CORPORATE LAW BULLETIN

Bulletin No 72, August 2003

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

Published by LAWLEX on behalf of  
Centre for Corporate Law and Securities Regulation,  
Faculty of Law, The University of Melbourne  
([http://cclsr.law.unimelb.edu.au](http://cclsr.law.unimelb.edu.au" \t "_new))

with the support of

The Australian Securities and Investments Commission ([http://www.asic.gov.au](http://www.asic.gov.au" \t "_new)),  
The Australian Stock Exchange ([http://www.asx.com.au](http://www.asx.com.au" \t "_new))

and the leading law firms:

Blake Dawson Waldron ([http://www.bdw.com.au](http://www.bdw.com.au" \t "_new))  
Clayton Utz ([http://www.claytonutz.com](http://www.claytonutz.com" \t "_new))  
Corrs Chambers Westgarth ([http://www.corrs.com.au](http://www.corrs.com.au" \t "_new))  
Freehills ([http://www.freehills.com](http://www.freehills.com" \t "_new))  
Mallesons Stephen Jaques ([http://www.mallesons.com](http://www.mallesons.com" \t "_new))  
Phillips Fox ([http://www.phillipsfox.com](http://www.phillipsfox.com" \t "_new))

ACCESS TO ARCHIVED ISSUES

As a subscriber, you may view and print the latest Bulletin immediately from the archive site on the Internet at:

[http://research.lawlex.com.au/cclsr/archive](http://research.lawlex.com.au/cclsr/archive" \t "default)

COPYRIGHT WARNING

Centre for Corporate Law and Securities Regulation 2003.

You may use this material for your own personal reference only. The material may not otherwise be used, copied or redistributed in any form or by any means without a multiple user licence with LAWLEX.

CHANGE OF EMAIL ADDRESS

Subscribers who change their email address should notify LAWLEX at "[cclsr@lawlex.com.au](mailto:cclsr@lawlex.com.au)".

CONTENTS

[1. RECENT CORPORATE LAW AND CORPORATE GOVERNANCE DEVELOPMENTS](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#1)

[(A) Survey of compliance with ASX corporate governance guidelines](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#1a)  
[(B) Fund managers and corporate governance](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#1b)  
[(C) ABA responds to corporate scandals and adopts new lawyer ethics rules](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#1c)  
[(D) IAASB proposes auditors take a more active role in seeking out fraud](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#1d)  
[(E) NASD proposes disclosure of mutual fund compensation arrangements](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#1e)  
[(F) SEC proposes disclosure requirements related to director nominations and shareholder communications](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#1f)  
[(G) New report: Do multinational enterprises benefit Australia?](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#1g)  
[(H) New guide to the EU Financial Services Action Plan](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#1h)  
[(I) New report presents international perspective on strengthening the financial reporting process](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#1i)  
[(J) Study: Independent directors see significant changes in remuneration](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#1j)  
[(K) ACCC welcomes issue of insurance report](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#1k)  
[(L) Study of 2003 financial restatements](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#1l)   
[(M) HIH Institute of Accountants Task Force](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#1m)   
[(N) SEC announces approval of SRO rules addressing research analyst conflicts of interest](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#1n)  
[(O) GMI launches global governance ratings](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#1o)   
[(P) SEC study on adoption by the US financial reporting system of a principles-based accounting system](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#1p)  
[(Q) Report: Corporate Governance and Climate Change](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#1q)

[2. RECENT ASIC DEVELOPMENTS](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#2)

[(A) Retirement of ASIC Chairman](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#2a)  
[(B) ASIC class order exempts issuers of certain documents from requirement to hold an AFSL](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#2b)  
[(C) ASIC releases fee disclosure model](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#2c)  
[(D) 440 listed entities to be reviewed by ASIC](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#2d)  
[(E) ASIC releases surveillance report on research analyst independence](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#2e)  
[(F) Superannuation sponsors](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#2f)

[3. RECENT TAKEOVERS PANEL MATTERS](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#3)

[(A) Resolution of proceedings relating to BreakFree Limited](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#3a)  
[(B) Panel declines application for a declaration of unacceptable circumstances in relation to PowerTel Ltd (No 3)](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#3b)

[4. RECENT CORPORATE LAW DECISIONS](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#4)

[(A) Extending limitation period for recovery of preferences](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#4a)  
[(B) Effect on trusts of liquidation of trustee companies and claims by persons claiming to be trustees](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#4b)  
[(C) Directors' duties - fiduciary duties and derivative proceedings](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#4c)  
[(D) Pooling in voluntary administration](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#4d)  
[(E) The Tax Commissioner's advantage in insolvent administrations](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#4e)  
[(F) Misleading and deceptive conduct under section 52 of the Trade Practices Act](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#4f)  
[(G) Whether a receiver is liable to employees in continued employment for annual leave, long service leave and retrenchment entitlements](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#4g)  
[(H) Reliance by insurer on an exclusion clause in a director's insurance policy before a finding of dishonesty](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#4h)  
[(I) When is the enforcement guarantee unconscionable?](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#4i)  
[(J) Approval of a scheme of arrangement between United Energy Limited and its members](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#4j)  
[(K) Extension of time granted to register charge in respect of company in administration](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#4k)

[5. CONTRIBUTIONS](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#5)

[6. MEMBERSHIP AND SIGN-OFF](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#6)

[7. DISCLAIMER](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0072.htm#7)

1. RECENT CORPORATE LAW AND CORPORATE GOVERNANCE DEVELOPMENTS

(A) SURVEY OF COMPLIANCE WITH ASX CORPORATE GOVERNANCE GUIDELINES

On 15 August 2003 Chartered Secretaries Australia (CSA) published a survey of Company Secretaries in the ASX Top 200 companies finding that a majority (67 per cent) had already extensively assessed their compliance with the ASX corporate governance guidelines, while 33 per cent had assessed it to a reasonable extent.

However, a major challenge for many companies will be in the rules relating to directors' independence.

"It seems many companies are finding it impractical to have a majority of independent directors, while some believe the definition of 'independent' is too strict. It is certainly the most commonly cited issue, with around a quarter of respondents choosing to explain their non-compliance", said chief executive of Chartered Secretaries Australia, Mr Tim Sheehy.

On the whole, however, he says, the guidelines are not causing major problems.

"Our survey found that 87 per cent of companies are confident they will meet all minimum requirements by the next phase of reporting, indicating a good understanding of the changes involved", said Mr Sheehy.

For the 64 per cent of companies who do not currently comply, and the 12 per cent who currently comply partially, it is high on the agenda. Ninety seven per cent plan to increase their compliance - 57 per cent in the next six months and 37 per cent within the year.

Despite a high level of cooperation, however, the jury is still out on the impact of the guidelines. Just over half believe the guidelines are fostering a culture of improved corporate governance in their organisation. Some say it has already prompted further discussion, review and action on the subject and, in turn, reinforced better behaviour from decision makers. But the other half is yet to be convinced.

The survey also revealed that the cost of meeting the requirements would not be too onerous for most. Sixty one per cent estimate only a zero to five per cent increase to compliance costs, and 18 per cent estimate a five to ten per cent increase.

