consecutive year. The United States is in second position, followed by Sweden, Denmark, Taiwan, Singapore, Iceland, Switzerland, Norway and Australia.  The following is a summary of the report prepared by the WEF.  The rankings are drawn from a combination of data, publicly available for each of the economies studied, and the results of the Executive Opinion Survey, an assessment conducted by the World Economic Forum, together with its network of partner institutes (leading research institutes and business organizations) in the countries covered by the Report. This year nearly 11,000 business leaders were polled in 117 economies worldwide. The survey questionnaire is designed to capture a broad range of factors affecting an economy’s business environment that are key determinants of sustained economic growth. Particular attention is placed on elements of the macroeconomic environment, the quality of public institutions which underpin the development process, and the level of technological readiness and innovation.  Finland is number one in the Growth Competitiveness Index (GCI) rankings and holds this position for the fourth time in the last five years. The country is very well managed at the macroeconomic level, but it also scores very high in those measures that assess the quality of its public institutions. Furthermore, the private sector shows a high proclivity for adopting new technologies and nurturing a culture of innovation. The United States, as last year, is ranked second: the country demonstrates overall technological supremacy, with a very powerful culture of innovation. However, technological prowess is partly offset by a weaker performance in other areas measured by the index. The US has a relatively low rank of 20 for the contracts and law indicator, with particular concerns on the part of the business community about the government's ability to maintain arm's-length relationships with the private sector, and in the formulation of policies more generally. But the country's greatest weakness concerns the health of its macroeconomic environment, where it ranks a low 47th overall. This echoes the increasingly vocal international concerns about the macroeconomic imbalances in the US economy, especially as regards the public finances.  The Nordic countries continue to hold prominent positions in the rankings among the top 10 most competitive economies this year, with Finland (1), Sweden (3), Denmark (4), Iceland (7) and Norway (9) all in privileged places. The performance of these countries demonstrates the great diversity within Europe, with some countries doing very well by any measure, while others struggle behind. The Nordics are also challenging the conventional wisdom that high taxes and large safety nets undermine competitiveness, suggesting that what is important is how well government revenues are spent, rather than the overall tax burden per se.  Elsewhere in Europe the most notable developments are the improvement in the relative position of Ireland, which has moved up 4 places to 26 in the overall rankings; the improvement of Poland, which has moved up 9 places to 51st place in the rankings; the continuing excellent performance of Estonia, ranked 20th for the second year in a row, and which is by a significant margin the most competitive economy among the 10 countries that joined the EU last year; and the significant decline of Greece (ranked 46, compared to 37 last year), which now has joined Italy (ranked 47) as the two lowest-ranking countries among the EU-25, bar Poland. Greece’s worsening performance is linked to a significant weakening in the quality of its overall macroeconomic environment, driven by a ballooning budget deficit and increasing pessimism on the part of the business community about the short-term economic outlook.  Leading within Asia are Taiwan and Singapore, ranked 5th and 6th respectively, some places ahead of the next Asian country covered by the GCI, Japan, ranked 12th. The distance between these top-ranked economies and Japan has increased since last year, reflecting Japan's relatively poor macroeconomic performance, particularly as regards management of the public finances. Taiwan and Singapore are economies that, through sustained good policies over the past few decades, have lifted their citizens from poverty, joining the ranks of the most prosperous and competitive economies in the world.  Compared with the other tigers, Hong Kong is ranked much lower at 28th place, having dropped 7 places since last year. This is attributable to a tangible deterioration in the quality of the institutional environment. Hong Kong saw a weakening in perceived judicial independence, the protection of property rights and in government favouritism in policy-making. Hong Kong’s ranks on irregular payments (corruption) have also fallen well below its previously excellent performance.  Australia, in 10th place, has moved up 4 places since last year, with improvements across many of the institutional and technology indicators measured by the index. The country has world-class public institutions, sound public finances and very low levels of corruption in the economy. And Australia's companies are measured as being very innovative, while harnessing new information and communications technologies extremely well.  China and India, 49th and 50th, respectively, now rank much more closely to one another than in previous years. While China dropped 3 ranks, India moved up 5 places. China had a slightly deteriorating score with regard to the country's macroeconomic environment, while India's improved position is due to a somewhat higher rank in the area of technology. Both China and India have had an excellent growth performance in recent years. However, both countries continue to suffer from institutional weaknesses which, unless addressed, are likely to slow down their ascension to the top tier of the most competitive economies in the world.  As in previous years, Chile, ranked 23rd, leads the way in Latin America by a wide margin. The gap with respect to the next best performer in the region has widened from 26 places in 2004 to 31 places in 2005, a characteristic not seen in any other region of the world. Chile continues to benefit from a combination of remarkably competent macroeconomic management and public institutions, which have achieved EU levels of transparency and efficiency: only 8 of the 25 EU members have stronger performances in the area of public institutions.  Mexico has fallen 7 places since last year to 55th, ceding its second spot in the regional ranking to Uruguay, while Brazil fell 8 places to 65th position. Both Mexico and Brazil suffered major plunges in those indicators that capture the quality of their public institutions, including factors such as judicial independence and favouritism of government officials in policy-making and procurement decisions. In the meantime, Venezuela, which had a ranking of 62 in 2001, continues its precipitous decline to the bottom of the rankings, falling another 4 places to 89th position overall this year. Widespread mismanagement has led to strong deterioration in all areas measured by the index: the macroeconomic environment has become highly unstable, the quality of public institutions has been eroded and there has also been a measured decline across a broad range of technology indicators.  Within the Middle East and North Africa (MENA) region, the small Gulf States perform quite well in the overall GCI rankings. The United Arab Emirates (UAE) and Qatar are ranked 18th and 19th, respectively. Terms-of-trade gains have boosted growth rates and reinforced already high levels of confidence in the business community, resulting from ongoing institutional modernization and improvements in macroeconomic management.  While most of the countries of the sub-Saharan African region are less competitive, the region does have a number of relative success stories. This includes South Africa (42nd), Botswana (48th), Mauritius (52nd) and Ghana (59th), the latter's competitiveness performance being even more notable, having improved by 9 places since 2004. Tanzania has also seen a significant improvement over the past year, moving up 11 places in the overall rankings. On the other hand, Namibia, a relatively good performer overall, lost 11 places over the past year, as, predictably, did Madagascar and Zimbabwe, losing 11 and 10 places, respectively. Zimbabwe is a particularly sad case, whose quick descent to the bottom of the world's competitiveness rankings reflects the continued deterioration of the institutional climate, including the disappearance of property rights, the corruption of the rule of law, and the implications these and other factors have had for macroeconomic management. The country has the worst ranking (117) for the quality of its macroeconomic environment.  The World Economic Forum continues to expand geographic coverage of The Global Competitiveness Report, currently featuring a total of 117 economies, of which the new entrants this year include Albania, Armenia, Azerbaijan, Benin, Cambodia, Cameroon, East Timor, Guyana, Kazakhstan, Kuwait, Kyrgyz Republic, Moldova, Mongolia, Qatar and Tajikistan.  Further information about the report is available on the [WEF website](http://www.weforum.org/site/homepublic.nsf/Content/Global+Competitiveness+Programme%5CGlobal+Competitiveness+Report" \t "_new).  **1.14 Changes in board structure and director remuneration in the top 100 US companies**  More top US firms are creating a relatively new leadership position that is independent of management - Lead Director - to share duties with the board chairman. Forty of the top 100 New York Stock Exchange (NYSE) and 27 of the top 100 NASDAQ companies now have a Lead Director position, typically offering additional compensation of US$15,000 to US$20,000, according to a survey published on 26 September 2005 by the executive compensation firm Frederic W Cook & Co. The Lead Director takes on some of the functions of the Chairman of the Board, such as presiding over executive sessions of the board.  The following companies have recently added lead (or presiding) directors:  Citigroup, Microsoft, Applied Materials, Chiron, Invitrogen, Dentsply and Career Education.  The top 100 firms in both the NYSE and NASDAQ also are restructuring the compensation for their boards of directors to be in sync with the changing operations of boards as corporate governance regulations take hold. According to the survey, America's top corporations are paying additional fees US$7,000 to US$10,000 to board members just for serving on a committee.  The 2005 Frederic W Cook & Co study, Director Compensation: NASDAQ 100 vs NYSE 100 also found:   * As a result of new Financial Accounting Standard Board (FASB) regulations requiring companies to record the fair value of compensation cost for stock options for fiscal years beginning after 15 June 2005, companies have been abandoning stock options for directors. As a result, compensation programs and levels for the NASDAQ and NYSE companies have become more similar. Last year, the compensation program at the NASDAQ companies was more than 50% higher than at the NYSE companies. This year, the difference has been reduced to 35%. Eight of the NASDAQ companies and 10 of the NYSE companies stopped granting options to directors. * Total compensation increased 17% at the NYSE companies and 4% at the NASDAQ companies over last year. * Companies commonly require directors to maintain share ownership levels: 26% of the NASDAQ and 67% of the NYSE companies disclose either formal ownership guidelines or share retention requirements.   A full copy of the report is available at:  [http://www.fwcook.com/](http://www.fwcook.com/" \t "_new)  **1.15 Regulation of the US mutual fund industry**  On 19 September 2005, the US Government Accountability Office (GAO) released a report on regulation of the US mutual fund industry.  As the frontline regulator of mutual funds, the US Securities and Exchange Commission (SEC) plays a key role in protecting the nearly half of all US households owning mutual funds, valued around US$8 trillion in 2005. Mutual fund abuses raised questions about the integrity of the industry and quality of oversight provided by SEC and self-regulatory organizations (SRO) that regulate broker-dealers selling funds.  The report assesses:   * changes SEC has made to, or is planning for, its mutual fund exam program; * key aspects of SEC's quality control framework for routine fund exams; and * the adequacy of SEC's oversight of NASD and the New York Stock Exchange in protecting shareholders from mutual fund sales abuses.   SEC is initiating several changes intended to strengthen its mutual fund exam program but faces challenges overseeing the fund industry. In the wake of the fund abuses, SEC has revised its past approach of primarily conducting routine exams of all funds on a regular schedule. It concluded these exams were not the best tool for identifying emerging problems, since funds were not selected for examination based on risk. To quickly identify problems, SEC is shifting resources away from routine exams to targeted exams that focus on specific risks. It will conduct routine exams on a regular schedule but only of funds deemed high risk. SEC also is forming teams to monitor some of the largest groups of advisers and funds. Although SEC is seeking to focus its resources on higher risk funds and activities, the resource tradeoffs it made in revising its oversight approach raise significant challenges. The tradeoffs may limit SEC's capacity not only to examine funds considered lower risk within a 10-year period but also to accurately identify which funds pose higher risk and effectively target them for routine examination. Potentially taxing its resources further, SEC recently adopted a rule to require advisers to hedge funds (investment vehicles generally not widely available to the public) to register with it. This rule is expected to increase SEC's exam workload, but the precise extent is not yet known. SEC has integrated some quality controls into its routine exams, but certain aspects of its framework could be improved.  SEC relies on experienced staff to oversee all exam stages but does not expressly require supervisors to review work papers or document their review. GAO found deficiencies in key SEC exam work papers, raising questions about the quality of supervisory review. SEC also does not require examiners to prepare written exam plans, though they use considerable judgment in customizing each exam. Written plans could serve as a guide for conducting exams and reviewing whether exams were completed as planned. As done by other regulators, SEC also could review a sample of work papers to test compliance with its standards. A primary tool that SEC uses to assess the adequacy of SRO oversight of broker-dealers offering mutual funds provides limited information for achieving its objective and imposes duplicative costs on firms. To assess SRO oversight, SEC reviews SRO exam programs and conducts oversight exams of broker-dealers, including their mutual fund sales practices. SEC's oversight exams take place 6 to 12 months after SROs conduct their exams and serve to assess the quality of SRO exams. However, GAO reported in 1991 that SEC's oversight exams provided limited information in helping SROs to improve their exam quality, because SEC and the SROs used different exam guidelines and their exams often covered different periods. GAO found that these problems remain, raising questions about the considerable resources SEC devotes to oversight exams. GAO also found that SEC has not developed an automated system to track the full scope of work done during its oversight exams. Thus, SEC cannot readily determine the extent to which these exams assess mutual fund sales practices.  The full report is available on the [GAO website](http://www.gao.gov/" \t "_new).  **1.16 SEC proposes changes in filing deadlines and accelerated filer definition; postpones section 404 compliance date for non accelerated filers; proposes issuing section 28(e) interpretive guidance**  On 21 September 2005, the US Securities and Exchange Commission (SEC) voted to propose for comment amendments to filing deadlines for periodic reports required by rules under the Securities Exchange Act of 1934 and changes in accelerated filer definitions; decided to postpone for an additional year the compliance date for filing internal control reports by companies not designated as accelerated filers; and voted to publish for comment proposed interpretive guidance concerning Section 28(e) of the Securities Exchange Act of 1934.  **(a) Periodic report filing deadlines and the definition of an accelerated filer**  The Commission voted to propose amendments to the periodic report filing deadlines and the Exchange Act Rule 12b-2 definition of an accelerated filer.  The proposals would:   * create a new category of companies called "large accelerated filers"; * adjust the definition of "accelerated filers"; * cause large accelerated filers to become subject to a 60-day Form 10-K annual report deadline and a 40-day Form 10-Q quarterly report deadline next year and in subsequent years; * maintain the current 75-day Form 10-K annual report deadline and 40-day Form 10-Q quarterly report deadline for accelerated filers next year and in subsequent years; and * amend the definition of accelerated filer to ease restrictions on the process for exiting accelerated filer status.   **(i) Large accelerated filers and accelerated filers**  The proposed amendments would create a new category of filers, "large accelerated filers", for companies that have a public float of US$700 million or more and meet the same other conditions that apply to accelerated filers. The proposed amendments also would redefine "accelerated filers" as companies that have at least US$75 million but less than US$700 million in public float.  **(ii) Amendments to the accelerated filer definition**  The proposed amendments would modify the procedures by which accelerated filers can exit accelerated filer status by permitting an accelerated filer whose public float has dropped below US$25 million to file an annual report on a non-accelerated basis for the same fiscal year that the determination of public float is made. The proposed amendments similarly would permit a large accelerated filer to exit large accelerated filer status once its public float has dropped below US$75 million.  **(b) Extension of compliance date of internal control reporting requirements for companies that are not accelerated filers**  The Commission voted to extend for an additional one year the compliance dates regarding its internal control reporting requirements rules for companies that are not accelerated filers. The amendments require a public company subject to the reporting requirements under the Securities Exchange Act of 1934 to include in its annual report a report by management on the effectiveness of the company's internal control over financial reporting and an accompanying auditor’s report.  Under the new compliance schedule, a company that is not an accelerated filer, including a foreign private issuer that is not an accelerated filer, will begin to be required to comply with the Section 404 requirements for its first fiscal year ending on or after 15 July 2007. A foreign private issuer that is an accelerated filer and that files its annual reports on Form 20-F or Form 40-F, must begin to comply with the internal control over financial reporting and related requirements in the annual report for its first fiscal year ending on or after 15 July 2006.  