(B) FUND MANAGERS AND CORPORATE GOVERNANCE

On 14 August 2003 the Investment and Financial Services Association (IFSA) released at its annual conference the survey results on "Shareholder Activism Among Fund Managers: Policy and Practice" prepared by IFSA and verified by KPMG.

IFSA is the peak Australian national body representing the wholesale and retail investment management, superannuation and life insurance industries. IFSA has over 100 members who invest approximately $630 billion dollars on behalf of over 9 million Australians.

IFSA Chief Executive Officer, Mr Richard Gilbert said, "the survey shows that fund managers are active shareholders in the companies in which they invest. High levels of voting and contact with management were shown to be key areas of fund manager's ever increasing activism to raise the bar on corporate governance."

IFSA members invest approximately $160 billion in the Australian equities market on behalf of superannuation beneficiaries and other investors. This accounts for approximately 25% of the ASX by market capitalisation (based on ASSIRT and ASX data). Survey respondents accounted for 98% of the investment in Australian equities.

Key findings of the report include:

- On average, fund managers vote on 92% of all company resolutions. This is a dramatic increase from the Eureka (2001) survey, which reported that the average voting level was 67% of resolutions.  
- Routine voters (who vote on at least 90% of all resolutions) accounted for 91% of fund managers and 98% of funds under management. This is an increase from the 2001 survey where 59% of fund managers were routine voters and accounted for 69% of funds under management.  
- Voting accounted for 40% of all time spent on corporate governance related issues. In 2001, voting accounted for 29% of time spent on corporate governance activity.  
- Voting is overwhelmingly considered to be the least effective method of influencing corporate governance outcomes. Fund managers rate direct contact with companies as nearly twice as effective in influencing board and management decisions as opposed to casting proxy votes.  
- All the major index managers are now voting their proxies.  
- Overwhelming fund managers were against publicly disclosing how they voted on a specific resolution, as they considered it limited their flexibility to use other forms of pressure to achieve the same goals.  
- On average less than four retail investors per fund manager requested information on how a manager voted their proxies in the past 12 months. (The IFSA Blue Book and Standard Investment Management Agreement require fund managers to disclose their voting policy and practices to superannuation trustees.)

Copies of the report are available on the IFSA website at [http://www.ifsa.com.au/](http://www.ifsa.com.au/" \t "_new)  
  
(C) ABA RESPONDS TO CORPORATE SCANDALS AND ADOPTS NEW LAWYER ETHICS RULES

On 12 August 2003 the American Bar Association House of Delegates concluded its 126th Annual Meeting by adopting new lawyer conduct rules responding to recent corporate scandals.

The House of Delegates approved three proposals from the ABA Task Force on Corporate Responsibility. The first amended Rule 1.6 of the ABA Model Rules of Professional Conduct to permit a lawyer to reveal confidential client information if the client is using the lawyer's services to commit a crime or fraud that would cause financial harm to others. The second proposal amended Rule 1.13 to permit a lawyer representing an organisational client to report up the corporate ladder violations by corporate officers of laws or legal duties that would harm the organization. The third endorsed structural and procedural reforms to improve corporate governance.

"These reforms are necessary steps that bring our standards into line with today's legal profession," said ABA President Dennis W Archer of Detroit. "Forty-two states have already adopted such measures on their own, with no adverse effect on client confidentiality."

Further information, including the report of the ABA Taskforce on Corporate Responsibility, is available on the ABA website at [http://www.abanet.org/](http://www.abanet.org/" \t "_new)

(D) IAASB PROPOSES AUDITORS TAKE A MORE ACTIVE ROLE IN SEEKING OUT FRAUD

On 12 August 2003 the International Federation of Accountants (IFAC) announced that at a meeting in New York on 21-25 July 2003, the International Auditing and Assurance Standards Board (IAASB) of the International Federation of Accountants (IFAC) addressed one of the most important issues facing auditors today: responsibility for detecting fraud. The IAASB approved the release of an exposure draft (ED) of an International Standard of Auditing (ISA) titled "The Auditor's Responsibility to Consider Fraud in an Audit of Financial Statements" (ISA 240).

At the same meeting, the IAASB took actions to strengthen and clarify the IAASB's international standard-setting role and process by issuing amended terms of reference and a Preface to its standards. It also approved the release of a second exposure draft entitled "Planning the Audit."

(1) Proposed ISA expands guidance for fraud detection

The ED of the proposed ISA on fraud sets out the auditor's responsibility to consider fraud in an audit of financial statements. The ED also explains that the primary responsibility for the prevention and detection of fraud rests with both those charged with governance and management of the entity and describes the responsibilities of these parties.

This ED also alerts auditors to risks of material misstatement due to fraud they may encounter in the conduct of an audit and requires the auditor to assess the risks of material misstatement due to fraud and to responds to the assessed risk. The new proposed ISA requires the auditor to respond to the presumed risk of improper revenue recognition and the risk of management override of controls. This response includes testing the appropriateness of journal entries, reviewing the accounting estimates for biases and obtaining an understanding of the business rationale of significant transactions that are outside of the normal course of business for the entity. It also discusses auditor communications with management and those charged with governance, as well as auditor communications to regulatory and enforcement authorities.

(2) New Preface emphasises IAASB's independence

The IAASB issued a new "Preface to International Standards on Quality Control, Auditing, Assurance and Related Services," which includes new terms of reference for the Board. The Preface clarifies the IAASB's role as an independent standard-setting body under the auspices of IFAC, highlights its public- interest responsibilities and emphasises its objective of achieving convergence of standards by working closely with national standard setters.

(3) Audit Planning ED includes new guidance

The ED of proposed ISA 300, "Planning the Audit," complements the IAASB's proposed guidance on audit risk issued in October 2002. It includes basic principles and essential procedures on the considerations and activities applicable to planning an audit of financial statements. In particular, it provides new guidance on matters the auditor should consider prior to performing significant planning activities: client acceptance and retention; ethical requirements including independence and communications with prior auditors; and the terms of the audit engagement. The ED also incorporates more specific guidance regarding planning considerations in initial audits and includes a discussion of the planning considerations related to the direction, supervision and review of the work of engagement team members.

(4) Accessing EDs and new guidance

The exposure drafts may be viewed by going to the IFAC website at [http://www.ifac.org/EDs](http://www.ifac.org/EDs" \t "_new). Comments must be submitted by November 15, 2003 to [Edcomments@ifac.org](mailto:Edcomments@ifac.org), faxed to the IAASB Technical Director at +1-212-286-9570 or mailed to the IAASB Technical Director at IFAC, 545 Fifth Avenue, 14th Floor, NY, NY 10017.

The Preface can be accessed by going to the IAASB website at [http://www.ifac.org/iaasb](http://www.ifac.org/iaasb" \t "_new) and looking in the section headed "2003 Publications."

(E) NASD PROPOSES DISCLOSURE OF MUTUAL FUND COMPENSATION ARRANGEMENTS

On 7 August 2003 the United States National Association of Securities Dealers (NASD) proposed for comment a rule that would expand the disclosure of two types of compensation paid for the sale of mutual fund shares. Disclosure of these practices would alert investors to the fact that a brokerage firm or its registered representatives may have financial incentives to recommend particular funds.

NASD's Board of Governors approved a proposal for disclosure of two types of compensation paid for the sale of mutual fund shares. The first type of compensation consists of cash payments to brokerage firms in return for shelf space. The second is the payment of a higher compensation rate to registered representatives for selling certain funds.

The proposal would require firms to disclose the nature of certain compensation arrangements in writing when the customer first opens an account or purchases mutual fund shares. The proposal also would require member firms to update this information twice a year and make it available on their websites.

The proposed amendments would require a securities firm to disclose:

- that information regarding a fund's fees and expenses may be found in the fund's prospectus;  
- that the fund's policies regarding selection of securities firms (such as soft dollar and directed brokerage arrangements) are described in the fund's statement of additional information, which an investor may request;  
- if applicable, that the member receives cash payments from mutual funds and their affiliates other than the fees disclosed in a fund's prospectus fee table, and the nature of this compensation;  
- a list of mutual fund firms that made these payments to the firm in descending order based upon the total amount of compensation received from each firm; and  
- if applicable, that registered representatives receive different rates of compensation for different investment company products, the nature of these arrangements, and the names of the investment companies favoured by these arrangements.

More information is available on the NASD website at [http://www.nasd.com](http://www.nasd.com" \t "_new)

(F) SEC PROPOSES DISCLOSURE REQUIREMENTS RELATED TO DIRECTOR NOMINATIONS AND SHAREHOLDER COMMUNICATIONS

At an open meeting on 6 August 2003 the United States Securities and Exchange Commission voted to propose rule changes that would strengthen disclosure requirements relating to nomination of directors and shareholder communications with directors. The proposals follow the recommendations made by the Division of Corporation Finance to the Commission in its 15 July "Staff Report: Review of the Proxy Process Regarding the Nomination and Election of Directors."

SEC Chairman William Donaldson said, "These rules are an important first step in improving the proxy process as it relates to the nomination and election of directors. The Commission believes that better information about the way board nominees are identified, evaluated and selected is critical for shareholder understanding of the proxy process regarding nomination and election of directors. We also believe that better information about the processes of shareholder communications with boards lies at the foundation of shareholder understanding of how they can interact with directors and director processes. We intend to continue our work in improving the proxy process by considering later this fall additional important proposals regarding enhanced shareholder access to the proxy process for nomination of directors. These are vital issues in strengthening the proxy process for the benefit of shareholders."

These disclosure proposals represent the first step in the implementation of the recommendations in the Staff Report. The Commission anticipates considering further rule proposals later this fall regarding enhanced shareholder access to companies' proxy statements and forms of proxy for nomination of directors. The Staff Report also discusses possible access proposals.

These proposals would call for important additional information regarding a company's process of nominating directors, including:

- whether a company has a separate nominating committee and, if not, the reasons why it does not and who determines nominees for director;   
- whether members of the nominating committee satisfy independence requirements;  
- a company's process for identifying and evaluating candidates to be nominated as directors;   
- whether a company pays any third party a fee to assist in the process or identifying and evaluating candidates;   
- minimum qualifications and standards that a company seeks for director nominees;   
- whether a company considers candidates for director nominees put forward by shareholders and, if so, its process for considering such candidates; and   
- whether a company has rejected candidates put forward by large long-term institutional shareholders or groups of shareholders.

These proposals also would call for important new information regarding shareholder communications with directors, including:

- whether a company has a process for communications by shareholders to directors and, if not, the reasons why it does not;   
- the procedures for communications by shareholders with directors;   
- whether such communications are screened and, if so, by what process; and   
- whether material actions have been taken as a result of shareholder communications in the last fiscal year.

The proposals would also apply to proxy statements of registered investment companies in the same manner that they apply to other companies.

These proposals are available on the Commission's website at [http://www.sec.gov/](http://www.sec.gov/" \t "_new)

(G) NEW REPORT: DO MULTINATIONAL ENTERPRISES BENEFIT AUSTRALIA?

Australia is failing to reap maximum benefit from foreign investment by multinational enterprises (MNEs), according to a new Committee for Economic Development of Australia (CEDA) report released on 6 August 2003.

The report argues that although foreign investment has played a major role in Australia's economic development, there is significant scope to improve the nature of linkages between MNEs and the domestic economy. Authored by Professor Stephen Nicholas of the University of Sydney, Dr Elizabeth Maitland (University of New South Wales), and Dr Andre Sammartino (University of Melbourne), the report presents the findings of a survey of the performance of 270 foreign-owned firms operating in Australia. The findings have significant implications for understanding the way in which Australia is connected to the global economy.

The report indicates that Australian subsidiaries of MNEs are often poorly integrated into parent global networks with little evidence of Australia acting as a regional headquarters. In addition, relatively few subsidiaries invest in R&D or product innovation in Australia, apply overseas knowledge learning to Australian operations, or engage in production for export markets. Overall there appears to be considerable scope for subsidiaries to link Australia more tightly into their global networks.

However, the good news is that the firms surveyed predicted that by 2006 there will be greater integration with global and regional subsidiary networks, more regional headquarters and greater production for exports.

The report is available on the CEDA website at [http://www.ceda.com.au](http://www.ceda.com.au" \t "_new)

(H) NEW GUIDE TO THE EU FINANCIAL SERVICES ACTION PLAN

On 6 August 2003 the United Kingdom Department of the Treasury, the Financial Services Authority and the Bank of England jointly published a guide to the EU Financial Services Action Plan (FSAP). The FSAP consists of a set of measures intended to achieve a Single Market in financial services across the EU by 2005.

John Healey, Economic Secretary to the Treasury, commented:

"With the Financial Services Action Plan nearing completion, it is essential that all stakeholders should be consulted on, and fully understand, the measures. Together with the Financial Services Authority and the Bank of England, we have prepared this guide so that all those involved are aware of the impact of new measures and the competitive opportunities of further EU financial integration ."

The guide is intended for financial institutions, companies and consumer groups in the UK that are not yet sufficiently familiar with the FSAP's potential impact.

The guide is available on the FSA's website at [http://www.fsa.gov.uk](http://www.fsa.gov.uk" \t "_new)

(I) NEW REPORT PRESENTS INTERNATIONAL PERSPECTIVE ON STRENGTHENING THE FINANCIAL REPORTING PROCESS

"Rebuilding Public Confidence in Financial Reporting: An International Perspective," a report from an independent task force that was commissioned by the International Federation of Accountants (IFAC) and released on 6 August 2003, includes recommendations for strengthening corporate governance, improving audit effectiveness, and raising the standard of regulation of issuers. It also presents an international perspective on the challenges facing not only the accountancy profession, but also those involved in regulating a profession that has such a significant involvement in capital markets worldwide.