Ongoing efforts by the Committee of Sponsoring Organizations of the Treadway Commission to develop an enhanced COSO Framework for smaller public companies, and the continuing evaluation of the impact of the internal control over financial reporting requirements on smaller public companies by the SEC Advisory Committee on Smaller Public Companies warrant the deferral of the compliance dates for non-accelerated filers. The extension is consistent with a recent Advisory Committee recommendation.  The Commission also is soliciting public comment on several questions about the application of the internal control reporting requirements including questions regarding the amount of time and expense that companies that are not accelerated filers have incurred to date to prepare for compliance with the internal control reporting requirements.  **(c) Proposed interpretive guidance regarding client commissions**  The Commission voted to publish for comment interpretive guidance on money managers' use of client commissions to pay for brokerage and research services under Section 28(e) of the Securities Exchange Act of 1934. Section 28(e) creates a "safe harbour" by providing that a person who exercises investment discretion with respect to an account is not deemed to have acted unlawfully or to have breached a fiduciary duty under state or federal law solely by reason of having caused an account to pay more than the lowest available commission if that person determines in good faith that the amount of the commission is reasonable in relation to the value of the "brokerage and research services" received.  The proposed interpretive guidance would clarify that the scope of the Section 28(e) safe harbour is limited to brokerage and research services that:   * satisfy the eligibility criteria in the statute; * provide lawful and appropriate assistance to the money manager in carrying out his decision-making responsibilities; and * satisfy the requirement that the money manager make a good faith determination that commissions paid are reasonable in relation to the value of the products and services provided by broker-dealers in connection with his responsibilities to the advisory accounts for which he exercises investment discretion.   The Commission also voted to publish for comment guidance on commission-sharing arrangements.  The full text of detailed releases concerning each of these items is available on the [SEC website](http://www.sec.gov/" \t "_new).  **1.17 Latest UK executive remuneration study**  A new report shows a rise in bonus levels, and a greater emphasis on performance-based reward for executives in leading UK companies. The report by Deloitte is titled "Executive Directors' Remuneration".  Salary increases are slowing, with the median basic salary increase for executive directors in the FTSE 350 being 6.5% compared to 7.1% in 2004 and 7.5% in 2003. Although executive salaries continue to increase faster than for all employees (average earnings increased by 4.4% in 2004), of more significance is the increase in the opportunity to earn more for performance. The typical maximum annual bonus award is now 100% of salary in both FTSE 100 and FTSE 250 companies. Within the 30 largest UK companies the maximum potential bonus has increased from 125% to 150% of salary. For achieving on target performance, 50% of the potential bonus is earned.  The rise in bonus levels has been accompanied by an increase in the introduction of a deferred element in these plans. Deferred annual incentive plans are now in place in 61% of FTSE 100 companies and 44% of FTSE 250 companies, compared to 56% and 34% two years ago.  Deferral arrangements vary greatly, but typically they require some of the annual bonus to be paid in shares which must then be retained for several years, working as a 'lock in'. There may also be the opportunity to receive additional 'matching' shares if further performance criteria have been achieved during the deferral period.  The number of share option plans being introduced and in operation is decreasing, with performance share plans being used in their place. Share options are regularly granted to executive directors in 52% of FTSE 100 companies and 48% of FTSE 250 companies compared to 85% and 76% respectively two years ago. Performance share plans are now operated by 82% of FTSE 100 companies and 62% of FTSE 250 companies compared to 64% and 43% respectively two years ago.  The value of executive pensions is significant and this is expected to lead to increasing attention from institutions, who will be seeking an explanation and justification for generous pension arrangements. Basic salary and pension increase with company size.  Pressure from the shareholders and institutional investors is having an impact. The 2005 report demonstrates two areas where such pressure has resulted in significant change. Only 2% of executive directors in FTSE 100 and 3% in FTSE 250 companies now have a notice period in excess of 12 months compared to 16% and 11% two years ago. This dramatic decrease has followed pressure from shareholders and governance bodies over the past 24 months to eradicate the possibility of rewarding executives when the business has failed.  The provision in share option plans that allow executives 'two bites at the cherry' i.e. where performance conditions can be measured more than once if they are not met at the end of the performance period, are also becoming less common, with a marked decrease in their prevalence in the past two years. Currently, 77% of FTSE 100 and 73% of FTSE 250 companies do not allow any re-testing of performance conditions compared with 33% and 45% last year.  More information about the study is available on the [Deloitte website](http://www.deloitte.com/dtt/home/0,1044,sid%253D2825,00.html" \t "_new).  **1.18 Emerging trends in internal controls**  In September 2005 Ernst & Young released its fourth annual global survey titled "Emerging Trends in Internal Controls". Ernst & Young interviewed 255 US companies regarding the impact of section 404 of the Sarbanes-Oxley Act 2002, which requires companies to self-assess their internal controls to prevent accounting mistakes and fraud, and have their internal controls approved by an external auditor. Some of the key findings of the survey included:   * Over one-fourth of companies with revenues greater than US$5 billion remediated more than 500 individual controls prior to initial compliance. * Over 70% of companies conducted significant remediation of IT systems and controls prior to initial compliance. * Among 70% of companies, section 404-related costs were over 50% higher than original estimates. * Over 80% of companies still expected to test 75% or more of the controls identified in Year 1. * 58% of companies with revenues less than US$5 billion will dedicate more than half of all internal audit resources to section 404-related activities. * 76% of companies anticipate using some form of control self-assessment (CSA) to support ongoing section 404 compliance. * 53% anticipate deploying an enterprise risk management (ERM) program within one year. * 87% anticipate value simply through the enhanced accountability and ownership of controls promoted by section 404. * A risk-based, top-down approach to establishing scope and testing strategies should help reduce required hours, although the shift may require several years to fully implement.   The full report is available on the [EY website](http://www.ey.com/global/content.nsf/International/Home" \t "_new).  **1.19 Trends in the corporate governance practices of the 100 largest US public companies**  A new report, published in September 2005 by Shearman & Sterling, examines trends in the corporate practices of the 100 largest US public companies.  The following is an extract from the report's executive summary.  **(a) Director independence and other qualifications**  The Top 100 companies have continued to exceed the minimum independent director requirements of the NYSE and Nasdaq listing standards. Although listing standards require that boards be comprised of a majority of independent directors, 54 of the Top 100 companies surveyed this year, eight more than in 2004, have adopted standards more stringent than a simple majority. The numbers are even more striking with respect to the actual practices of the Top 100 companies.  Independent directors continue to comprise 75% or more of the boards of 81 Top 100 companies surveyed this year as they did in 2004, and the CEO is the only non-independent director of 37 of the Top 100 companies surveyed this year, an increase from 35 such companies in 2004.  As financial reporting issues remain in the spotlight, so does the role of the audit committee. It is perhaps not surprising, then, that many companies continue to take steps to bolster public confidence, including increasing the level of financial expertise represented on the audit committee. SEC rules require disclosure of the name of only one audit committee financial expert even if more than one such expert serves on the audit committee, but 48 of the Top 100 companies surveyed this year, six more than in 2004, voluntarily chose to publicly disclose the name of more than one audit committee financial expert. Of those 48 companies, 15 disclosed that all of their audit committee members are audit committee financial experts.  **(b) Board leadership**  One area in which there has been little change over the last three years is the number of companies at which different individuals serve as chairman of the board and chief executive officer (CEO).  As of 15 May 2003, different individuals served as chairman and CEO at 14 of the Top 100 companies. This number was unchanged as of 15 June 2004 and has increased to 19 companies as of 15 June 2005. Of these 19 companies, only four have adopted policies requiring that different individuals serve as chairman and CEO.  In most instances, any separation of the two offices continues to be more closely related to the relevant company's CEO succession process than adoption of a particular corporate governance policy. The absence of any significant increase in the separation of the two offices since 2003, coupled with the reduction in the number of shareholder proposals advocating such separation included in the proxy statements of the Top 100 companies during the 2005 proxy season, may signal that this issue has become a lower priority for shareholder activists. Although there was a significant increase in the number of such shareholder proposals included in the proxy statements of the Top 100 companies from 11 in 2003 to 19 in 2004, there were only 12 such proposals during the 2005 proxy season.  The presence of a lead independent or presiding director has often been suggested as an alternative to a requirement that an independent director serve as chairman of the board. Despite the NYSE listing standard requirement that companies disclose the name or method of selection of the director who presides over executive sessions of non-management directors, no consensus regarding the selection or responsibilities of such presiding director has developed. Thirty-one of the Top 100 companies provide for rotation of the presiding director based upon the subject matter to be discussed at each executive session or various other criteria, 24 have named the nominating/governance committee chair as the presiding director and 20 require that the independent or non-management directors select the presiding director. Only 28 of the Top 100 companies have given their presiding directors responsibilities in addition to presiding over executive sessions.  **(c) Director time commitments**  The number of board and committee meetings has continued to increase in connection with the widespread expectation that directors would be required to devote significantly more time in order to fill their responsibilities. In 2003, 51 Top 100 companies reported holding eight or more meetings of the board of directors; that number increased to 54 companies in 2004 and 65 in 2005. Even more significant are the increases in the numbers of committee meetings over the last three years. In 2003, 81 Top 100 companies reported holding six or more audit committee meetings; that number increased to 86 companies in 2004 and 94 in 2005. In 2003, 67 Top 100 companies reported holding five or more compensation committee meetings; that number increased to 74 companies in 2004 and 81 in 2005. In 2003, 27 Top 100 companies reported holding five or more nominating/governance committee meetings; that number increased to 45 companies in 2004 and 55 in 2005.  Given the increased time commitment required of directors to fill their responsibilities, investors have focused on the number of boards on which directors serve. Institutional Shareholder Services (ISS) announced that, for the 2004 proxy season, it would recommend withholding votes from directors who serve on more than six public company boards. For the 2005 proxy season, ISS announced that in addition to its six-board policy, it would recommend withholding votes from CEOs of publicly traded companies who serve on more than two public company boards in addition to their own board. Investor attention to this issue may well explain the increase in the number of Top 100 companies that have adopted some sort of policy relating to service on multiple boards from 76 in 2004 to 86 in 2005 and the increase in the number of Top 100 companies that place any limits on the number of boards on which their directors may serve from 29 in 2004 to 42 in 2005.  However, in most instances, any policies limiting the number of boards on which a director may serve either exempt directors who at the time of adoption of the limitation serve on a number of boards in excess of the limits or allow the board to find that such service does not interfere with such director’s ability to fulfil his or her responsibilities. Nonetheless, 45 of the Top 100 companies surveyed this year have at least one director who continues to serve on five or more public company boards, an increase from 42 such companies surveyed in 2004.  **(d) Director compensation**  Given the increased meeting frequency of boards and their committees, it is not surprising that director compensation levels have also increased. Nearly all of the Top 100 companies, 98 of those surveyed in each of 2003, 2004 and 2005, paid their directors annual cash retainers, and the aggregate amount of annual cash retainers paid to directors has increased over the last three years. In 2003, three Top 100 companies reported annual cash retainers in excess of US$80,000; that number increased to nine companies in 2004 and 11 in 2005. In 2003, 55 of the Top 100 companies reported annual cash retainers in amounts of US$40,000 or less; that number fell to 39 companies in 2004 and 29 in 2005.  The composition of director compensation has also evolved over the last three years. The number of Top 100 companies that reported the inclusion of committee retainers in their director compensation packages has increased from 80 companies surveyed in 2003 to 91 companies surveyed this year. Recent trends in the nature of equity compensation for directors reflect the concern that options, which only have value if the stock price increases, could divert the loyalty of directors by keeping their focus on short-term gains in contrast to aligning director compensation with the long-term interests of shareholders. The number of Top 100 companies surveyed this year that reported grants of stock options as a component of director compensation decreased to 55 from 70 in 2003. Conversely, the number of Top 100 companies surveyed this year that reported grants of stock and restricted stock increased to 36 and 47, respectively, from 31 and 25, respectively, in 2003.  **(e) Stock ownership guidelines**  In an additional effort to more closely align the interests of directors and executive officers with the long-term interests of shareholders, a significant majority of the Top 100 companies surveyed this year have adopted director or executive officer stock ownership guidelines, and the number of such companies has steadily increased over the last three years. Sixty-six of the Top 100 companies surveyed this year reported stock ownership guidelines for both directors and executive officers, nine reported guidelines for executives only and nine reported guidelines for directors only, compared to 34, 20 and 11, respectively, of the Top 100 companies surveyed in 2003. Thirty-eight of the director stock ownership guidelines and 63 of the executive stock ownership guidelines require the director or executive officer, as applicable, to hold stock valued at a percentage of his or her base salary or annual retainer.  In order to help directors meet these guidelines, 49 of the Top 100 companies surveyed this year permit directors to elect to receive their cash compensation in the form of stock, restricted stock, options or a combination thereof, a significant increase from 38 such companies in 2003.  **(f) Shareholder proposals**  The last three years have seen a shift in the numbers and types of shareholder proposals included in the proxy statements of the Top 100 companies. Despite speculation that the number of shareholder proposals would continue to increase as a result of shareholder activism and the SEC's proposed proxy access rule, nearly one-third of the Top 100 companies did not include any shareholder proposals in their proxy statements during the 2005 proxy season. The number of certain "traditional" shareholder proposals, such as those advocating removal of poison pills and declassification of boards, has declined over the past three years. Rather than reflecting a lack of interest of shareholder activists in these topics, the decline is more indicative of the fact that fewer Top 100 companies have a poison pill or staggered board.  In 2004, 33 Top 100 companies had a poison pill, and 54 Top 100 companies had a staggered board; in 2005, those numbers fell to 27 and 38, respectively. From 2003 to 2005, there was a corresponding reduction in the number of shareholder proposals calling for redemption of, or a shareholder vote on, poison pills from 25 to three and in the number of shareholder proposals calling for the annual election of directors from 10 to four.  In addition, certain "new" shareholder proposals have gained prominence. In 2003, no Top 100 company included a shareholder proposal in support of the removal of supermajority voting provisions in its proxy statement, but, in 2005, seven of the Top 100 companies included such a shareholder proposal in their proxy statements.  The number of shareholder proposals for majority voting in director elections has seen the largest increase, from no such proposals included in the proxy statements of the Top 100 companies in 2003 to 15 such proposals in 2005, fuelled primarily by the demise of the SEC's proxy access proposed rule and the campaigns of various unions. Although the official results of the majority vote proposals have not yet been reported in SEC filings, there have been press reports that these proposals have received significant support from shareholders, and a few companies have voluntarily adopted forms of majority voting in director elections.  The full annual survey is available at: [http://www.shearman.com/](http://www.shearman.com/" \t "_new)  **1.20 Adoption of a directive on cross-border mergers in the European Union**  On 20 September 2005, the Council of the European Union adopted a directive on cross-border mergers of companies aiming at facilitating the carrying-out of cross-border mergers between various types of limited liability companies governed by the laws of different Member States of the European Union (PE-CONS 3632/05, 11444/05 and 11444/05 ADD1). The directive was adopted at first reading under the CO-decision procedure.  