"Rebuilding Public Confidence in Financial Reporting" was developed by a Task Force chaired by John Crow, former Governor of the Bank of Canada. It included individuals with backgrounds in commercial banking, international economics, academia and law, as well as accounting and auditing, from six countries: Australia, Canada, France, Japan, the United Kingdom, and the United States.

The report's recommendations are built on three basic assumptions:

- The credibility of financial reporting is both an issue in each country and an  
international issue, with action required at both levels.  
- To improve credibility in financial reporting, action will be necessary at all points in the supply chain that delivers financial information.  
- Integrity - both individual and institutional - is essential for building confidence in financial reporting, and, therefore, needs to be fostered.

"Failure to recognize the fundamental responsibility to report fairly has been a major contributor to the financial scandals of recent years," states John Crow, chair of the Task Force on Rebuilding Confidence in Financial Reporting (Credibility Task Force).

"In crafting our recommendations, we have kept in mind that public reporting is intrinsically a public-interest activity. So, our report addresses the roles of all those who are involved in the process, including groups such as lawyers, bankers, brokers, analysts, and public relations advisors. All parties, besides the management, board of directors, and independent auditors, have an unavoidable duty to ensure that public reporting presents the information fairly, and the rules and regulations surrounding corporate reporting should clearly reinforce them."

Specific recommendations include the following:

- Effective corporate ethics codes need to be in place and actively monitored; such codes should be supported by training.  
- Codes of conduct need to be put in place for other participants in the financial reporting process - such as investment analysts and lawyers - and their compliance should be monitored.  
- Incentives to misstate financial information need to be reduced, and companies must refrain from forecasting profits with an unrealistic level of precision.  
- Audit effectiveness needs to be raised, primarily through greater attention to audit quality control processes.

The members of the International Taskforce were: John Crow (Canada - Chair), Christian Aubin (France), Olivia Kirkley (USA), Kosuke Nakahira (Japan), Ian Ramsay (Australia), Guylaine Saucier (Canada), and Graham Ward (United Kingdom).

The full report and complete list of recommendations can be accessed on IFAC's website at [http://www.ifac.org/credibility](http://www.ifac.org/credibilityq" \t "_new). A database of relevant articles and speeches may also be accessed through this area of the website.

(J) STUDY: INDEPENDENT DIRECTORS SEE SIGNIFICANT CHANGES IN REMUNERATION

America's largest public companies are changing how they compensate non-employee, independent directors, and paying a sharply higher premium for Audit Committee Chairmen. These are the central findings of an analysis published on 4 August 2003 by The Todd Organization of director compensation practices in 2002 and 2001 at 255 large public companies with revenues of at least $5 billion.

At these 255 companies, the average amount of non-employee directors' compensation actually declined slightly, 1.6 percent, to $112,698 in 2002 from $114,490 in 2001. The primary reason for the decline is a 12.1 percent decrease in the average amount of compensation directors received from stock options. The percentage of companies that offered stock options to directors also declined in 2002 to 52 percent (132 of 255 companies), from 57 percent in 2001 (145 of 255 companies).

Non-employee directors' compensation

2001:

Cash - $37,532 - 33%   
Stock - $28,058 - 24%   
Stock Options - $48,900 - 43%   
Total compensation - $114,490 - 100%

2002:

Cash - $36,785 - 33%  
Stock - $32,939 - 29%   
Stock Options - $42,974 - 38%  
Total compensation - $112,698 - 100%

The preceding figures do not include separate board meeting or committee meeting fees that some companies pay to directors.

By contrast, during 2002, directors saw a significant increase, of more than 17.4 percent on average, in more direct forms of stock compensation including outright grants of shares, as well as deferred, restricted, and phantom stock programs. The number of companies compensating directors with more direct forms of stock compensation rose 38.5 percent. In 2002, there were 151, or 59 percent of the 255 companies that offered this compensation, up from 109, or 41 percent of the 255 companies in 2001.

There is also an increase in compensation for independent Audit Committee Chairmen. In 2002, 184 of the 255 companies paid an additional premium averaging $11,499 premium for Audit Committee Chairmen. This premium is a 41 percent increase from the average additional premium of $8,145 that 163 companies paid for non- employee Audit Committee Chairmen in 2001.

The study also found that two-thirds of public companies with revenues of more than $5 billion offer directors compensation deferral plans. A minority of companies also offers retirement plans (13%), charitable gift programs (12%), and matching gift programs (9%) that help bolster directors' philanthropic activities.

(K) ACCC WELCOMES ISSUE OF INSURANCE REPORT

On 4 August 2003 the Australian Competition and Consumer Commission (ACCC) welcomed the Federal Government's issuing of the ACCC's public liability and professional indemnity insurance monitoring report.

The report follows a Federal Government request that the ACCC monitor costs and premiums in public liability and professional indemnity insurance to assess the impact on premiums of measures taken by governments to reduce and contain legal and claims costs. The report is the first in a series of four reports to be produced during the next two years.

"The report shows an improvement in the profitability of both public liability and professional indemnity insurance", ACCC Chairman, Mr Graeme Samuel, said. "Importantly, in a turnaround from recent years, insurers are expected to make an underwriting profit in these classes for the year ending 31 December 2002".

Underwriting profit (where premium income exceeds claims costs and other direct costs attributable to a class of insurance) is just one part of the overall profit picture for a particular class of insurance. This underwriting profit has been secured, in large part, by recent premium increases.

The report found that:

- public liability insurance premiums rose by an average of 19% in 2001 and 44% in 2002; and   
- professional indemnity premiums rose by an average of 31% in 2001 and 36% in 2002.

In the absence of the recent government reforms, insurers expected that premiums for both classes of insurance would have risen between 11% and 20% in 2003. However, with reforms, some insurers expected that in 2003:

- in the case of public liability insurance, claims costs would be reduced by around five per cent and premiums constrained by about three per cent; and   
- in the case of professional indemnity insurance, claims costs would remain the same and there would be no constraint on premiums. This is because claims under professional indemnity policies tend to reflect economic loss rather than personal injury. Most of the law reform to date has focussed on personal injury rather than economic loss. Other insurers considered it too early to try and quantify the impact of government reforms on premiums.

Copies of the report can be obtained at the ACCC website at [http://www.accc.gov.au/](http://www.accc.gov.au/" \t "_new)

(L) STUDY OF 2003 FINANCIAL RESTATEMENTS

On 29 July 2003 Huron Consulting Group released findings regarding financial restatements filed with the US Securities and Exchange Commission (SEC) as of 30 June 2003. For the twelve months ending 30 June 2003, 354 public companies have restated earnings because of accounting errors. Of these, 158 restatements were filed during the first six months of 2003. Problems applying accounting rules, human and system errors and fraudulent behaviour are the three primary causes for accounting errors.

Hurons data regarding financial reporting matters for the twelve months ending 30 June 2003, is included in the report titled "Rebuilding Investor Confidence, Protecting US Capital Markets, The Sarbanes-Oxley Act: The First Year" released by the House Committee on Financial Services. The report from the Committee is available at [http://financialservices.house.gov/](http://financialservices.house.gov/" \t "_new)

Quarterly restatement activity for the four quarters ending 30 June 2003 is: Q3 2002 93; Q4 2002 103; Q1 2003 70; and Q2 2003 88. The number of restatements filed during Q3 and Q4 2002 represent the highest two quarters during the past five years.

In the past twelve months as of 30 June 2003, 22 percent of the restatements were filed by companies with greater than $1 billion in revenue and 44 percent were filed by companies with under $100 million in revenue. During this twelve-month period, revenue recognition, which is defined as instances where a company improperly recognizes revenue from transactions, was the leading cause of restatements.

Huron tracks restatements based on filing date, not announcement date. Some companies announce a restatement, but do not file amended financials due to bankruptcy or delisting. Huron's full analysis of financial reporting matters for the year ending 31 December 2003 will be available in January 2004.

(M) HIH INSTITUTE OF ACCOUNTANTS TASK FORCE

On 29 July 2003 the Institute of Chartered Accountants in Australia (ICAA) accepted recommendations made by its independent HIH Task Force focusing on discipline of members, member support and whistleblowers, following review of the formal HIH Royal Commission report released in April.

The key recommendations in the report cover the following areas:

(1) Professional conduct (discipline) and Institute membership

(a) Start the disciplinary process as soon as evidence of possible misconduct becomes available, so that any members who have forfeited their right to the CA designation because of gross incompetence, dishonesty, or serious negligence have their membership terminated at the earliest possible time.

(b) In the interests of transparency, members names and details of the charges against them to be made public immediately after it is determined there are grounds for disciplinary action, and again at the completion of the disciplinary process.

(2) Member support

(a) Strengthen support processes for members under pressure to act unethically.

(b) Provide guidance in difficult professional circumstances in a secure and confidential setting.

(c) Expand the scope and coverage of the Chartered Accountants Advisory Group, CAAG, (formerly the Members Ethical Counselling Service). CAAG provides secure and confidential support to members under pressure to act unethically.

(3) Whistleblowers

(a) The Institute is to champion legislative change to implement extension of corporate responsibility to provide an acceptable means for whistleblowers to act within the corporation.

(b) Non-executive directors to receive written concerns on issues such as questionable conduct or regulatory standards.

(4) Standards

(a) Support the establishment of a Financial Reporting Panel to review financial statements, as proposed in the Government's Corporate Law Economic Reform Program proposals.

(b) Amend audit standards to require audit firms to classify clients according to risk and to require the audit opinion to be subjected to an effective second partner review.

(5) Institute members as directors

(a) Provide guidelines for members considering Board appointments with ongoing education opportunities for this segment of the membership.

The Report of the HIH Taskforce is available at [http://www.icaa.org.au/news](http://www.icaa.org.au/news" \t "_new)

(N) SEC ANNOUNCES APPROVAL OF SRO RULES ADDRESSING RESEARCH ANALYST CONFLICTS OF INTEREST

On 29 July 2003 the United States Securities and Exchange Commission Chairman William H Donaldson announced the approval of a series of self-regulatory organisation ("SRO") research analyst rules that fulfil the requirements of the Sarbanes-Oxley Act of 2002. The rules approved build on previous regulatory actions and take a number of significant additional steps towards promoting the independence and objectivity of research.

SEC Chairman William H Donaldson said, "Working closely with the New York Stock Exchange and the NASD, the rules approved by the SEC require a critical and necessary separation of research analyst compensation from investment banking. Such conflicts have undermined confidence in our markets, and must stop. This effort will provide participants with clear guidelines for restoring confidence in the integrity of research. I applaud the efforts of all involved in reaching this important milestone."

Specifically, the rules approved separate research analyst compensation from investment banking influence and insulate research analysts from investment banking interests by prohibiting analysts from participating in "pitches" or other communications for the purpose of soliciting investment banking business. They extend quiet periods for all firms involved in offerings and prohibit "booster shot" research reports in and around lock-up expirations. The rules also require enhanced disclosure of compensation arrangements between firms and issuers and client relationships between firms, their affiliates, and issuers.

The rules also require firms to notify their customers in final reports when they are terminating research coverage of covered companies. Analyst independence will be further protected by a rule that prohibits firms from retaliating, or threatening to retaliate, against research analysts who publish research reports or make public appearances that may adversely affect firms' investment banking business. Finally, the rules impose registration, qualification, and continuing education requirements on research analysts.

These rules are the latest among a series of regulatory actions taken during the last year to promote the integrity of research. Most recently, on 28 April 2003, the Commission, the NASD, the NYSE, and the States announced the settlement of enforcement actions against ten of the nation's top securities firms alleging undue influence by investment banking interests on the firms' research. This Global Settlement includes substantial monetary relief and imposes structural reforms that seek to promote analyst independence. Earlier, the Commission approved a series of SRO rule changes addressing analyst conflicts, as well as a Commission rule requiring that analysts certify that their research reports accurately reflect their personal views and disclose whether they received compensation for their specific recommendation.

(O) GMI LAUNCHES GLOBAL GOVERNANCE RATINGS

On 28 July 2003 GovernanceMetrics International (GMI), an independent governance ratings agency, announced ratings on 1600 global companies. Seventeen companies - fifteen US and two Canadian, received scores of 10.0, GMI's highest rating (see below). The rating universe covers 1000 US and 600 non-US companies from a total of fifteen countries.

In the GMI sample, Canadian companies had the highest overall average rating of 7.2 followed closely by the UK, US and Australia, in that order. Companies with overall global ratings of 7.5 or more, which GMI considers above average, are almost exclusively from these four countries. In continental Europe, French companies scored the lowest with an average of 4.1, but the lowest governance performance of all was Japan, where the average rating was 3.5. US companies comprise 62% of the GMI universe and include a number of smaller corporations which skew the country results somewhat. The average rating for the top 100 US companies was 7.7 which is a more accurate comparison with the UK, Canadian and Australian companies in the universe.

Even though US and Canadian firms scored well overall, there are still five companies from these two countries that received a global rating of 3.0 or less, which GMI considers well below average. This indicates that despite a strong legal and regulatory framework, companies can still satisfy basic requirements but represent a governance risk to shareholders. Sixteen companies received GMI's lowest rating of 1.0; of these, ten were Japanese, two were French, two were Dutch, and one Swiss and one American.

The data provided useful insights into differences between industries and markets. The highest scoring industries globally were Utilities (average rating of 7.0), Energy (6.9) and Insurance (6.8). The poorer performers were Construction (4.9), Autos (5.6) and Media (5.8). Not surprisingly, more regulated industries tended to have better governance practices overall, although GMI would have expected Financial Services as a regulated industry to have had better ratings overall than the 6.1 the industry achieved.

Noticeable differences were found in how companies performed in particular categories. In the area of potential dilution, Japanese companies scored well since stock options are generally not a feature of compensation practices in that country. On the other hand, of the 483 companies in the ratings universe with potential options dilution of 15% or more, all but seven were American. In financial disclosure, Japanese and European companies tended to score lower than US, Canadian, UK and Australian companies because of fewer disclosure requirements. In addition, 21% of the companies in the ratings do not report their accounts under US GAAP or International Accounting Standards practices, but under purely local standards. These companies are predominately Japanese and Continental European.