This directive will facilitate the cooperation and consolidation between companies from different Member States by reducing the difficulties encountered, at the legislative and administrative levels, by cross-border mergers of companies in the Community. It is expected to reduce costs of such operations, while guaranteeing the requisite legal certainty and enabling as many companies as possible to benefit.  The key features of the agreed text are:  • The directive will apply to mergers of limited liability companies, as defined in the Directive, formed in accordance with the law of a Member State and having their registered office, central administration or principal place of business within the Community, provided at least two of them are governed by the laws of different Member States.  • The directive provides for the possibility for Member States to apply certain provisions and formalities applying to domestic mergers to transnationals mergers in a manner which takes into account the cross-border nature of such mergers. In addition, Member States will have the possibility to adopt specific provisions regarding the protection of minority members of a merging company, who have opposed the cross-border merger.  • The establishment of a minimum content of the common draft terms of cross-border mergers for each of the companies concerned in the various Member States while leaving the companies free to agree on other items.  • The principle that the common draft terms of a cross-border merger must be approved by the general meeting of each of those companies.  • The monitoring of the completion and legality of the decision-making process in each merging company must be carried out by the national authority having jurisdiction over each of those companies, whereas monitoring of the completion and legality of the cross-border merger should be carried out by the national authority having jurisdiction over the company resulting from the cross-border merger.  • On the key issue of employee participation rights, the general principle is that the national law governing the company resulting from the cross-border merger will apply. As an exception to this general principle, the principles and procedures concerning employee participation laid down in the European Company (SE) Regulation and Directive should apply if at least one of the merging companies has an average number of employees in the six months before the publication of the draft terms of the cross-border merger that exceeds 500 and is operating under an employee participation system, or where the national law applicable to the company resulting from the cross-border merger does not:  – provide for at least the same level of participation as operated in the relevant merging companies, measured by reference to the proportion of members of the administrative or of the supervisory organ or their committees or of the management group, which covers the profit units of the company, subject to employee representation, or  – provide for employees of establishments of the company resulting from the cross-border merger and situated in other Member States the same entitlement to exercise participation rights as is enjoyed by those employees employed in the Member State where the registered office of the company resulting from the cross-border merger is situated.  The threshold for the application of the European Company standard rules will be 33 1/3% of the total number of employees in all merging companies that must have operated under some kind of employee system.  Another important provision aims at protecting employees' rights in subsequent domestic mergers for a period of three years after the cross-border merger has taken effect.  Member States will have a period of two years to adapt national laws to comply with the provisions of the new directive.  **1.21 Government response to report on corporate insolvency laws**  In June 2004, the report of the Australian Parliamentary Joint Committee on Corporations and Financial Services titled "Corporate Insolvency Laws: a Stocktake" was published.  The report made a number of recommendations for reform. The report is available on the [Committee website](http://www.aph.gov.au/senate/committee/corporations_ctte/index.htm" \t "_new).  On 13 October 2005, the Government responded to the Committee's report. The Government's response is contained in the Senate Hansard of 13 October 2005 (pages 75 - 86) which is available at [http://www.aph.gov.au/hansard/senate/dailys/ds131005.pdf](http://www.aph.gov.au/hansard/senate/dailys/ds131005.pdf" \t "_new)  **1.22 Lecture - enlightened shareholder value and the new responsibilities of directors**  On 4 October 2005, Professor Paul Davies, Cassell Professor of Commercial Law at the London School of Economics, delivered a lecture at the University of Melbourne Law School titled "Enlightened shareholder value and the new responsibilities of directors".  The transcript of the lecture is available on the Centre for Corporate Law and Securities Regulation website at:  [http://cclsr.law.unimelb.edu.au/research-papers/index.html](http://cclsr.law.unimelb.edu.au/research-papers/index.html" \t "_new)  **1.23 Employee entitlements and corporate insolvency and reconstruction**  A paper by Justice Simon Whelan, Supreme Court of Victoria and Leon Zwier, Partner, Arnold Bloch Liebler, titled "Employee entitlements and corporate insolvency and reconstruction" is available on the Centre for Corporate Law and Securities Regulation website at: [http://cclsr.law.unimelb.edu.au/research-papers/index.html](http://cclsr.law.unimelb.edu.au/research-papers/index.html" \t "_new)  **1.24 The Melbourne Law School 2006 graduate law program**  Commercial and corporate law provides the framework for business transactions.  The Melbourne University Graduate Law Program offers diversity, quality and the opportunity to specialise in key areas of law including Commercial and Corporate Law and Banking and Financial Services Law.  Highlights of the 2006 program include: 127 subjects, 25 of which are completely new, 35 interlinked coursework degrees and diplomas, expert tuition blending theory and practice, 40 visiting international Faculty, a stimulating graduate student cohort and maximum use of information technology.  80% of the 2006 subjects are taught on an intensive basis (offering a high level of convenience for interstate and overseas based students).  Some of the 127 subjects offered in 2006 are:  **Finance**   * Banking and Debt Recovery in Asia * Consumer Banking * Derivatives Law and Practice * Financial Services Law * Law of Secured Finance * New Directions in Law and Economics * Project Finance * Securitisation   **Corporate and General Commercial**   * Advanced Restrictive Trade Practices * Commercial Law in Asia * Company Takeovers * Comparative Companies Law in Asia * Competition Regulation of Mergers * Corporate Governance and Directors’ Duties * Equity and Commerce * Liability for Pure Economic Loss * Market Power and Competition Law * Personal Property * Regulation of Securities Offerings * United States Securities Regulation   **Construction**   * Advanced Construction Claims * Advanced Construction Contracts * Avoiding and Managing Construction Disputes * Construction Contracts * Construction: Principles into Practice * International Construction Law * Remedies in Construction Disputes * Rights and Liabilities in Construction   **Dispute Resolution**   * Advanced Litigation * Alternative Dispute Resolution * Commercial Dispute Resolution in Asia * International Commercial Arbitration * Proof in Litigation * Transnational Commercial Litigation   **e-Law**   * Cybercrime * Cybersecurity Law * Electronic Commerce Law   **Energy, Resources and the Environment**   * Infrastructure Delivery A: Principles and Practice * International Environmental Law * International Oil and Gas Transactions * Mineral Law * Native Title Law and Practice * Regulation and the Law   **Insurance**   * Professional Indemnity Insurance   **Intellectual Property**   * Copyright Law * Designs Law and Practice * Intellectual Property in the Digital Age * International Issues in Intellectual Property * Interpretation and Validity of Patent Specifications * Licensing Law and Technology Transfer * Patent Law * Patent Practice * Trade Mark Practice * Trade Marks and Unfair Competition   **International Law**   * Developing Countries and the WTO * Free Trade Agreements * International Trade Law * International Trade Remedies in the WTO * Principles of WTO Law   **Legal Organisations Management**   * Law Firm Strategy and Structure * Managing Clients * Managing Resources and Processes   **Media**   * Defamation Law * Film and Television Law: Production, Financing and Distribution   **Sports Law**   * Event Management Law * Introduction to United States Sports Law * Sports Law: Entities and Governance * Sports Labour Law   **Taxation**   * Advanced Corporate Taxation * Australian International Taxation * Capital Gains Tax: Problems in Practice * Corporate Taxation * Current Issues in Tax Avoidance * Fiscal Reform and Development * Goods and Services Tax Principles * State Taxes and Duties * Taxation Administration: Penalties, Prosecutions and Ethics * Taxation of Business and Investment Income A * Taxation of Business and Investment Income B * Taxation of Consolidated Groups * Taxation of Remuneration * Taxation of Small and Medium Enterprises B * UK International Taxation in its European Context |
| **2. Recent ASIC Developments** |
| **2.1 Directors notification of shareholdings**  On 19 October 2005, the Australian Securities and Investments Commission (ASIC) and the Australian Stock Exchange Limited (ASX) urged company directors to ensure they are complying with the requirement to notify their interests, or changes in their interests, to the market under the Listing Rules and the [Corporations Act 2001](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "Default) (the Act).  ASIC and ASX are undertaking a joint campaign to increase awareness among listed public company directors of their obligations under the Listing Rules and the Act, and to ensure a high level of compliance.  This campaign follows a review of ASX referrals to ASIC over the past 18 months and the recent work done by the BT Governance Advisory Service that indicate compliance with these obligations is not adequate at present.  The Act requires every director of a listed company to notify the relevant market operator (ASX, Bendigo Stock Exchange, Newcastle Stock Exchange or Australia Pacific Exchange) about holdings and changes to relevant interests, no matter how small, in securities of the company of which they are a director. This section of the Act is different from the substantial shareholding provisions and covers a wider variety of securities.  ASIC periodically conducts focused reviews of compliance with the Act, specifically section 205G, and most recently in 2001 targeted over 80 directors for failing to lodge notifications. As a result of this work 99 per cent of these directors subsequently lodged notices with the ASX. As well as failure to lodge, ASIC has also seen many instances of late lodgement ranging from days to months.  ASIC will conduct this work in cooperation with the ASX who have responsibility for ensuring compliance with Listing Rules 3.19A and 3.19B. These listing rules require listed entities to notify the ASX within five days of certain interests in securities held by directors at the time of commencing and ceasing to be directors, as well as any changes to a director's interests in securities while holding office. These listing rules complement the requirements of section 205G in promoting a transparent market.  The director is personally responsible for notifying their interest, within five business days under the Listing Rules and within 14 days under the Act, of appointment or listing of the company (whichever is relevant) and thereafter within five or 14 days of any change (as the case may be).  ASIC has produced guidance (ASIC information sheet: Notifying the ASX about directors' interests in company securities) which is available on the [ASIC website](http://www.asic.gov.au/asic/asic.nsf" \t "_new).  ASX has also produced guidance - Guidance Note 22 - Director Disclosure of Interests and transactions in Securities and Companies Update 11/05 - Action on non-disclosure of directors' interests, which is available on the [ASX website](http://www.asx.com.au/" \t "_new).  **2.2 ASIC's 2004-2005 annual report**  On 14 October 2005, the Chairman of the Australian Securities and Investments Commission (ASIC), Mr Jeffrey Lucy, announced that the Parliamentary Secretary to the Treasurer, The Hon Chris Pearce MP, had tabled ASIC's annual report for the 2004-05 financial year.  In highlights of the year, ASIC:   * brought wrongdoers to justice: HIH directors Rodney Adler, Ray Williams and Terry Cassidy were among 27 criminals jailed for more than 96 years. * helped more people by responding to a greater number of complaints: there was 40 per cent more action on reports of crime and misconduct, and ASIC staff answered 40 per cent more phone calls on enforcement, consumer and regulatory issues; * promoted stronger markets: ASIC achieved better disclosure for investors, and conducted assessments of new financial markets to create more certainty for business, and * assisted companies restructure or merge in transactions worth at least $41 billion.   The 2004-2005 annual report is available on the [ASIC website](http://www.asic.gov.au/asic/asic.nsf" \t "_new).  **2.3 ASIC, ACCC promote fair debt collection practices**  On 14 October 2005, the Australian Competition and Consumer Commission (ACCC) and the Australian Securities and Investments Commission (ASIC) issued two jointly produced publications, aimed at improving standards in the debt collection industry and assisting consumers dealing with debts and debt collection. These are the Debt collection guideline: for collectors and creditors and, for consumers, Dealing with debt: your rights and responsibilities.  A debt collector who breaches the harassment and coercion provisions of the Commonwealth consumer protection laws risks fines of up to $220,000 for individuals or $1.1 million for a corporation. Similar fines are risked if a collector is convicted of knowingly making false or misleading representations.  Apart from criminal sanctions, ASIC or the ACCC can seek civil court orders against a collector, including injunctions against future conduct and non-punitive orders, such as corrective advertising.  Someone who has suffered loss or damage from a collector's action may be able to recover their losses in certain circumstances.  Copies of both the debt collection guidelines are available on the [ACCC website](http://www.accc.gov.au/content/index.phtml/itemId/142" \t "_new) and the [ASIC website](http://www.asic.gov.au/asic/asic.nsf" \t "_new).  **2.4 ASIC gives relief for unsolicited offers to acquire shares in a foreign company**  On 10 October 2005, the Australian Securities and Investments Commission (ASIC) granted relief from the [Corporations Act 2001](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "Default) (the Act) to those making unsolicited offers to holders of shares in a foreign company under a foreign regulated takeover bid.  ASIC Class Order [CO 05/850] gives relief from disclosure provisions of the Act that regulate the making of unsolicited offers to purchase financial products off-market: Div 5A of Part 7.9. The provisions require that unsolicited offers include the following information:   * if the financial products are quoted, the market price of the financial product; or * if the financial products are unquoted, a fair estimate of the value of the financial product as at the date of the offer and an explanation of the basis on which the estimate was made.   Offers under an Australian off-market takeover bid are exempted from the unsolicited offer requirements: paragraph 1019D(1)(d)(iv). Relief for foreign regulated takeover bids is consistent with this exemption.  Class Order [CO 05/850] applies to takeovers regulated in Canada, France, Germany, Hong Kong, Italy, Japan, Malaysia, The Netherlands, New Zealand, South Africa, Singapore, Switzerland, The United Kingdom and The United States of America.  The foreign takeover bid must involve an offer to all holders of securities in the foreign company in the same class.  ASIC may give case-by-case relief for a takeover bid regulated in another jurisdiction if the applicant satisfies it that the takeover is subject to regulation (particularly disclosure requirements) comparable to Australian regulation.  A copy of [CO 05/850] is available on the [ASIC website](http://www.asic.gov.au/asic/asic.nsf" \t "_new).  **2.5 ASIC's 2005-06 financial reporting surveillance program focuses on international accounting standards**  On 6 October 2005, the Australian Securities and Investments Commission (ASIC) announced that it would focus on the adoption of the Australian equivalents of international accounting standards (AIFRS) when conducting its financial reporting surveillance program for 2005-06.  **(a) Effects of transition**  It is important that the users of financial reports are adequately informed of the impacts of the transition to the new standards so that they can understand what changes are attributable to the underlying performance of the entity. AIFRS apply for financial years commencing on or after 1 January 2005. The first half-year and full-year financial reports under AIFRS will include relevant reconciliations of information to pre-AIFRS standards.  For half-years and full years commencing before 1 January 2005, the pre-AIFRS standards apply and AASB 1047 Disclosing the Impacts of Adopting the Australian Equivalents to International Financial Reporting Standards, requires financial reports to disclose information concerning the entity’s management of the transition to AIFRS and the key differences in accounting policies on adopting AIFRS.  ASIC outlined its views about the nature and extent of disclosures required by AASB 1047 in Information Release [IR 05-16] ASIC Guidance on disclosing the impact of AIFRS for full-year financial reports (26 April 2005). ASIC believes that, in most cases, entities have been able to quantify AIFRS impacts in their 30 June 2005 full year financial reports.  In 2004-05 ASIC reviewed over 1,400 listed entity full-year financial reports and 220 half-year financial reports for compliance with accounting standard AASB 1047. The AASB 1047 disclosures did not suggest that entities would have difficulty in meeting the timetable for the adoption of AIFRS.  **(b) Scope of surveillance**  ASIC is now in its third year of reviewing about 440 listed entity financial reports per year for compliance with all accounting standards. The reviews are part of ASIC's on-going systematic surveillance program which aims to review the financial reports of all listed entities at least once every four years.  As well as reviewing selected financial reports for the year ending 30 June 2005 for compliance with pre-AIFRS standards, ASIC will review all listed entities' financial reports for the year ending 30 June 2005 for disclosure of information required by AASB 1047.  ASIC will review financial reports for years ending 31 December 2005 to 31 March 2005 for compliance with AIFRS. Given that AIFRS will first apply to listed entity half-year financial reports, ASIC will also review selected financial reports for half years ending 30 June 2005 to 31 March 2006 for compliance with AIFRS.  ASIC will consider appropriate intervention in relation to significant non-compliance with the standards.  **2.6 ASIC clarifies impact of IFRS on dividends**  On 5 October 2005, the Australian Securities and Investments Commission (ASIC) announced its interpretation of the impact that the adoption of Australian International Financial Reporting Standards (AIFRS) will have on a company's ability to use past retained profits to pay dividends.  