European corporations outperform in the area of broader stakeholder relations. In environmental, labour and social matters, European companies have far better practices and disclosure policies than US companies and consistently score better in this category. This is not surprising given the greater attention to those issues by European investment houses, governments and communities.

Legislative and regulatory initiatives this past year in the US, Europe, Japan and Australia have been designed to strengthen corporate governance practices and produce greater shareholder protection, but GMI's Chief Executive Officer, Gavin Anderson said, "that while compliance with new standards has produced improvement, there are still practices and patterns of behaviour at many companies that cause shareholder concern; among the myriad of questionable practices we found are a chairman and president who were forced to resign because of bid rigging, but have now been re-hired as advisors; directors who sit on as many as fourteen public company boards as well as several committees; one director who collects a $600,000 annual consulting fee on top of his director fees, and one firm that does not designate either executive directors or a CEO and thus regulations relating to directors remuneration do not apply to them. What our ratings help determine is the culture of accountability and integrity at companies. We know from a number of studies that shareholders will pay a premium for companies with good corporate governance."

GMI's rating system incorporates more than 600 data points across seven broad categories of analysis, including board accountability, disclosure, executive compensation, shareholder rights, ownership base, takeover provisions and corporate behaviour and social responsibility.

Companies with a global score of 10 (GMI's highest rating) are:

Alcan Inc (Canada) McDonald's Corporation (US)  
BCE Inc (Canada) Occidental Petroleum Corporation (US)  
ChevronTexaco Corporation (US) PepsiCo, Inc (US)  
Chubb Corporation (US) Pfizer Inc (US)  
Colgate-Palmolive Company (US) Pinnacle west Capital (US)  
E I DuPont de Nemours & Co (US) Praxair Inc. (US)  
Eastman Kodak Company (US) SLM Corporation (US)  
Exxon Mobil Corporation (US) The Allstate Corporation (US)  
Gillette Company (US)

Average Overall Ratings by Country

Country, Number of companies, % of GMI Global Cos, Avg Overall Rating

Canada (3) 301.9% 7.2  
UK (101) 6.3% 7.1  
USA (1002) 62.3% 7.0  
Australia (48) 3.0% 6.9  
Finland (5) 0.3% 6.3  
Germany (30) 1.9% 5.8  
Sweden (29) 1.8% 5.8  
Italy (29) 1.8% 5.3  
Portugal (4) 0.2% 4.3  
Netherlands (24) 1.5% 4.2  
Spain (16) 1.0% 4.2  
Switzerland (26) 1.6% 4.2  
France (39) 2.4% 4.1  
Japan (225) 14.0% 3.5  
Total (1608) 100.0% 6.3

(P) SEC STUDY ON ADOPTION BY THE US FINANCIAL REPORTING SYSTEM OF A PRINCIPLES-BASED ACCOUNTING SYSTEM

On 25 July 2003 the United States Securities and Exchange Commission announced the release of a staff study prepared by the Office of the Chief Accountant and the Office of Economic Analysis on the adoption by the US financial reporting system of a principles-based accounting system. The study was conducted pursuant to the provisions of section 108(d) of the Sarbanes-Oxley Act of 2002. The study has been submitted to the Committee on Banking, Housing, and Urban Affairs of the US Senate and the Committee on Financial Services of the US House of Representatives.

The staff study recommends that accounting standards should be developed using a principles-based approach and that such standards should have the following characteristics:

- be based on an improved and consistently applied conceptual framework;   
- clearly state the accounting objective of the standard;   
- provide sufficient detail and structure so that the standard can be operationalised and applied on a consistent basis;   
- minimise the use of exceptions from the standard; and  
- avoid use of percentage tests ("bright-lines") that allow financial engineers to achieve technical compliance with the standard while evading the intent of the standard.

To distinguish the particular approach taken to implementing principles-based standard setting, the staff labels its approach "objectives-oriented." Fundamental to this approach is that the standards would clearly establish the objectives and the accounting model for the class of transactions, while also providing management and auditors with a framework that is sufficiently detailed for the standards to be operational. The staff concludes in the study that an objectives-oriented approach should ultimately result in more meaningful and informative financial reporting to investors and also would hold management and auditors responsible for ensuring that financial reporting complies with the objectives of the standards.

The staff acknowledges that the FASB has begun the shift to objectives-oriented standard setting and is doing so on a prospective, project-by-project basis. The staff expects that the FASB will continue to move towards objectives-oriented standard setting on a transitional or evolutionary basis. Operationalising an objectives-oriented approach to standard setting in the US requires that the following key steps be taken over time:

- ensure that newly-developed standards articulate the accounting objectives and avoid scope exceptions, bright-lines and excessive detail;   
- address deficiencies and inconsistencies in the conceptual framework;   
- when developing new standards, ensure that they are aligned with an improved conceptual framework;   
- address current standards that are more rules-based;   
- redefine the GAAP hierarchy; and   
- continue efforts on convergence of US, foreign, and international accounting standards.

The full text of the staff study can be found at [http://www.sec.gov/news/studies/principlesbasedstand.htm](http://www.sec.gov/news/studies/principlesbasedstand.htm" \t "_new)

(Q) REPORT: CORPORATE GOVERNANCE AND CLIMATE CHANGE

On 9 July 2003 a report titled 'Corporate Governance and Climate Change: Making the Connection" was published. The report, was commissioned by CERES, a coalition of investor, environmental and public interest groups, and written by the Investor Responsibility Research Center (IRRC), an independent firm that advises institutional investors managing more than $5 trillion in assets.

The report is a study of 20 of the world's largest companies and it is argued in the report that most of America's biggest carbon dioxide-emitting companies are not adequately disclosing the financial risks posed by climate change and also are failing to deal with global warming issues in other key corporate governance areas.

The widest disparity in corporate governance responses to climate change is in the oil industry, according to the study. BP (BP) and Royal Dutch/Shell (RD) have pursued all 14 items listed on the Climate Change Governance Checklist contained in the report, positioning the companies to deal with emerging issues related to climate change, while American-based ChevronTexaco, ConocoPhillips (COP) and ExxonMobil have pursued only four or five actions. The report notes that the US-based oil companies are continuing to devote virtually all development efforts toward fossil fuels, while European competitors are gaining a foothold in renewable energy technologies that are among the fastest-growing energy sources.

The electric power industry as a whole scored lowest on the checklist, despite being the largest source of US emissions and vulnerable to changing clean air regulations. The auto industry failed to measure and disclose the emissions of its products, the source of more than 95 percent of that industry's emissions. At the same time, Japanese competitors are taking the lead in introducing hybrid gas-electric vehicles that substantially reduce tailpipe emissions.

(1) Key findings

(a) Board oversight and shareholder disclosure: The boards of 17 of the profiled companies have discussed climate change, illustrating the growing importance of the issue, yet only 12 of the companies made reference to climate change in their 2001 SEC Form 10-K filings. Just nine mentioned the issue in the front section of their 2001 annual reports.