Under s254T of the [Corporations Act 2001](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "Default) (the Act), a company can only pay dividends out of profits. The retained profits shown in the last financial report of a company are relevant for this purpose.  Upon the adoption of AIFRS, the retained profits of some companies will change and in a number of instances, there will be material adjustments.  ASIC believes that retained profits previously reported on a pre-AIFRS basis cease to have relevance for paying dividends after the first half-year financial report of a disclosing entity, or full year financial report of a non-disclosing entity prepared under the Act using AIFRS, is completed. Only retained profits and current year profits recorded under AIFRS will be relevant from that time going forward.  The impact on each company will depend upon its particular circumstances, the level of any reduction in retained earnings, volatility of future profits and its dividend policy.  In addition to the above considerations, ASIC reminds company directors that in determining whether to pay a dividend, they must also have regard to the solvency of the company (refer s588G of the Act) and their general directors' responsibilities.  AIFRS apply for reporting periods commencing on or after 1 January 2005. For companies that are disclosing entities (including listed companies) with a 30 June 2005 balance date, this will be their financial report for the half-year ended 31 December 2005.  Under s254T of the Act, a company may be able to pay a dividend in excess of current year profit by using past retained profits. The effect of ASIC's interpretation is that the future level of past retained profits, as affected by AIFRS, will be the new level for the purposes of determining whether a company can pay dividends in future years.  **2.7 ASIC releases new version of in-use notice**  On 3 October 2005, the Australian Securities and Investments Commission (ASIC) released a new version of the FS 53 PDS in-use notice form for product disclosure statements.  Responsible persons must notify ASIC using form FS53 PDS in-use notice when a copy of the product disclosure statement (PDS) or supplementary PDS is first used. This is a requirement under the [Corporations Act 2001](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "Default).  The new in-use notice includes a second part that deals with superannuation fee data. This part deals with fee data collection for the purpose of uploading superannuation fee data onto ASIC's FIDO website.  The Government has made a public commitment to monitor and report on superannuation fees and charges for at least the first five years following the introduction of the Choice of Fund legislation. As part of this initiative ASIC has been asked to collect, and make publicly available on its consumer website [www.fido.gov.au](http://www.fido.gov.au" \t "_new), 'single fee and cost of fund' fee information that must be included in PDS's for superannuation funds. The initiative is designed to assist consumers when they are comparing funds.  ASIC is gathering this information via this notice to ensure that such information is updated.  More information is available on the [ASIC website](http://www.asic.gov.au/asic/asic.nsf" \t "_new).  **2.8 ASIC releases policy statement on external administration: liquidator registration**  On 30 September 2005, the Australian Securities and Investments Commission (ASIC) released its policy approach to the registration of suitably qualified persons as registered liquidators and official liquidators.  Policy Statement 186 - External administration: liquidator registration [PS 186] details how applications for registration as a liquidator or official liquidator should be made. It also explains the ongoing obligations of registered liquidators under the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "Default) and outlines ASIC's expectations in relation to the way in which registered liquidators perform these obligations.  Policy Statement [186] replaces ASIC's policy in Policy Statement 40 - Registration of liquidators experience criteria [PS 40] and Policy Statement 24 - Registration of official liquidators [PS 24].  The new policy statement is the outcome of consultation undertaken by ASIC in the second half of last year on the registration of liquidators and official liquidators under Part 9.2 of the Act.  Copies of the policy statement, together with the updated liquidator's registration kit, may be obtained from the [ASIC website](http://www.asic.gov.au/asic/asic.nsf" \t "_new) or by calling 1300 300 630. |
| **3. Recent ASX Developments** |
| **3.1 Listing rule amendments - effective date 24 October 2005**  Listing rule amendments came into effect on 24 October 2005. The matters the amendments relate to include:   * chairman's open proxy, * nomination of directors, * debt listings, and * other amendments dealing with technical matters and redundant provisions.   Not all listing rule amendments suggested in ASX's September 2004 Exposure Draft came into effect on 24 October 2005. Listing rules, to which amendments were proposed in the September 2004 Exposure Draft, and which are not proceeding are:   * listing rule 1.3.3(a) (working capital statement in product disclosure statements); * listing rule 3.10A (proposed deletion of requirement to tell ASX if securities being released from escrow agreement); * listing rule 10.18 (termination benefits of officers on change of shareholding or control); * listing rule 6.18 (percentage options); * listing rules 7.8 and 14.11 (recognition of trustees holding on behalf of beneficial owners). Only those amendments to listing rule 14.11 proposed in Section 11 of the Exposure Draft will not proceed. The less substantial amendments to listing rule 14.11.1 proposed in Section 13 are still intended to proceed; and * all of the amendments relating to Exchange Traded Funds which were set out in Section 12 of the Exposure Draft.   The full text of the amended rules is available on the [ASX website](http://www.asx.com.au/supervision/rules/listing/index.htm" \t "_new).  **3.2 ASX and corporate governance**  ASX Managing Director and CEO, Tony D'Aloisio, spoke at the APEC Business Advisory Council Symposium on 19 October. His speech, titled "Corporate Governance: Translating Words into Actions" is available on the [ASX website](http://www.asx.com.au/" \t "_new). |
| **4. Recent Takeovers Panel Developments** |
| **4.1 Panel release of draft guidance notes for public consultation**  On 13 October 2005, the Takeovers Panel published two Guidance Notes for public comment.  The first is a new Guidance Note which the Panel advised was a follow on from the Panel's decision in Southcorp Limited [2005] ATP 4. The draft Guidance Note addresses two issues:  (a) disclosure to the target company of the selling material which is frequently published at the front of bidder's statement (wrap information); and (b) the use in bidder's and target's statements of valuations (or price recommendations) published by stock brokers (broker valuations). The Guidance Note discusses bidders and targets using broker valuations in aggregated form where the individual brokers have not given express consent to the use of their valuation.  The second is an update of the Panel's current Guidance Note 16 'Correction of Takeovers Documents'. This Guidance Note has been revised in light of the Panel's experiences since its original publication.  The two documents are available from the [Takeovers Panel website](http://www.takeovers.gov.au/" \t "_new).  The decision of the Takeovers Panel in Southcorp Limited is available at:  [http://cclsr.law.unimelb.edu.au/judgments/states/tp/2005/march/2005atp4.htm](http://cclsr.law.unimelb.edu.au/judgments/states/tp/2005/march/2005atp4.htm" \t "_new) |
| **5. Recent Corporate Law Decisions** |
| **5.1 Challenge by the Commonwealth to a deed of company arrangement**  (By Sabrina Ng and Felicity Harrison, Corrs Chambers Westgarth)  Commonwealth of Australia, in the matter of Leahy Petroleum - Retail Pty Ltd (subject to deed of company arrangement) [2005] FCA 1422, Federal Court of Australia, Finkelstein J, 7 October 2005  The full text of this judgment is available at:  [http://cclsr.law.unimelb.edu.au/judgments/states/federal/2005/october/2005fca1422.htm](http://cclsr.law.unimelb.edu.au/judgments/states/federal/2005/october/2005fca1422.htm" \t "_new)  or  [http://cclsr.law.unimelb.edu.au/judgments/index.html](http://cclsr.law.unimelb.edu.au/judgments/index.html" \t "_new)  **(a) Summary**  The Commonwealth of Australia (the Commonwealth) applied for orders that a Deed of Company Arrangement (the Deed) entered into by Leahy Petroleum – Retail Pty LTD (Leahy Petroleum) be terminated pursuant to section 445D of the [Corporations Act 2001](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "Default) on the basis of injustice or unfair discrimination against the Commonwealth.  Leahy Petroleum had been placed into administration shortly after the Federal Court of Australia had ordered it to pay pecuniary penalties to the Commonwealth of $2.5 million upon finding it had engaged in price fixing.  The Deed provided that all the creditors be paid out, leaving a surplus of approximately $916,700, to be shared equally between the Commonwealth and Leahy Petroleum’s holding company.  The defendants argued that the Commonwealth had no standing to bring the application as a penalty or fine is not admissible as proof against an insolvent company. This argument was rejected by Finkelstein J.  After an analysis of relevant United Kingdom and Australian legislation and case law, Finkelstein J ordered that the Deed be terminated. The effect of this order was that Leahy Petroleum be subject to winding up pursuant to section 446B of the Corporations Act and regulation 5.3A.07 of the [Corporations Regulations 2001](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56758" \t "Default). The Commonwealth could expect to receive the whole of the surplus following the winding up.  **(b) Facts**  The Commonwealth held a debt of record against Leahy Petroleum – Retail Pty LTD being a judgment order of $2.5 million for a pecuniary penalty and costs order in excess of $60,000. After the order of judgment was made against Leahy Petroleum, the company was declared insolvent and administrators were appointed.  Creditors resolved that Leahy Petroleum execute the Deed that provided that all company creditors (other than the Commonwealth) be paid in full out of the company assets. The surplus, approximately $916,700, was then to be divided equally between the Commonwealth and Leahy Family Holdings Pty LTD (which was deemed a "contributory" as it owned all the issued shares in Leahy Petroleum). It should be noted that the chairman of Leahy Petroleum (who was also one of the appointed administrators) exercised a casting vote in relation to the execution of the Deed. The Commonwealth claimed that in a winding up process, it would recover the debt due to it prior to the contributories.  The grounds for termination of the Deed argued by the Commonwealth were that:   * effect cannot be given to the Deed without injustice (section 446D(1)(e)); * the Deed unfairly discriminates against the Commonwealth (section 445D(1)(f)); or * termination for some other reason (section 445D(1)(g).   **(c) Decision**  Finkelstein J first addressed the issue of the Commonwealth's alleged lack of standing pursuant to section 553B of the Corporations Act. The defendants argued that the Commonwealth had no standing because a penalty or fine is not admissible to proof against an insolvent company, and as such the Commonwealth was not a creditor. Justice Finkelstein noted that section 553B relates to the proof and ranking of claims in a winding up of a company, and not claims where a company has been placed in administration. He rejected case law submitted by the defendants that had been applied to instances of administration on the basis that in those particular cases section 55B had been incorporated as a term of the deed of company arrangement, which it was not in this case.  Justice Finkelstein then addressed the Commonwealth's argument that it would receive its payment of debts due prior to contributories under a winding up process. Justice Finkelstein determined that, in relation to section 553B, if a company being wound up is insolvent when it is placed into liquidation, fines and penalties cannot be admitted as proof. However, if all provable claims are paid in full and, for one reason or another, there is still a surplus, the company is no longer insolvent and the surplus can be applied to the discharge of fines and penalties. He supported this by reference to English case law, Australian case law and parliamentary intention in relation to section 553B.  Justice Finkelstein ordered that the Deed be terminated on the following two grounds:   * the Commonwealth was unfairly prejudiced by the Deed because if the Deed were given effect, the Commonwealth would receive only half of the amount that it would receive if the company was wound up; and * the Chairman executed his vote on a mistaken view of the law.   **5.2 Does a purchaser obtain any equitable rights under a purported assignment of shares in breach of a preemption provision?**  (By Katherine Scutella, Freehills)  Rathner v Lindholm [2005] VSC 399, Supreme Court of Victoria, Whelan J, 6 October 2005  The full text of this judgment is available at:  [http://cclsr.law.unimelb.edu.au/judgments/states/vic/2005/october/2005vsc399.htm](http://cclsr.law.unimelb.edu.au/judgments/states/vic/2005/october/2005vsc399.htm" \t "_new)  or  [http://cclsr.law.unimelb.edu.au/judgments/index.html](http://cclsr.law.unimelb.edu.au/judgments/index.html" \t "_new)  **(a) Summary**  A sale and transfer of shares in contravention of preemption provisions in a company's constitution is not a complete nullity. The purchaser under such a sale and transfer has no rights as against the company, but does have equitable proprietary rights which bind the vendor of the shares. Where the shareholders, other than the vendor, wish to enforce the rights of preemption as against the purchaser, the equitable rights of the other shareholders will almost inevitably prevail.  **(b) Facts**  This case forms part of a wider dispute involving a complex series of transactions and claims, between a number of persons, including the parties in this case. It concerns a company named ACTA, and in particular, shares owned by ACTA in a company named AEPL.  ACTA granted a company named Global a debenture charge over all its assets, including the shares in AEPL. Subsequently, the plaintiff was appointed deed administrator of ACTA. A dispute arose under the deed of company arrangement (DOCA) between the plaintiff and Global. As part of the settlement of the dispute, Global, in its capacity as mortgagee in possession of the AEPL shares, purported to assign those shares to the plaintiff.  Global then appointed receivers and managers (the first and second defendants) to ACTA. The receivers entered into an agreement with all the other defendants, which included shareholders of AEPL, purporting to deal with ACTA’s shares in AEPL.  The question in this case was what rights did the plaintiff have to ACTA's shares in AEPL.  Significantly, AEPL's constitution and shareholders' agreement contained preemption provisions that prohibited a transfer of shares unless the rights of preemption in favour of the other shareholders of AEPL had first been exhausted. The defendants therefore contended that the purported transfer was void as being in contravention of the constitution of AEPL. The defendants also alleged that the plaintiff did not have the power to bring proceedings to enforce the DOCA.  The plaintiff contended that the settlement deed merely changed control of, rather than assigned, the AEPL shares and thus created a trust over the equitable interest in those shares in favour of the plaintiff in his capacity as deed administrator.  **(c) Decision**  **(i) Does a deed administrator have the power to take proceedings to enforce a deed of company arrangement?**  Whelan J dealt with this issue briefly, concluding that the plaintiff, as deed administrator, was empowered to take proceedings to enforce the provisions of the DOCA and, further, was empowered to compromise such proceedings.  **(ii) Did the settlement deed provide for share assignment or merely a change in control?**  The settlement deed was expressed as an agreement to "assign" the AEPL shares to the plaintiff, and went on to refer to the plaintiff as the "owner" of such shares. Therefore, Whelan J inferred that the intention of the parties was to assign the entire legal and equitable interest in ACTA's shares in AEPL to the plaintiff. Thus the purported assignment contravened the preemption provisions in AEPL's constitution and shareholders' agreement.  **(iii) Does a purchaser of shares obtain any equitable rights when there is a purported share assignment in breach of preemption provisions?**  Whelan J undertook a comprehensive review of the authorities from which he drew the following applicable principles:  1. A transfer of shares in contravention of preemption provisions would not be a complete nullity. 2. The purchaser has no rights as against the company. 3. The purchaser does have equitable proprietary rights that bind the vendor of the shares. If the vendor receives a higher purchase price as a result of compliance with the preemption provisions, or receives dividends, or the proceeds of a capital reduction, then it is liable to account to the purchaser. 4. In so far as conflict arises between shareholders other than the vendor wishing to enforce the rights of preemption and the purchaser, the equitable rights of the other shareholders will almost inevitably prevail. Shareholders entitled to the benefit of preemption provisions can restrain registration of a transfer which contravenes those provisions and can have the register rectified if such a transfer is registered.  Therefore, the plaintiff was held to have an equitable proprietary interest in ACTA's shares in AEPL as a result of the assignment from Global – it was not a complete nullity simply because the assignment was in contravention of the pre-emptive provisions in the constitution and shareholders' agreement of AEPL. No relief was granted, however, as further issues, which had been deferred, were now required to be determined.  **5.3 When can the court grant leave to enforce a charge which would otherwise be unenforceable under section 267(1)?**  (By Justin Fox and Fiona Rosen, Corrs Chambers Westgarth)  Exception Holdings Pty LTD v Albarran (No 2) [2005] NSWSC 981, New South Wales Supreme Court, Young CJ in Equity, 29 September 2005  The full text of this judgment is available at:  [http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/september/2005nswsc981.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/september/2005nswsc981.htm" \t "_new)  or  [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)  **(a) Summary**  This was an application under section 267(3) of the [Corporations Act 2001 (Cth)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "Default) ("the Act") seeking leave to enforce a charge over the assets of a company. The charge had previously been held to be void under section 267(1) of the Act, on the grounds that it was given in favour of a "relevant person", within the meaning of section 267(1) and the chargee took steps to enforce the charge within 6 months after it was created. The court dismissed the application on the grounds that retrospective leave could not be given after the chargee had taken steps to enforce the charge. The court concluded that its power to validate enforcement action under section 267(3) ceased once the chargee had taken steps to enforce the charge without leave of the court, and that the charge could not subsequently be revived.  **(b) Facts**  Highland, Labraga and Pomfret were associated in a business. The corporate vehicle used for their enterprise was the plaintiff company, Exception Holdings Pty LTD ("Exception") in which each had a one third interest. Highland's interests in Exception were held through Nowhere in Particular Pty LTD ("Nowhere").  In 2004, each of Nowhere and Labraga advanced loans to Exception, which Exception used to make payments to its bankers. The loan from Nowhere was secured by a charge over the assets of Exception, the terms of which entitled Nowhere to appoint a receiver upon an event of default. Exception was subsequently wound up. Albarran was appointed as receiver under the Nowhere charge.  The liquidator of Exception brought an action (the "Initial Proceedings") seeking a declaration that the charge was invalid under section 267(1).  **(c) The initial proceedings**  Section 267(1) of the Act relevantly provides that:  "Where:  (a) a company creates a charge… in favour of a… relevant person in relation to the charge; and (b) within 6 months after the creation of the charge, the chargee purports to take a step in the enforcement of the charge, without the Court having, under subsection (3), given leave for the charge to be enforced;   the charge, and any powers purported to be conferred by… the charge are, and are taken always to have been, void".  Young CJ found, based on the specific fact circumstances of the Initial Proceedings, that the charge was invalidated by section 267(1) of the Act. In giving his reasons in the Initial Proceedings, Young CJ noted, however, that there is an escape in section 267(3), that if the chargee can satisfy the Court that immediately after the creation of the charge the company that created the charge was solvent and it is just and equitable for the Court to grant leave to enforce the charge, it may do so. Young CJ allowed time for an application to be made under section 267(3), which was heard on 18 July 2005.  **(d) Decision**  Young CJ refused to grant leave to enforce the charge on the basis that section 267(3) does not permit leave to be granted once enforcement action has been taken. He accepted the argument advanced by Exception's liquidator that section 267(1) fixes on the chargee purporting to take an enforcement step without the court having given leave under subsection (3). Once that act has occurred, the charge has been vitiated and there is no room for the court to give leave subsequently.  Young CJ concluded that the words in section 267(1)(b) mean what they say, namely that if a chargee takes the step of enforcing the charge and at that time has not got the leave of the court to do so, then the charge is vitiated for all purposes and cannot thereafter be revived by an application under section 267(3).  Young CJ also considered whether the court had power under section 1322(4) of the Act to grant retrospective leave validating the charge. Section 1322(4) gives the court broad discretion to extend time frames imposed by the Act or to declare that an action is not invalid by reason of a contravention of the Act, where certain circumstances exist.  Young CJ agreed with the comments made by Ryan J in Re The 21st Century Sign Company Pty LTD [1994] 1 Qd R 93 that in determining whether section 1322(4) would authorise the court to give retrospective leave, it was necessary to consider whether the legislative scheme excluded the operation of section 1322(4). Young CJ quoted with approval the comments of Ryan J that the object of section 267(3) was to ensure that the court will examine the circumstances in which a charge is created to ensure that other creditors are not prejudiced by enforcement of the charge and that it would be inconsistent with that object to give an operation to section 1322(4) which would have the effect that an order could be made validating the taking of a step to enforce a charge without the leave of the court having first been obtained.  Therefore, Young CJ held that it was of no value to look at section 1322(4) and 1322(6), and retrospective leave was not given.  **5.4 Enforceability of a fixed charge over a mortgage book and mistrust between directors as grounds for winding up**  (By Peter Hulbert, Blake Dawson Waldron)  Labraga v Pomfret; Highland v Labraga [2005] NSWSC 973, New South Wales Supreme Court, Equity Division, Young CJ in Equity, 29 September 2005  The full text of this judgment is available at:  [http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/September/2005nswsc973.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/september/2005nswsc973.htm" \t "_new)  or  [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)  **(a) Summary**  This case involved two proceedings arising out of problems within the Exception Holdings Pty LTD (Holdings) group of companies. In the Company Proceedings the plaintiff sought an order that Holdings be wound up and a declaration that the defendants had agreed to grant the plaintiff a first ranking fixed charge over the mortgage book owned by Exception Finance Pty LTD (Finance).  Young CJ found that the plaintiff was not entitled to an equitable charge over the mortgage book because the book was by nature a constantly changing bundle of choses in action, and therefore not capable of being the subject of a fixed charge. Young CJ ordered that the defendant company be wound up because it was just and equitable to do so on the basis that the directors had lost all trust and confidence in each other.  In the Estate Proceedings the wife of a deceased one-third owner of the group obtained an order that the grant of probate to the two surviving owners be revoked in her favour on the grounds that the two executors had lost all trust and confidence in each other.  **(b) Facts**  The businesses of the various group members were disparate due to the diverse backgrounds of the 3 owners, Richard Highland, Julio Labraga and Philip Pomfret. The three men each held equal equity interests in each of the group companies. The companies had slipped into insolvency or financial distress during the period around Mr Highland's death in March 2003. At around the same time Holdings' overdraft account with the Westpac Banking Corporation (Westpac) exceeded $1.5 million.  Each of the men had lent money to the group in the past on an unsecured basis. As probate of Mr Highland's estate had been granted to Mr Labraga and Mr Pomfret, the two men agreed that the Estate would contribute $890,000 towards the Westpac debt and Mr Labraga made available $400,000 which he borrowed at interest from another source.  Mr Labraga and Mr Pomfret volunteered different accounts of their discussions about the loan from Mr Labraga to the group. Mr Labraga asserted that Mr Pomfret and the company had agreed to provide security over the mortgage book owned by Finance in the form of a "fixed and floating charge". The charge was said to have been fixed over the mortgage book and floating over the other assets of Finance. The mortgage book was a bundle of choses in action, each of which was a right to obtain an income stream (commission) in return for directing business to certain mortgage houses. Mr Pomfret on the other hand asserted that there had been no such agreement, as evidenced by a complete lack of any documents to that effect. Mr Pomfret also argued that none of the men had ever received security for previous loans, and to do so in such dire circumstances would have been illogical.  Over the next few months the relationship between the two men further disintegrated with Mr Labraga threatening to leave the business. In fact, he took what he described as "extended leave", which Mr Pomfret took as his resignation. Mistrust and suspicion abounded, and Mr Pomfret had the security door combination changed. The company also stopped paying Mr Labraga's expenses and drawings. During this time Mr Labraga repeatedly requested that the company execute his charge over the mortgage book. At the hearing, Mr Labraga gave evidence that he had requested the company solicitor draw up the security documents, but the solicitor swore he had never received such instructions.  **(c) Decision**  **(i) The company proceedings**  Young CJ laboured over whose account of the facts should be believed. Although his Honour did not have much faith in either story, he preferred that of Mr Pomfret. Accordingly, Young CJ found that there was not an enforceable agreement between Mr Labraga and the company to charge the mortgage book in his favour. However, Young CJ went on to consider whether, had there been such an agreement, a fixed charge over the mortgage book would have been enforceable.  Firstly, there is no requirement that a charge over a chose in action be in writing; see National Provincial & Union Bank of England v Charnley [1924] 1 KB 431 at 440. Also, a charge over a mortgage book usually takes the form of an equitable assignment of the choses in action; see Rodick v Gandell (1852) 1 De GM & G 763 at 777-8; 42 ER 749 at 754. It was said by White J in Jackson v Richards [2005] NSWSC 630 at [19]-[21] that in such cases it is necessary that the fund (the mortgage book) be kept separate from the other assets of the debtor. Counsel for Mr Pomfret argued that in this case there was no certainty as to the asset because the mortgage book would by its very nature change all the time in the course of the business.  Young CJ contrasted the facts with the analogy put forward by counsel for Mr Pomfret, being a legal mortgage over any land then and thereafter held by a guarantor, which was said to be enforceable; see Bridge Wholesale Acceptance Corporation (Australia) LTD v Burnard (1992) 27 NSWLR 415. Young CJ distinguished the cases in the following terms (at 77),  "..there is a world of distinction between a charge which is to be in respect of particular pieces of property plus any further property that is to be acquired, and a charge which is over a piece of property generally described and the content of which is fluctuating."  Young CJ determined that a mortgage book is not a fixed asset, describing it as a "moving pond". Rights to receive commission fluctuate constantly as new mortgages are added and old mortgages are paid out. It is of the essence of an assignment that the control of adding or subtracting from the property is denied to the assignor. Accordingly, there could not be a fixed charge over a volatile asset such as a mortgage book.  Young CJ went on to consider whether, had there been an enforceable charge, which there wasn't, equity would grant specific performance. His Honour decided that equity would not grant specific performance because of the great uncertainty over the terms of the alleged agreement.  On the winding up application, Mr Labraga argued that Holdings should be wound up on alternative grounds, first that it was just and equitable, and secondly, that it should be wound up in insolvency.  Young CJ found that it was just and equitable to wind up Holdings. His Honour said that in a small proprietary company where the key shareholders and/or directors are persons who repose trust and confidence in each other rather like the trust and confidence that is imposed in each other by partners, if the Court can see that the relationship has broken down and that the trust and confidence no longer exists, it is often appropriate to wind the company up (at 93); see Ebrahimi v Westbourne Galleries LTD [1973] AC 360 especially at 379 and Thomas v Mackay Investments Pty LTD (1996) 22 ACSR 294 at 300-1.  Young CJ found that irreparable damage had been done to the relationship between Mr Labraga and Mr Pomfret and that both men had behaved in a most un-cooperative fashion towards each other and the conduct of the business. Indeed since the death of Mr Highland each man had done little but maneuver to obtain an advantage against the other.  **(ii) The estate proceedings**  His Honour found that for the same reasons discussed in the winding up application, the two executors had shown that they could not get on together and had reached a stage where each had disagreed with almost everything the other had done.  His Honour discussed the position that where a person appoints his business partner executor, then the testator has consented to any conflict of duty and interest that must invariably arise (at 113); see Hordern v Hordern [1910] AC 465 at 475. However, as Lord Cairns said in Vyse v Foster (1874) LR 7 HL 318 at 332, courts would nonetheless watch the conduct of an executor as surviving partner rather narrowly.  The question of fact that must be answered is whether the due and proper administration of the estate has been put in jeopardy or has been prevented by acts or omissions of the executor or by matters personal to the executor; see Mavrideros v Mack (1998) 45 NSWLR 80. His Honour found that this was a borderline case, but that in any event Mr Labraga had lost all enthusiasm for administering an estate for which he received no thanks, and that Mr Pomfret was quite happy for Mrs Highland to administer the estate. Accordingly, Young CJ made orders revoking the grant of probate to Mr Labraga and Mr Pomfret and ordered that probate of Mr Highland's will be granted instead to Mrs Highland. His Honour found that the problems had arisen equally because Mr Highland had made his business partners joint executors and because of the internecine squabbles between them. Accordingly, no order as to costs was made.  **5.5 Termination of deeds of company arrangement and use of section 447A**  (By Mark Burger, Phillips Fox)  In the matter of Centaur Mining & Exploration LTD (in Liq) (Receivers and Managers Appointed) and Centaur Nickel Pty LTD (in Liq) (Receivers and Managers Appointed), Robyn Beverley McKern and Stephen Andrew Hawke (as liquidators of Centaur Mining & Exploration LTD and Centaur Nickel Pty LTD) v Roche Mining Pty LTD [2005] VSC 367, Victorian Supreme Court, Mandie J, 20 September 2005  The full text of this judgment is available at:  [http://cclsr.law.unimelb.edu.au/judgments/states/vic/2005/september/2005vsc367.htm](http://cclsr.law.unimelb.edu.au/judgments/states/vic/2005/september/2005vsc367.htm" \t "_new)  or  [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)  **(a) Summary**  This case concerned two companies, Centaur Mining and Exploration Limited, and Centaur Nickel Pty LTD (the Companies) both subject to a deed of company arrangement. The issue was whether the deeds of company arrangement had been effectively terminated and the Companies placed into liquidation.  The plaintiffs were the deed administrators/liquidators. They sought a declaration that the companies had commenced to be wound-up on 2 August 2002 or, if they had not commenced winding up at this time, seeking appropriate orders pursuant to section 447A of the [Corporations Act 2001 (Cth)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "Default) (Act). In essence the plaintiffs claimed that Part 5.3A of the Act should operate in relation to the Companies as if the deeds of company arrangement provided for their winding-up upon termination of the deeds on 2 August 2002. The defendant in this case was an unsecured creditor of Centaur Mining & Exploration LTD who would be likely to be subject to a preference claim if the liquidations were found to have commenced or deemed to have commenced on 2 August 2002.  **(b) Facts**  On 14 March 2001 the Companies appointed administrators pursuant to section 436A of the then Corporations Law. On 2 August 2001, the Companies executed deeds of company arrangement which provided for a moratorium on creditors claims during a 3 month "arrangement period" commencing on the 2 August 2001.  Clause 6.2 of the deeds empowered the administrators to extend the arrangement period for no more that 3 months if they were of the opinion that the purposes of the deed could be achieved within such extended period. The deeds of company arrangement made express provision for the termination of the deeds. Clause 6.1 provided that the deed would terminate upon the earlier of the happening of the number of events as follows:  "(a) The deed administrators determining that the purposes of the deed could not be achieved and the majority of creditors resolving to terminate the deed and that the Companies be wound up; or (b) The termination date or extended termination date being reached and the majority of creditors resolving as in (a); or (c) The termination date or extended termination date being reached and the majority of creditors resolving to accept a settlement with directors or others, or some other relevant scheme, as proposed by the administrators; or (d) A court terminating the deeds pursuant to s.445D of the Corporations Law; or (e) Certain defined payments being made during the arrangement period."  At a meeting of creditors on 31 January 2002 it was resolved to vary the deeds of arrangement extending the termination by a further period of 3 months to 2 May 2002 with an option for the deed administrators to extend the period by a further period of 3 months at their discretion. A further resolution was carried in the following terms:  "that the Deed of Company Arrangement be further varied to provide that the Deed Administrators, with the approval of the Committee of Inspection have the discretion to terminate the Deed at which time the Company will be wound up and the Deed Administrators will act as the liquidators."  At a meeting of creditors on 16 July 2002 the deed administrators advised the creditors that "the Deed will expire on 2 August 2002 and the Company will then automatically be placed into liquidation". The court held this advice ignored the requirement of clause 6.1(a) and (b) of the deeds which required a resolution of the majority of creditors to terminate the deeds and further ignored the requirements of the deeds, as varied on 31 January 2002, that the committee of creditors approved any termination of deeds by the deed administrators.  The deed administrators filed notices with ASIC on 5 August 2002 notifying that a special resolution for the winding up of the Companies was taken to have been passed in that "circumstances existed, which under the terms of the deed of company arrangement executed by the company, result in the termination of the deed and the winding-up of the company".  Since 2 August 2002, the deed administrators acted as if they were liquidators of the companies being wound up under a creditors’ voluntary liquidations.  **(c) Decision**  **(i) Valid termination of the deeds**  Justice Mandie held that the conduct of the deed administrators could not be objectively characterized as amounting to an exercise of their expressed power or discretion under the deeds to terminate them, and that even if the conduct of the deed administrators was characterized as amounting to an exercise of their power or discretion to terminate the deeds, it is clear that the committee of creditors was not asked to approve any such decision. His Honour found that the mere acquiescence of the committee of creditors could not be considered or treated as amounting to "approval" within the meaning of the variations to the deeds. On this basis his Honour formed the view that the plaintiffs failed to establish that the companies had commenced to be wound-up on 2 August 2002.  **(ii) Winding up pursuant to section 447A**  The plaintiffs submitted in the alternative that the court had the power to make, and the court should make, an order varying the terms of the deeds of company arrangement so that they should terminate on 2 August 2002 and therefore the companies would have been placed in liquidation on that date.  