(b) Executive compensation and management accountability: All 20 profiled companies have environmental links to compensation, and 19 of the 20 companies have their top environmental officer reporting directly to the CEO or one level below. Yet only three of the companies have linked attainment of greenhouse gas targets to executive compensation.

(c) Emissions inventories and reporting: By the end of 2003, all 20 profiled companies will be taking regular greenhouse gas inventories of emissions from their facilities. Yet only 11 companies have set historical emissions baselines (dating back at least 10 years), and only nine companies have made forward-looking emissions projections. Especially lacking are inventories and projections of product and other end-use emissions, the major share of worldwide emissions.

(d) Product development and renewable energy: Seventeen of the profiled companies are purchasing and/or developing renewable energy sources that do not emit greenhouse gases. However, the commitments and investments made by most of these companies still account for only a tiny fraction of their total energy budgets. Greater progress is being made in terms of improving the energy efficiency of manufacturing.

- Independent directors: New governance listing standards require corporations to have a majority of independent directors, while the SEC is considering new rules allowing shareholders to nominate their own board candidates, clearing the way for nomination of directors who understand the issue and would take steps to address it.

- Executive compensation: Emerging efforts to redefine "pay for performance" - and align executive performance with long-term investor value - make attainment of greenhouse gas targets a logical addition to many executive compensation plans.  
Proxy voting: New SEC rules require mutual funds to disclose their proxy guidelines and proxy votes, opening them to scrutiny and client pressure to support global warming related shareholder resolutions.

- Investment research: A legal settlement involving major US investment banks is putting greater separation between banks' brokerage and underwriting arms, giving analysts more leeway to conduct critical analyses of companies' responses to climate change.

- Potential liability: As a sign of growing legal and economic concerns about how companies respond to global warming, the giant Swiss Re reinsurance company has begun asking companies applying for directors and officers liability insurance whether they have developed a strategy for addressing the issue.

(2) Report recommendations

(a) Investors:

- Encourage best practice among portfolio companies, including the 14 actions on the "Climate Change  
Governance Checklist."   
- Seek expert science and policy advice on climate change and discuss climate change risks and opportunities with fund managers and trustees.  
- Join in discussions with other investors concerned about climate change risks and opportunities, through CERES, IRRC, and other organizations.  
- Support requests for greater disclosure of climate change risks and opportunities by portfolio companies,  
including taking steps such as: voting proxies in favour of climate change shareholder resolutions and disclosing those votes publicly, communicating with companies and sponsoring shareholder resolutions.  
- Undertake a portfolio-wide assessment of climate change risk exposures, and have portfolio managers integrate climate change considerations into investment policies and strategies.  
- Identify and pursue clean energy investment opportunities that are advancing the transition to a  
low-carbon economy.  
- Ask stock exchanges to include disclosure of climate change risk in their listing standards.  
- Support recommendations for corporate boards/CEOs, Congress, SEC.

(b) Corporate Boards/CEOs:

- Ensure that the board has sufficient expertise and counsel to make informed and responsible decisions regarding climate change.  
- Consider taking the 14 actions on the Climate Change Governance Checklist and report to shareholders regularly on company progress.  
- Develop, announce and implement an explicit strategy on climate change that is integrated into the company's overall business strategy.  
- Support climate change policy solutions.

(c) Policymakers:

- SEC: Enforce regulations that require companies to disclose material financial risks and opportunities related to climate change and regulation of greenhouse gases, and companies' strategies for addressing these risks and opportunities.  
- Congress: Develop national policies to limit US greenhouse gas emissions to create certainty for companies and investors, including, among others policies and measures,

(i) a national mandatory program that is marketbased, with reduction targets and timetables for large-emitting sectors, and

(ii) a national renewable energy standard requiring an increasing amount of electricity produced from renewable resources such as biomass, geothermal, solar and wind.

The report is available on the IRRC website at [http://www.irrc.org](http://www.irrc.org" \t "_new)

2. RECENT ASIC DEVELOPMENTS

(A) RETIREMENT OF ASIC CHAIRMAN

On 12 August 2003 the Chairman ASIC, Mr David Knott, informed the Commonwealth Treasurer, the Hon Mr Peter Costello MP that he will step down from the position at the end of 2003.

The Treasurer stated that Mr Knott has been a highly successful member of ASIC over the past four years. He was appointed as ASIC Deputy Chair in July 1999 and was appointed as ASIC Chairman in November 2000.

Under David Knott's leadership, ASIC has proven to be highly effective. Action taken by ASIC over the last 3 years has resulted in the jailing of 70 people, the removal of 40 company directors from office and over $1 billion of funds protected, recovered or ordered in compensation.

According to the Treasurer, Mr Knott's commitment to the timely and vigorous enforcement of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) has succeeded in better protecting Australian consumers and promoting best corporate practice amongst Australian business.

(B) ASIC CLASS ORDER EXEMPTS ISSUERS OF CERTAIN DOCUMENTS FROM REQUIREMENT TO HOLD AN AFSL

On 6 August 2003 ASIC released a new Class Order exemption, [CO 03/606], relating to the requirement to hold an Australian financial services licence (AFSL) for the provision or giving of financial product advice in certain documents.

The Class Order relief exempts a person from the requirement to hold an AFSL for the provision of financial product advice where that advice is general advice, and the advice is contained in a document that is required by, and prepared by the person as a result of a requirement in the [Corporations Act 2001](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) (the Act) or the [Superannuation Industry (Supervision) Act 1993](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=6785" \t "default).

The relief has been provided using ASIC's general licensing relief power under section 911A(2)(l), relating to the need for an Australian Financial Services Licence, rather than specific legislative provisions regarding exempt documents.

The Class Order relief applies to the following documents or statements:

- a statement setting out information about a reduction in share capital of the kind referred to in subsection 256C(4) of the Act; or  
- a statement setting out information about a share buy-back of the kind referred to in subsections 257C(2) or 257D(2) or section 257G of the Act; or  
- a statement setting out information about financial assistance given by a company to a person to acquire shares of the kind referred to in subsection 260B(4) of the Act; or  
- a financial report; or  
- an explanatory statement about a compromise or arrangement of the kind referred to in section 412 of the Act or a draft of such a statement of the kind referred to in subsection 411(3) of the Act; or  
- a bidder's statement, a supplementary bidder's statement, a target's statement or a supplementary target's statement; or  
- a document setting out information about a proposed acquisition of shares of the kind referred to in item 7 of the table in section 611 of the Act; or  
- a continuous disclosure notice; or  
- a disclosure document; or  
- a supplementary or replacement document of a kind referred to in section 719 of the Act; or  
- a document setting out information given to members of superannuation funds and others under Part 2 of the [Superannuation Industry (Supervision) Regulations 1994](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=8413" \t "default) (SIS Regs); or  
- a document setting out information about investment strategies of the kind referred to in paragraph 4.02(2)(b) of the SIS Regs.