Justice Mandie held that there was a strong case for the relief sought by the plaintiffs being granted as:   * The companies had no assets and were insolvent as at 2 August 2002. * By 2 August 2002, the purposes of the deeds of company arrangement had wholly failed and their continuation was futile. * It was unlikely that the creditors would have extended the deeds of company arrangements further. * It was inconceivable that the companies should be returned to the control of their directors.   Hence, there was no alternative but to place the companies into liquidation. The latest date that this would have happened, would have been 2 August 2002. The court stated "no other sensible course was available."  Justice Mandie relied upon the decision of the High Court in Australasian Memory Pty LTD v Brien (2000) CLR 270 (Australasian Memory) where the High Court held that section 447A of the Act allowed an order to be made that "altered the timing requirement of section 439A(2) of the Act" so as to validate the intended consequences of an invalid meeting of creditors.  Justice Mandie was of the view that it was just, convenient and in the interests of unsecured creditors that the relief sought by the plaintiffs be granted. In granting the relief pursuant to section 447A of the Act, Justice Mandie held that this was appropriate despite the termination of the deeds of company arrangement still being available to the creditors. This was due to the retrospective application that an order by the court under section 447A of the Act would have.  The court held that an order be made pursuant to section 447A. This order varied the deeds of company arrangement such that the deeds were automatically terminated on 2 August 2002 and the winding-up of the Companies commenced on that date.  **5.6 Limitations on the implied duty of good faith in commercial contracts**  (By Beth Midgley, Blake Dawson Waldron)  Esso Australia Resources Pty LTD v Southern Pacific Petroleum NL [2005] VSCA 228, Supreme Court of Victoria Court of Appeal, Warren CJ, Buchanan JA and Osborn AJA, 15 September 2005  The full text of this judgment is available at:  [http://cclsr.law.unimelb.edu.au/judgments/states/vic/2005/september/2005vsca228.htm](http://cclsr.law.unimelb.edu.au/judgments/states/vic/2005/september/2005vsca228.htm" \t "_new)  or  [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)  **(a) Summary**  In Esso Australia Resources Pty LTD v Southern Pacific Petroleum NL (Esso v SPP), the court examined whether a duty of good faith could be implied into a clause in a joint venture agreement pertaining to the assignment of a joint venture participant's interests.  Buchanan JA (Warren CJ and Osborn AJA concurring) found that the duty of good faith could not be implied in the circumstances. The case provides some clarification about the circumstances in which a duty of good faith will be implied into the terms of a contract. In obiter, Warren CJ suggested that the implied duty of good faith may not have a place in contracts between "commercial leviathans".  **(b) Facts**  Esso v SPP arose in the context of a joint venture agreement entered into in 1985 by Esso, Southern Pacific Petroleum NL (SPP) and Central Pacific Minerals (CPM). In 2002, CPM became a subsidiary of SPP. In 2004, SPM and CPM went into administration.  Article 24.01 of the joint venture agreement provided as follows:  (a) Each participant shall have the right to assign all or part of its Interest to a Related Corporation without the consent of the other Participant, subject only to the Related Corporation's assumption of the assignor's obligations under the various agreements relating to the Joint Venture and the assignor guaranteeing the performance of the Related Corporation. Such a guarantee will not cease merely because the assignee ceases to be a Related Corporation. (b) Subject to this Article each Participant may with the prior written consent of the other, which shall not be unreasonably withheld, assign all or part of its Interests to a third party…  SPP and SPV were Related Corporations under the definition set out in the joint venture agreement. The companies' administrators drafted 2 deeds of company arrangement providing for the disposal of the companies' interests in the joint venture. The first deed provided for the purchase of SPP's shares in CPM by Queensland Energy Resources Ltd. The second deed provided for the assignment of SPP's interest in the joint venture to a company called SPV. The second deed also provided for SPP to be liquidated after creditors had been paid their entitlements. This would leave Esso without a guarantee of SPV's performance under article 24.01(a) of the joint venture agreement.  Esso brought proceedings to seek to restrain SPP and the administrators from assigning SPP's interests in the joint venture to SPV. Esso was unsuccessful at first instance. On appeal, Esso raised the following arguments:   * that the proposed assignment constituted a breach of article 27 of the joint venture agreement, which related to conflict of interest and required joint venture participants to use best endeavours to work in the best interests of the other participants in respect of the joint venture; and * that SPP was in breach of an implied obligation of good faith as a consequence of the provision in the draft deed of company arrangement stating that SPP would be wound up.   Justice Buchanan also discussed an argument put by Esso at trial but not pursued on appeal to the effect that:   * the proposed assignment to SPV under article 24.01(a) constituted a breach of an implied obligation of good faith.   **(c) Decision**  Buchanan JA delivered the leading judgment (Warren CJ and Osborn AJA concurring, and Warren CJ making some supplementary comments in relation to the duty to act in good faith). The court's findings in relation to each of the arguments put by Esso are set out below:   * Esso's argument in relation to article 27 of the joint venture agreement was dismissed. Buchanan JA noted that the clause could not have been intended to impose a "fiduciary like" obligation on the participants to the joint venture to act in the best interests of other participants. * In relation to the second argument, Buchanan JA declined to draw any conclusion as to whether a duty of good faith was implied into article 24 noting that, even if such a duty did exist, it had not been breached. He found that the deed of company arrangement was not "unreasonable or capricious" and did not deny Esso any of its benefits. Furthermore, the arrangement was entered into in the interest of the creditors of SPP. To conclude that a duty of good faith had been breached by the creation of the deed of company arrangement would have been to place the interests of Esso above those of the creditors. His Honour stated that the duty of good faith "is not a duty to prefer the interests of the other contracting party". * Although not required to do so, Buchanan JA also commented on whether the deed of company arrangement could amount to a breach of the duty of good faith in article 24.01(a) of the agreement. He said that article 24.01(a) conferred on the parties a power which would serve in their own interests and that:   "if a contractual right or power, which is intended to advance only the interests of the party on whom it is conferred, is fettered by an implied obligation of good faith, resort to the duty may become an obstacle to the promotion of that party's legitimate interests".  His Honour contrasted article 24.01 of the agreement with a clause in a contract which concerns cooperation to produce a result beneficial to all parties. His Honour noted that a duty of good faith would be more likely to be implied into the latter clause.  **(d) Conclusion: some limitations on implied good faith**  The decision in Esso v SPP indicates that a duty of good faith does not attach to the exercise of every right and power conferred by a contract. Good faith obligations may be breached where a party acts unreasonably or "capriciously" or for an ulterior purpose. However, the duty of good faith to a contracting party will not override a party's primary interest to its creditors. Nor is good faith likely to be implied into a clause that confers power on a party to act in its own interests.  Warren CJ made some additional comments about the duty of good faith. Her Honour noted that, in the interests of certainty, a contract should only be interfered with when there is a power imbalance between the parties and one party is particularly disadvantaged or vulnerable.  In her Honour's view,  "[w]here commercial leviathans are contractually engaged, it is difficult to see that a duty of good faith will arise, leaving aside duties that might arise in a fiduciary relationship".  Esso v SPP, then, suggests that there are significant limitations on the scope for a duty of good faith to be implied into commercial contracts - particularly into contracts between commercially savvy parties.  **5.7 Shareholders as creditors**  (By Farayi Chipungu, Mallesons Stephen Jaques)  Sons of Gwalia LTD (Administrator Appointed) v Margaretic [2005] FCA 1305, Federal Court of Australia, Emmett J, 15 September 2005  The full text of the judgment is available at:  [http://cclsr.law.unimelb.edu.au/judgments/states/federal/2005/september/2005%20fca%201305.htm](http://cclsr.law.unimelb.edu.au/judgments/states/federal/2005/september/2005%20fca%201305.htm" \t "_new)  or  [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)  The decision deals with the circumstances in which a shareholder will be treated as a creditor of a company that is in administration. Ordinarily section 563A of the [Corporations Act 2001 (Cth)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "Default) ("the Corporations Act") requires the claims of shareholders to be postponed until all debts of the company are paid. However, this decision means that in certain circumstances shareholders' claims will be elevated to rank equally with those of unsecured creditors.  **(a) Background**  On 18 August 2004, Mr Margaretic paid just over $26,000 for shares in the capital of Sons of Gwalia LTD ("the Company"). Some 11 days later, on 29 August, voluntary administrators were appointed to the Company under Part 5.3A of the Corporations Act. At that stage the shares in the Company were worthless.  Subsequently, the administrators proposed that the company and its creditors enter into a deed of company arrangement. The proposed deed included provisions based on section 563A of the Corporations Act which states that in the context of a winding up, debts owed to a person in their capacity as a member of the company (e.g. for dividends, profits or otherwise) are to be postponed until all debts owed to, or claims made by, persons other than as members have been satisfied. The purpose of the section is to protect the interests of creditors by preventing shareholders from indirectly reducing a company’s available assets.  **(b) The issues**  Mr Margaretic alleged that at the time of his purchase, the Company had information which it was required to disclose to the Australian Stock Exchange ("ASX") under the continuous disclosure requirements in section 674 of the Corporations Act and under ASX Listing Rule 3.1. The purpose of the disclosure requirements is for companies to keep the ASX and market participants informed of any matters that may have a material effect on the price or value of securities.  In this case, the relevant information was that the Company's gold reserves were insufficient to meet its gold delivery commitments to the extent that there was a very high risk that the Company would have to be wound up. The information had not been disclosed.  Consequently, Mr Margaretic argued that this failure to disclose meant that the Company had engaged in misleading and deceptive conduct in breach of various consumer protection provisions in the law, causing him to suffer loss and damage for which the Company should compensate him. This was the source of Mr Margaretic’s claim that he was a creditor of the Company.  The administrators of the Company and another creditor ING Holdings LLC (whose creditor status was not in dispute), brought an action in the Federal Court seeking:   * a declaration that Mr Margaretic's claim would not be provable under the deed of company arrangement; or alternatively * a declaration that the effect of section 563A was that the payment of his claim under the proposed deed of company arrangement would be postponed until all debts owed to, or claims made by, persons otherwise than in their capacity as members of the company, have been satisfied.   Mr Margaretic filed a cross-claim seeking a declaration that he was a creditor of the Company (by virtue of his claim, if proven, for damages) and that he was entitled to be treated as a creditor under Part 5.3A in connection with any meetings convened to consider the proposed deed of company arrangement.  Note that in these proceedings, the court was concerned solely with questions relating to Mr Margaretic's status and did not make determinations with regard to whether the requirements of the disclosure and misleading and deceptive conduct provisions mentioned had been contravened.  **(c) The decision**  **(i) The section 563A issue**  In considering whether Mr Margaretic's claim was a debt owed to him in his capacity as a member of the Company and therefore liable to be postponed, Justice Emmett examined a series of decisions relating the priority of shareholder claims in insolvency. In particular, his Honour considered the decision of Webb Distributors (Aust) Pty LTD v State of Victoria (1993) 179 CLR 15 where the High Court determined that a shareholder could not claim damages against a building society as a consequence of breach of a subscription contract between the shareholder and the society. In that case, the Court found that the shareholder was precluded from rescinding their subscription contract and thus from claiming as a creditor and that their claim for damages for misleading conduct under the [Trade Practices Act 1974 (Cth)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=6426" \t "Default) should be postponed under the then equivalent of section 563A since it related directly to the subscriber’s membership of the society.  Justice Emmett found that the facts of that case were distinguishable from the present case. In Webb, the subscriber shareholder had attained their holding through a subscription agreement with the company, whereas in the present case, Mr Margaretic had acquired his shares from a third party in a transaction that had no connection whatsoever with the company. In these circumstances, Justice Emmett concluded that if Mr Margaretic's claim was a debt at all, then it was a debt arising as a result of the operation of the consumer protection provisions mentioned above and was not a debt owed to him in his capacity as a member of the Company. Mr Margaretic was therefore a creditor of the Company and section 563A did not require postponement of his claim.  **(ii) Creditor rights**  In the event that his conclusion on the section 563A issue was wrong, Justice Emmett went on to consider whether there would be any restrictions on Mr Margaretic exercising rights as a creditor of the Company under the proposed deed of company arrangement even though his claim might be postponed.  Here, the Court held that even if Mr Margaretic's claim was postponed by the operation of section 563A, it was still a debt or claim provable in the winding up of the Company and he was therefore entitled to exercise his rights as a creditor under the proposed deed of company arrangement such as the rights to attend and vote at meetings of creditors and to receive information and circulars sent by the Company to its creditors.  **(d) Conclusion**  This decision extends the rights of transferee shareholders where the company in which they invest engages in misleading conduct and may have a significant impact on insolvency law. The decision has been appealed to the Full Federal Court.  There is further discussion of this decision in Corporate Law Bulletin No 97 (September 2005).  **5.8 Houldsworth rule stands against section 729**  (By Porscia Lam, Mallesons Stephen Jaques)  Cadence Asset Management Pty LTD v Concept Sports Limited [2005] FCA 1280, Federal Court of Australia, Finkelstein J, 14 September 2005  The full text of this judgment is available at:  [http://cclsr.law.unimelb.edu.au/judgments/states/federal/2005/september/2005fca1280.htm](http://cclsr.law.unimelb.edu.au/judgments/states/federal/2005/september/2005fca1280.htm" \t "_new)  or  [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)  **(a) Summary**  A former shareholder alleged that it subscribed for shares in a company in reliance upon the prospectus of the company which did not contain all the information required by section 710 of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "Default), which contained misleading and deceptive statements, and which contained false implied representations as to the accuracy and full disclosure of material information. The former shareholder did not rescind the subscription contract but sold the shares at a loss and then commenced proceedings seeking damages.  This judgment was a determination on an interlocutory application to resolve a point of law arising from the pleadings. The issue was whether a shareholder is precluded from claiming damages under section 729 where the subscription contract has not first been rescinded. Finkelstein J ruled that a shareholder is so precluded.  **(b) Facts**  Concept Sports Limited ("Concept") issued a prospectus offering ordinary shares.  Cadence Asset Management Pty LTD ("Cadence") claimed that in reliance upon the prospectus it subscribed for shares in Concept. It then sold its shares in Concept at a loss to a third party and commenced these proceedings seeking damages for the difference between the subscription price and the proceeds of sale.  Cadence alleged that:   * the prospectus did not contain all the information required by section 710 of the Corporations Act; * the financial information and statements in relation to Concept's business outlook were misleading and deceptive; and * false implied representations had been made that all material information had been disclosed and investigations had been taken to ensure the accuracy of the information.   The pleadings raised the question of whether the rule in Houldsworth v City of Glasgow Bank (1880) 5 App Cas 317 ("Houldsworth") that a shareholder cannot sue for damages for fraud or misrepresentation inducing subscription for shares, unless the contract is first rescinded, has been displaced by section 729 of the Corporations Act which allows any person who suffers loss or damage as a result of a contravention of section 728 to recover damages. Section 728 provides that a prospectus must not omit certain information required by section 710 or contain misleading or deceptive statements. The parties sought to have this point disposed of prior to trial.  **(c) Decision**  **(i) Rationale behind Houldsworth**  Houldsworth is founded upon the principle that to allow a shareholder, who has elected not to rescind the share subscription contract, to claim damages for misrepresentations by the company in relation to those shares, would conflict with the implied term of the contract of membership between the company and its shareholders that the capital of the company should be applied only in payment of the debts and liabilities of that company.  Houldsworth concerned an insolvent company. It is not necessary to repeat Finkelstein J's summary of the law that was applicable at the time of Houldsworth save to note that his Honour considered that the modern statutory equivalent to the law as it stood at that time is section 563A which prevents a member from claiming a debt until all debts owed to creditors have been satisfied. In his Honour's view, the order of priority of creditors before shareholders to the assets of a company in a winding up before a subscription contract has been rescinded justifies the bar to damages after winding up.  **(ii) Has Houldsworth been overruled by statute?**  The question for Finkelstein J was whether section 729 has overruled Houldsworth. His Honour's analysis began by considering the history of the legislative changes leading up to section 729. His Honour mapped out a gradual progression in the legislative reforms in relation to misleading and deceptive statements in a prospectus to:   * permit shareholders who had been misled by a prospectus to claim damages from every director, promoter and other person who authorised the issue of the prospectus (section 3 of the Directors Liability Act 1890); and * expand the scope of persons liable for making misleading statements to include the company itself (section 1006 Corporations Act 1989 which was reproduced by s 1006 of the Corporations Law).   However, Finkelstein J noted that those reforms stopped short of the English reforms, in which section 111A of the Companies Act 1985 (UK) expressly provides that "a person is not debarred from obtaining damages … from a company by reason only of his holding shares … in the company…".  His Honour then canvassed factors both for and against finding that Houldsworth had been overturned by section 729. Those which his Honour viewed as being in favour of overturning Houldsworth were that:   * section 729, being remedial in nature should be given broad effect so as to permit damages even where the contract had not been rescinded; * the language of section 729 is not restricted and the requirement to firstly rescind the subscription contract would be inconsistent with the express words; and * if section 729 were not read as prevailing over Houldsworth, but as requiring rescission and restitution first, it would have limited operation and a plaintiff could only ever recover consequential or indirect damages.   Those factors which his Honour viewed as being against a finding that Houldsworth had been overturned were that:   * if Parliament had intended to overturn Houldsworth it could have done so by clear words to that effect, such as those in the Companies Act 1989 (UK); * as Parliament is aware of the consequences of Houldsworth, it could have overcome its effects by providing additional remedies, such as by expressly giving a right to return the securities and have the application money repaid; * a similar argument was made in State of Victoria v Hodgson [2002] 2 VR 613 ("Hodgson") and rejected by the Full Court of the Supreme Court of Victoria in relation to section 52 of the [Trade Practices Act 1974 (Cth)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=6426" \t "Default). The argument in Hodgson was that section 52 had overturned Houldsworth so as to allow damages for false statements by the officers of building societies which resulted in the plaintiffs subscribing for shares. Tadgell J in Hodgson said that it would be surprising if the Trade Practices Act had the intention of overturning "by implication a cardinal tenet of limited liability which has prevailed for 130 years"; and * if Houldsworth had been overturned by section 729, then a shareholder would be permitted to claim damages only in a situation where a company was a going concern as section 563A would operate so as to preclude such claims where a company was in liquidation.   Finkelstein J did not articulate how he weighed up these factors apart from saying that it seemed that the reasons for finding that Houldsworth stands is to be preferred. However, his Honour did appear to place emphasis on the final point, saying that a finding that section 729 had overturned Houldsworth would produce an "anomalous situation" and it would "require a good reason to impute to Parliament" an intention to treat a claim for damages for misleading and deceptive statements differently in the case where a company is a going concern from a case where it is in liquidation. Further, his Honour felt bound to follow the decision of the appellate court in Hodgson which held Houldsworth to be good law in spite of section 52 of the Trade Practices Act.  **5.9 What conduct will contravene section 206A (ie, what constitutes managing a company while disqualified)?**  (By Charlotte Oppy, Phillips Fox)  Australian Securities and Investments Commission v Reid [2005] FCA 1275, Federal Court of Australia, Lander J, 13 September 2005  The full text of this judgment is available at:  [http://cclsr.law.unimelb.edu.au/judgments/states/federal/2005/september/2005fca1275.htm](http://cclsr.law.unimelb.edu.au/judgments/states/federal/2005/september/2005fca1275.htm" \t "_new)  or  [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)  **(a) Summary**  The case involved proceedings commenced by the Australian Securities and Investments Commission (ASIC) seeking an order that Maxwell John Reid (Reid), the first defendant, be restrained from engaging in conduct that contravenes section 206A of the [Corporations Act 2001](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "Default).  On 10 March 1992, an order was made against Reid, pursuant to section 230 of the former Corporations Law, prohibiting him from managing a corporation until 10 August 2036.  Section 206A identifies certain acts which constitute an offence if a person is disqualified from managing corporations including that person making decisions that affect the whole or a substantial part of the business of a corporation, exercising the capacity to affect significantly its financial standing or communicating instructions or wishes to the directors of a corporation knowing that the directors are accustomed to act in accordance with that person's instructions or wishes or intending that the directors act in accordance with those instructions or wishes.  In support of its case ASIC relied upon Reid's conduct in relation to a number of entities including: Australian Marble Pty LTD (Australian Marble), Battstone Australia Pty LTD (Battstone), International Meats Pty LTD (International Meats) and Adelaide Granites Pty LTD (Adelaide Granites).  Justice Lander was satisfied that Reid's conduct in relation to all of the entities was conduct contravening section 206A and granted the order sought by ASIC. It further ordered that Reid pay ASIC's costs.  **(b) Facts**  **(i) Australian Marble**  During 2002 Reid gave instructions to associates to incorporate five companies one of which eventually came to be called Australian Marble. Reid was not a director. On 10 February 2003 Reid and the directors of Australian Marble approached Pay Now Pty LTD (Pay Now), a Sydney based financier for the purpose of obtaining a debt factoring facility of $1 million. Reid was the negotiator and played the lead role. Pay Now agreed to provide Australian Marble with the debt factoring facility.  **(ii) Battstone business**  Reid approached Battstone with the purpose of purchasing the business. An agreement was entered into whereby Battstone sold 50 per cent of its business to Australian Marble in return for Australian Marble paying all its accounts.  Subsequently Reid requested Frank Battista (a director of Battstone) to sign an invoice from Australian Marble to Battstone for materials supplied to Battstone by Australian Marble. This was faxed to Pay Now and the debts factored. Reid instructed staff as to their duties; chaired production meetings which set the order of production; negotiated with suppliers; negotiated with potential customers; collected payments from any substantial debtors; interviewed and employed staff and dealt with the bank financiers and creditors.  In March 2003 winding up proceedings were commenced against Battstone.  Subsequently, a deed was executed whereby Australian Marble acquired all the shares in Battstone. Reid's involvement in the acquisition was significant.  Post acquisition, Reid called a meeting of the staff informing them that he was 'their boss'; met with key creditors; instructed accountants; chaired production meetings and formulated a job description for the general manager before eventually terminating the general manager's employment.  On 3 June 2003 an order was made for the winding up of Battstone. Soon after, on 14 July 2003, a liquidator was appointed to Australian Marble.  **(iii) Cottage Meats business**  On 14 October 2003 Reid, on behalf of International Meats, made an offer to purchase the business and assets of Cottage Meats Pty LTD (Cottage Meats) in response to an advertisement placed by the administrator of that company (Nicholas Gyss).  Reid was not a director of International Meats but he was present at discussions that took place between it and the administrators of Cottage Meats for the purposes of discussing a deed of company arrangement. On 10 November 2003 Gyss (the administrator), received a letter that International Meats was unable to satisfy the administrator’s requirements that all funds be paid prior to possession and control of the company.  **(iv) Adelaide Granites business**  During November 2003, Reid made a series of telephone inquiries regarding the purchase of RMS Natural Stone & Ceramics Pty LTD (RMS Stone) on behalf of Adelaide Granites. This was followed by an offer via email on the letterhead of Adelaide Granites. A counter offer was addressed to Reid on 11 December 2003 to which he never responded.  **(c) Decision**  Justice Lander approached the proceeding on the basis that ASIC was required to prove its case beyond reasonable doubt rather than to the standard of proof ordinarily required in civil cases, ie, on the balance of probabilities. The fact that the allegations were serious and could lead to a finding that the first defendant had committed an offence was integral to adopting this standard even though the proceedings were not 'criminal'.  His Honour also gave importance to the fact that there were a number of facts common to this proceeding and the separate contempt proceedings brought against Reid where the standard of proof is higher, ie beyond reasonable doubt. To avoid confusion ASIC was required in the present proceedings to prove its case to the same level of satisfaction as required in the contempt proceedings, ie, beyond reasonable doubt.  **(i) Australian Marble**  His Honour was satisfied that Reid made decisions that affected if not whole, then a substantial part, of the business of Australian Marble. He had the capacity and exercised that capacity to significantly affect Australian Marble's financial standing. The directors were accustomed to act in accordance with Reid's wishes and any power they exercised was done at his direction. Reid involved himself in all the decisions and did so knowing and intending the directors would act in accordance with his wishes and directions.  **(ii) Battstone Australia**  The same finding was made with respect to Battstone. The court held that Reid made decisions that affected the whole or a substantial part of the business of Battstone. The directions given to both the general manager and accountant showed their subservience to Reid. Further, those directions showed that he made, or participated in making, decisions that affected the whole, if not a substantial part of the business of Battstone. Moreover, those matters established that he exercised the capacity to affect Battstone's financial standing.  Further, his Honour found that prior to his resignation as director, Frank Battista acted in accordance with the instructions of Reid in relation to the provision of an invoice used for debt factoring.  **(iii) International Meats**  The court was satisfied that Reid made decisions which affected a substantial part of the business of International Meats in its attempt to purchase Cottage Meats. A further finding was made that Reid communicated instructions or wishes to the directors of International Meats knowing that they were accustomed to act in accordance with his instructions and wishes and intending that they do so.  **(iv) Adelaide Granites**  The court found that as Reid made the offer to purchase RMS Stone on Adelaide Granites' letterhead, he expected that the directors of Adelaide Granites would act in accordance with his wishes.  Justice Lander noted that the conduct of Reid, of which ASIC complained, continued over a significant part of 2003. ASIC had therefore clearly established that it was likely that Reid, unless restrained, would continue to contravene section 206A of the Act. As such the court was prepared to make the orders sought.  **5.10 Validity of deathbed instructions and the extent of powers of attorney in relation to corporate transactions**  (By Aaron Hockly, Solicitor, Clayton Utz)  Saad v Doumeny Holdings Pty Limited [2005] NSWSC 893, New South Wales Supreme Court, Burchett AJ, 8 September 2005  The full text of this judgment is available at:  [http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/september/2005nswsc893.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/september/2005nswsc893.htm" \t "_new)  or  [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)  **(a) Summary**  The estate of Michael Saad sought declarations that the purported appointment of the second defendant, Bassam Ghantous, as a director of, and the issue of shares to the plaintiff and the second defendant in, Doumeny Holdings Pty LTD were invalid. Mr Ghantous purported to appoint himself a director and issue shares on the basis of a brief discussion he had with Michael Saad hospital prior to Michael Saad's death and on the basis of a power of attorney previously granted to him by Michael Saad.  The court granted the declarations requested for 6 main reasons. Firstly, the words used by the deceased did not amount to the actual appointment of Mr Ghantous as a director and, at the time of the conversation, was merely a hypothetical scenario not then expected to occur. Secondly, although the company's constitution enabled Michael Saad to appoint another director, this power could only be exercised by Michael Saad personally and not by his agent, ie Ghantous as Saad's attorney. Thirdly, as there was no specific discussion about the issuing of shares, the conversation between Mr Ghantous and Michael Saad did not amount to an agreement to issue shares. Fourthly, Mr Ghantous purported to issue new shares via a general meeting of the company whereas the articles of the company gave this power to the directors, and accordingly, the general meeting could not issue new shares. Fifthly, new shares could not be issued merely to dilute or destroy an existing majority, as was Ghantous' purpose. Finally, Mr Ghantous exceeded the scope of his authority as Saad's attorney through seeking to dilute the shareholding of his principal, Michael Saad, thereby acting against the interests of his principal.  **(b) Facts**  In 1970, Mr Arthur and Mrs Afifi Saad (both deceased) formed a company, Doumney Holdings Pty LTD, for their dry-cleaning business. Through various share transfers, the majority of the shares in Doumney Holdings ended up being owned by Mr and Mrs Saad's son, Michael Saad (deceased), and Michael Saad and Mr Bassam Ghantous as joint trustees for Mr and Mrs Saad's second son, Nicholas Saad.  Mr Ghantous was the accountant for Doumney Holdings and an uncle of Nicholas and Michael Saad. Mr Ghantous held powers of attorney for Michael Saad.  In 2004, while in hospital for what was believed at the time to be non-life threatening surgery, Michael Saad was visited by Mr Ghantous. During this visit, Mr Ghantous and Michael Saad had the following conversation- Mr Ghantous "Mate, what if something happens to you?" Michael Saad "Look, just look after everybody". Mr Ghantous "You know I'll do that, but I may have to get appointed as director of all the companies". Michael Saad "Yep, do that, you've got the power of attorney".  Shortly thereafter Michael Saad lapsed into a coma.  On the basis of the above conversation, Mr Ghantous, alone in his own home, purported to hold two meetings of Doumney Holdings to appoint himself as director and secretary and to issue further shares to Michael Saad and to himself as trustee for Nicholas Saad. The minutes of the meetings were signed by Michael Saad "per Bassam Ghantous (signed under a power of Attorney)". Mr Ghantous testified in Court that he had issued new shares to equalise the shareholding of Michael Saad and Nicholas Saad.  Michael Saad subsequently passed away.  **(c) Decision**  The purported appointment of Mr Ghantous as a director of Doumney Holdings and the purported issues of shares in Doumney Holdings to Mr Michael Saad and Mr Ghantous were held to be void.  **(i) No appointment as a director**  Burchett AJ found that the conversation between Michael Saad and Mr Ghantous did not amount to a request from Michael Saad that Mr Ghantous become a director at that time. His Honour held that the words used by Michael Saad suggested that only if something happened to him would the need arise for Mr Ghantous to "get appointed" as a director. His Honour placed emphasis on the fact that Michael Saad was not "expecting or expected to lapse into a coma [or die]". Furthermore, Burchett AJ found that no words of appointment were actually used.  **(ii) An attorney cannot perform "personal" responsibilities of a director**  Burchett AJ noted that Michael Saad had been acting as the sole director of Doumney Holdings for some years and that the articles allowed a sole director to appoint another director in order to meet the necessary quorum of 2. However, his Honour also noted that, as Michael Saad had failed to utilise this provision, Mr Ghantous was unable to do so under his authority as attorney of Saad. Burchett AJ referred to Mancini v Mancini (1999) 17 ACLC 1570 at 1577-1578 where Bryson J stated that "[t]he office of a director is not a property right capable of being exercised by an attorney or other substitute or delegate of the person holding the office … ".  **(iii) No direction to issue further shares**  Burchett AJ found that nothing in the conversation between Mr Ghantous and Michael Saad amounted to an agreement that Mr Ghantous should issue further shares.  **(iv) General meeting could not issue new shares**  Burchett AJ noted, from the title of the minutes of the meeting purporting to issue new shares, that it was a purported meeting of the company rather than of its directors. His Honour found that the articles of Doumney Holdings reserved the power to issue shares to the directors and, relying on precedent (Quin & Axtens Limited v Salmon [1909] AC 442 per Lord Loreburn LC at 443, National Roads & Motorists' Association v Parker (1986) 6 NSWLR 517 per McLelland J at 521 and National Roads & Motorists' Association v Bradley (2002) 42 ACSR 616, per Windeyer J at 618), noted that matters which are reserved for directors by a company's constitution cannot be interfered with by a company in general meeting. Only a directors’ meeting, rather than a general meeting, had the power to issue new shares in this company.  **(v) New shares cannot be issued merely to destroy an existing majority**  Even if shares were issued at a directors' meeting, relying on precedent (Howard Smith LTD v Ampol Petrolem LTD [1974] AC 821, per Lord Wilberforce at 837), Burchett AJ noted that Mr Ghantous nevertheless could not validly issue new shares merely to equalise the respective holdings of Michael Saad and Nicholas Saad (which he claimed was his aim).  **(vi) An agent's powers must be used for the benefit of their principal**  Burchett AJ also held that Mr Ghantous was acting outside the scope of his appointment by deliberately attempting to use his power of attorney to dilute the shareholding of Michael Saad, his principal, thereby departing from "his undivided loyalty to his principal's interests".  **5.11 The difference between a wish and an intention in relation to a contractual dispute**  (By Chris Spalding, Clayton Utz)  GPT RE LTD v Lend Lease Real Estate Investments LTD [2005] NSWSC 964, New South Wales Supreme Court, White J, 27 September 2005  The full text of this judgment is available at:  [http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/September/2005nswsc964.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/september/2005nswsc964.htm" \t "_new)  or  [http://cclsr.law.unimelb.edu.au/judgments/index.html](http://cclsr.law.unimelb.edu.au/judgments/index.html" \t "_new)  **(a) Summary**  GPT RE LTD (GPT) and Lend Lease Real Estate Investments LTD (Lend Lease) each owned a 50% interest in a shopping centre. Their ownership was regulated by a Joint Ownership Agreement which contained certain preemptive rights. GPT entered into a put and call option deed (Deed) with Westfield Management LTD (Westfield) over a 25% interest in the property. The options were subject to conditions, including a condition that Lend Lease not exercise its preemptive rights under the Joint Ownership Agreement in respect of the property.  Lend Lease contended that GPT, by entering into the Deed, had triggered preemptive provisions contained in the Joint Ownership Agreement.  The questions for determination by the court involved the interpretation of the terms of the Joint Ownership Agreement, namely whether:   * GPT had "dealt with" part of its "Interest" as defined in the Joint Ownership Agreement; * GPT wished to deal with its Interest; and * GPT, if it wished to deal with its Interest, had to follow the steps set out in the Joint Ownership Agreement for dealing with its Interest.   **(b) Facts**  GPT and Lend Lease were parties to a Joint Ownership Agreement made on 25 June 1992 between their predecessors in title. On 17 February 2005, the previous responsible entity of the trust of which GPT was now the responsible entity gave a call option to Westfield Management LTD for it to purchase a 25% interest in the property. At the same time, Westfield gave a put option to GPT to require Westfield to purchase a 25% interest in the property. The options were subject to conditions, including a condition that Lend Lease not exercise its preemptive rights under the Joint Ownership Agreement in respect of the property.  Lend Lease contended that, because of these transactions, and because GPT wished to sell a 25% interest in the shopping centre but did not comply with the preemptive provisions of the Joint Ownership Agreement, Lend Lease was entitled to acquire all of GPT's Interest at valuation. GPT brought the proceedings to establish that Lend Lease was not entitled under the Joint Ownership Agreement to instigate the valuation of its 50% interest and that it could not be forced to sell its Interest to Lend Lease at valuation.  Clause 9(a) of the Joint Ownership Agreement provided:  "(a)(1) unless otherwise agreed by the Owners, an Owner (Selling Owner) may not deal with its Interest in whole or in part other than as provided in this clause 9 and unless the procedures set forth in this clause 9 have been followed strictly."  Clause 9(c) provided:  "A Selling Owner wishing to deal with its Interest in whole or in part ("Sale Interest"), must serve notice in writing to that effect on the other owner(s) ("Offeree") and AFM, such notice to contain the terms and conditions referred to in clause 9(d) ("Transfer Notice")."  Clause 9(d) described what should be included in the Transfer Notice. Clause 10 of the agreement was concerned with the consequence of an owner committing an "Event of Default". An Event of Default included an owner failing to comply with, observe or perform any of its obligations under the agreement. Under clause 10, if an Event of Default was not remedied or waived or compensation was not paid within a reasonable time, then the non-defaulting owners would be entitled to acquire the defaulting owner's interest at valuation.  By 17 June 2005, all of the conditions precedent to the put and call options had been satisfied, except for the condition that Lend Lease not exercise its pre-emptive rights under the Joint Ownership Agreement. The Deed was varied by GPT and Westfield and made conditional upon Lend Lease waiving its pre-emptive rights in respect of the property and Lend Lease not exercising its pre-emptive rights in respect of the property. Clause 2.2(b) of the Deed provided that GPT would, if requested by Westfield, give notice to Lend Lease instigating the procedures in clause 9 of the Joint Ownership Agreement applicable to a selling owner in respect of its Interest.  **(c) Decision**  **(i) The meaning of "deal with"**  White J first dealt with the issue of whether GPT had "dealt with" part of its "Interest" under the Joint Ownership Agreement by entering into the Deed. White J found that it was only transactions which amounted to an alienation of the whole or part of an owner's interest which would fall within the definition of "deal with". His Honour found that the grant of an option to a third party to acquire land gave the optionee an equitable interest in the land in respect of which the option was given. Lend Lease submitted that, notwithstanding the conditions precedent to the exercise of the option, Westfield had acquired an equitable interest in the property. White J did not regard the fact that GPT had entered into a contract whereby it might be obliged to part with half its interest in the future if Lend Lease did not exercise, and waived, its pre-emptive rights, as amounting to a present disposition or alienation of part of its Interest. His Honour found Westfield had a contingent equitable interest in the property that operated as an imposition on GPT's title, not as a subtraction from it. His Honour found that GPT had not parted with an Interest in the property.  Lend Lease made a separate submission that a number of GPT's "interests, rights and benefits" as owner of the property were dealt with by its entering into the Deed which did not depend on Lend Lease waiving its pre-emptive rights. White J did not accept that the unconditional promises GPT made to Westfield as to how it would exercise its rights under the Joint Ownership Agreement were a dealing with its interest in breach of clause 9(a) of the Joint Ownership Agreement.  **(ii) "Wish to deal"**  White J drew a distinction between "wishing" and "intending". GPT stated that it did not intend to deal with its Interest unless and until Lend Lease waived its pre-emptive rights under the Joint Ownership Agreement. It asserted that in the absence of such a waiver, it did not "wish" to deal with its Interest. GPT contended that it was unreasonable to construe the phrase "wishing to deal" as including a conditional wish or desire on the part of an owner to deal with part of its Interest, at least where the wish to deal was expressly conditional on the non-exercise or the waiver by the other owner of its pre-emptive rights. The court found that GPT wished to transfer part of its Interest but only intended to transfer part of its Interest if the conditions in the Deed were satisfied.  **(iii) Clause 9(c) - promissory or facultative?**  Lend Lease argued that clause 9(c) had a promissory effect, ie it obliged GPT to give a transfer notice once it formed its wish to deal with its Interest.  White J found that, when clause 9(c) was read in the context of clause 9(a), it should be construed as a merely facultative provision. Clause 9(c) and the following subclauses described the procedures to be followed if an owner wished to deal with its Interest, ie it set out what an owner must do if it wished to deal with its Interest in the way permitted by clause 9.  His Honour found that an owner did not breach clause 9(c) if it formed a wish to deal with its Interest and did not serve a transfer notice. GPT had not failed to comply with, observe or perform any of its obligations or undertakings in clause 9(c) by not serving a transfer notice. Rather, it had not taken advantage of the facility which that clause provided if it wished to deal with its Interest.  **5.12 Statutory derivative action**  (By Elliot Raleigh, Clayton Utz)  Maher v Honeysett & Maher Electrical Contractors [2005] NSWSC 859, New South Wales Supreme Court, Brereton J, 25 August 2005  The full text of this judgment is available at:  [http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/august/2005nswsc859.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/august/2005nswsc859.htm" \t "_new)  or  [http://cclsr.law.unimelb.edu.au/judgments/index.html](http://cclsr.law.unimelb.edu.au/judgments/index.html" \t "_new)  This judgment deals with an application under sections 236 and 237 of the [Corporations Act 2001 (Cth)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "_new) (the "Act") by a member of a deadlocked company to defend proceedings against the company and to bring a cross-claim against the other member and director. Brereton J's judgment clarifies a number of the requirements for leave to bring a derivative action.  **(a) Facts**  The plaintiff, David John Maher ("Maher") and the first defendant Mark William Honeysett ("Honeysett") were the only directors of and equal shareholders in Honeysett & Maher Electrical Contractors Pty Limited ("HME"). Irreconcilable differences arose between them as to the future of HME. Maher instituted proceedings to have HME wound up on the just and equitable ground, and to enforce agreements which he contended had been made between him, Honeysett and HME as to the distribution of HME's assets. Honeysett opposed the winding-up of HME and enforcement of the alleged agreements, and by cross-claim asserted that those agreements were procured by the duress or unconscionable conduct of Maher. Honeysett sought leave to defend Maher's claim on behalf of HME, and to bring a cross-claim in the name and on behalf of HME against Maher and his company Demaher Pty Limited ("Demaher"), for equitable compensation and/or an account of profits by reason of alleged breaches by Maher of his fiduciary obligations as a director of HME, for which Demaher was said to have benefited.  **(b) Decision**  Brereton J held that Honeysett should be granted leave to bring a cross-claim in the name and on behalf of HME against Maher pursuant to section 237 of the Act.  However, Brereton J held that in circumstances where the claims against HME could be resisted by Honeysett in his own right as a defendant, it would add nothing to grant him leave to do so on behalf of HME. As such, Honeysett was not granted leave to intervene in the proceedings for the purpose of taking responsibility on behalf of HME for the defence of the proceedings.  **(c) Principles**  Brereton J's judgment clarifies a number of the requirements in obtaining leave to bring statutory derivative actions.  Section 236 of the Act allows a member of a company, acting with the leave of the Court granted under section 237, to bring proceedings on behalf of the company, in the name of the company. By section 237(1), such a person may apply to the court for leave to bring, or intervene in, such proceedings, and by section 237(2), the Court must grant the application if it is satisfied that:   * it is probable that the company will not itself bring the proceedings, or properly take responsibility for them, or for the steps in them; and * the applicant is acting in good faith; and * it is in the best interests of the company that the applicant be granted leave; and * if the applicant is applying for leave to bring proceedings – there is a serious question to be tried. This criterion was conceded by Maher, and the Court also readily concluded that this criterion had been established; and * either:   i. at least 14 days before making the application, the applicant gave written notice to the company of the intention to apply for leave and of the reasons for applying; or ii. it is appropriate to grant leave even though subparagraph (i) is not satisfied.  **(i) "Must" all five criteria be satisfied?**  Brereton J considered that the nature of the criteria makes it highly improbable that it was intended that there be a residual discretion to grant leave. Accordingly, Brereton J concluded that leave under section 237 may not be granted unless the applicant satisfies each of the five criteria. Furthermore, Brereton J held that as a consequence of the requirement that all five criteria be satisfied, the relevant considerations are limited to the five specified criteria.  **(ii) Probable that the company will not itself bring the proceedings**  Brereton J held that determining whether it is probable that the company will or won't bring proceedings requires a "judgment to be made of the probabilities based on the presenting circumstances at the time of the hearing" of the section 237 application. In other words, deferral of that judgment on the basis that the state of the company’s affairs might change in the future is not permitted.  Brereton J cited Talisman Technologies Inc v Queensland Electronic Switching Pty Limited [2001] QSC 324. In this case Mullins J said that there was a question of timing in determining whether it was probable that the company would not itself bring proceedings, and that, until the disputes among the shareholders were determined, the company would not be in a position itself to endeavour to pursue claims that might accrue to it.  However, Brereton J considered that this criterion requires a judgment to be made of the probabilities based on the presenting circumstances at the time of the hearing of the section 237 application. Brereton J held that "while judgments as to whether it is probable that the company will not itself bring proceedings requires some prediction of what may transpire in the future, those possible future eventualities form part of the factual matrix upon which a judgment of the present probabilities is to be based".  Applied to the facts in this case, considering Maher's 50% shareholding and Honeysett's opposition to a winding up, Brereton J held that it was more probable than not that HME would not bring the proposed proceedings against Maher and Demaher, and would not take steps for the defence of the proceedings against it.  **(iii) Good faith**  Brereton J referred to the judgment of Palmer J in Swansson v R A Pratt Properties Pty Ltd (2002) 42 ACSR 313 ("Swansson"), in which Palmer J identified two inter-related factors to which the courts would always have regard in determining whether the good faith requirement imposed by section 237(2)(b) would be satisfied:   * whether the applicant for leave honestly believes that a cause of action exists and has a reasonable prospect of success; and * whether the applicant is seeking to bring the derivative suit for such a collateral purpose that the application would amount to an abuse of process.   Palmer J added that whether the applicant honestly holds such a belief would not simply be a matter of bald assertion (whether by affidavit or otherwise) and that the applicant may be disbelieved if no reasonable person in the circumstance would hold that belief.  On the other hand, Brereton J also referred to the judgment of Mandie J in Chapman v E-Sports Club Worldwide Limited (2000) 35 ACSR 462 ("Chapman"), which gave significance to the circumstance that the applicant had not gone on affidavit, and had not even sought the opportunity to do so when substantial material had been filed giving a complete version of what took place.  Maher submitted that it would have been very easy for Honeysett to make the relevant assertion but he did not make one and as such, as in Chapman, it should be inferred that Honeysett did not have the requisite honest belief.  However, Brereton J distinguished this case from Chapman on the basis that Honeysett had sworn affidavits upon which he could have been cross-examined and by which his state of mind could have been tested. Furthermore, Brereton J did not take Palmer J in Swansson to have stipulated that there must be a sworn assertion by the applicant that he believes that a good cause of action exists and has reasonable prospects of success, but rather that Palmer J identified a state of mind (honest belief that a cause of action exists and has a reasonable prospect of success) which must be found to exist in the applicant, rather than any particular means by which that state of mind is to be proved. Brereton J stated that, while in some cases the presence or absence of a sworn assertion of the relevant state of mind might be very important, generally speaking such statements must be of little weight or utility, and the objective facts will speak louder than the applicant’s words. Brereton J considered that a sworn assertion will almost always be an unqualified opinion founded on hearsay, since a lay applicant will rarely know whether or not a good cause of action exists, or its prospects of success, and will be dependent upon the advice of lawyers for forming the relevant belief.  Brereton J was satisfied that Honeysett was acting in good faith: he had filed and served all evidence on which he proposed to rely in the substantive proceedings, he was a current shareholder of HME, he had a large shareholding, and the derivative action sought compensation for HME.  **(iv) Best interests of the company**  Brereton J concluded that the cross-claim on behalf of HME would be in the best interests of the company, so long as HME would not be exposed to the risk of suffering adverse costs consequences.  However, Brereton J held that in circumstances where the claims against HME could be resisted by Honeysett in his own right as a defendant, it would add nothing to grant him leave to defend proceedings on behalf of HME. Nor was Brereton J satisfied that it was in the best interests of HME that Honeysett be granted leave to intervene in the proceedings for the purpose of taking responsibility on behalf of HME for the defence of the proceedings.  It was held that the existence in an applicant of a personal interest in the outcome of a proposed derivative action cannot be significant, let alone decisive, to the question of whether the proposed action is in the best interests of the company. Brereton J considered that "they are usual concomitants of the types of disputes which lead to derivative actions, and few if any such actions would be brought but for personal interest on the part of the relevant applicant and in the absence of animus against the company or other shareholders."  Nor did Brereton J think that the mental fitness of an applicant should be a relevant consideration when assessing the company's best interest. Maher had claimed that Honeysett was not a suitable person to be granted leave as, due to his "moderate depression" (as diagnosed by a psychiatrist), he would not be capable of making rational decisions. It was held that mental fitness of the applicant was not relevant to the question of whether it is in the best interests of the company for such an applicant to be granted leave. If it were established that an applicant satisfied the five criteria but was incapable of managing his or her affairs, the proper conclusion would be to grant leave, but require that a tutor conduct the proceedings.  Finally, Brereton J considered how to strike a balance between the prejudice that the company would suffer if claims were pressed unsuccessfully on its behalf and it was called upon to meet an adverse costs order, and the advantage that it would gain indirectly for the benefit of its shareholders if the claim was successful. In this instance, Brereton J found that a suitable way of dealing with this was to grant leave on terms that Honeysett be responsible for any costs ordered against the company and for Honeysett to undertake not to seek contribution or indemnity from HME for such costs. |
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