A copy of the Class Order can be obtained from the ASIC's Infoline by calling 1300 300 630 or from the ASIC website at [http://www.asic.gov.au](http://www.asic.gov.au" \t "_new)

(C) ASIC RELEASES FEE DISCLOSURE MODEL

On 5 August 2003 ASIC released a good practice model for fee disclosure in the Product Disclosure Statements (PDSs) of investment products.

'Investors have a right to clear, concise, and comprehensive information about the fees they will pay for an investment product', ASIC Executive Director, Financial Services Regulation, Mr Ian Johnston said.

'ASIC believes that significant fees should be disclosed in a single table which investors can read easily "at a glance". Used consistently by providers, this sort of table will help people understand their fees, and help them to compare fees across different products', Mr Johnston said.

ASIC suggests that a second table should itemise ongoing fees, and be supplemented by a section for other important additional disclosure items such as worked examples, information about adviser remuneration and information about fee changes.

'Improving fee disclosure is an ongoing process, and our good practice model is an important foundation of that process. While we acknowledge that it will take time to make the transition to using it consistently, we encourage industry to adopt it as soon as possible', Mr Johnston said.

The development of a fee disclosure model follows the release in September 2002 of Professor Ian Ramsay's report Disclosure of Fees and Charges in Managed Funds, which was commissioned by ASIC. Professor Ramsay is Dean of the Law School at Melbourne University, and Director of the Centre for Corporate Law and Securities Regulation.

'ASIC has prepared this report using Professor Ramsay's recommendations as a basis, and we believe it is the best example that can be achieved through a consensus-based approach. In the absence of specific legislation regarding a comparability tool such as an MER or OMC\*, ASIC encourages industry to do further work on these issues and is happy to be involved in the process', Mr Johnston said.

ASIC's model aims to address issues identified in the report as requiring attention, such as:

- the use of common terms;   
- standardised descriptions;   
- disclosure of the purpose of particular fees;   
- improved disclosure of adviser remuneration; and   
- transparency of fees.

ASIC recommends that industry participants undertake consumer testing of the model, as suggested by Professor Ramsay.

The fee disclosure model appears as Appendix A to ASIC's report on the fee disclosure project. The report outlines the approach taken in developing the model, the consensus reached and potential areas for further development as industry standards.

The model was developed following extensive consultation with industry stakeholders over more than six months.

ASIC consulted stakeholders including:

- the Investment and Financial Services Association Ltd (IFSA);   
- the Association of Superannuation Funds of Australia Ltd (ASFA);   
- the Australian Consumers Association (ACA);   
- the Industry Funds Forum (IFF);   
- the Australian Institute of Superannuation Trustees (AIST);   
- the Corporate Superannuation Association (CSA);   
- the Institute of Actuaries;  
- the Australian Investors Association (AIA);   
- the Australian Friendly Societies Association (AFSA); and   
- Mr Colin Grenfell.

'We have consulted widely in reaching a position on consistent disclosure of fees and charges. Consumer groups, industry bodies and professional experts have all made a valuable contribution to the process, and I would like to acknowledge the cooperation we have received', Mr Ian Johnston said.

A copy of the report is available from ASIC's website at [http://www.asic.gov.au](http://www.asic.gov.au" \t "_new)

(D) 440 LISTED ENTITIES TO BE REVIEWED BY ASIC

On 4 August 2003 ASIC announced details of its financial reporting surveillance program for 2003-2004.

'ASIC will review the financial reports of 440 publicly listed Australian entities for their compliance with accounting standards', ASIC Chief Accountant, Mr Greg Pound said. 'ASIC is committed to regular and comprehensive surveillance of financial reporting, and every listed entity can expect to have their financial reports reviewed at least once every four years', Mr Pound said.

ASIC will select the companies by a combination of random sample and risk-based selection, including those who receive a qualified audit report for non-compliance with an accounting standard.

(1) Continuous monitoring

The review will cover compliance with all accounting standards, but will be constantly monitored to respond to market circumstances and any indications of inappropriate reporting trends.

(2) Board and auditor accountability

The program reinforces the legal responsibility of Boards to ensure compliance with accounting standards. Performance in this area is being monitored, and blatant abuse of the requirements will be liable for enforcement action. The surveillance program will also result in an increased focus on auditor compliance.

(3) Valuation of options

ASIC has recently issued Guidelines (MR 03/147) about the way listed companies should include values of options when disclosing emolument in directors' reports. ASIC has already announced a specific review of the directors' report for all listed companies, relating to disclosure of the value of options granted to each director and each of the five highest-remunerated executive officers.

Enforcement action will be considered against companies or directors where full remuneration including option values has not been disclosed.

For further information contact:

Greg Pound  
Chief Accountant  
ASIC  
Tel: (03) 9280 3309  
Mobile: 0413 050 353

(E) ASIC RELEASES SURVEILLANCE REPORT ON RESEARCH ANALYST INDEPENDENCE

On 22 August 2003 ASIC released the findings of its industry surveillance review examining the independence of research analysts within the investment banking industry. The review was established to consider the extent to which investment banks identify and manage 'conflicts of interest'. This issue has generated debate both domestically and overseas, primarily in the United States (US).

In conducting this project, ASIC reviewed the practices and activities of research analysts in Australia, the standards of conduct and supervision of research analysts, and the effect of current regulatory requirements.

'The review indicates that Australia is unlikely to have experienced the extent and seriousness of misconduct that occurred in the United States. This is also consistent with the position found to exist in the United Kingdom by the Financial Services Authority', ASIC Executive Director of Financial Services Regulation, Mr Ian Johnston said.

'ASIC emphasises that the review was conduced as a surveillance campaign rather than an investigation, because no breaches of the law have been detected. While none of the findings in the report are indicative of breaches of the law, ASIC cannot say that the industry is without flaw or is immune from misconduct, because its review was necessarily limited to a sample selection of entities and a limited period of time.

'However, the review has identified a number of compliance issues that require further improvement, particularly relating to the independence of research analysts and the processes for managing conflicts of interest when they are identified.

'Our findings will form the basis for our policy proposal paper on managing conflicts of interest. These policy initiatives will further support the legislative reforms introduced through the Federal Government's CLERP 9 Bill, and the statement of principles currently being prepared by the International Organization of Securities Commissions (IOSCO), of which ASIC is a member', Mr Johnston said.

(1) Surveillance methodology

In undertaking the review, ASIC has sought to determine whether conflicts of interest are being adequately identified and managed, and whether the processes and systems currently in place effectively protect the independence of the research analyst function.

The project was carried out in two stages. The first stage was a high-level review of the research practices of eight investment banks, comprising three US, three European and two Australian investment banks. Four of these entities were selected for closer examination in the second stage of the review. The review was conducted in an environment of enhanced compliance procedures, following on from the implementation of regulatory changes in the United States and internationally. The positive impact of these compliance enhancements was observed between the first and second stages of the project, but may also be attributable to ASIC's publicised campaign, proposals by the Australian Stock Exchange (ASX) and the Federal Government's CLERP 9 reform agenda. ASIC was pleased with the level of co-operation it received both from the entities it reviewed, as well as their representative associations.

(2) Report findings

The review identified some particular compliance deficiencies relating to the management and disclosure of conflicts of interest within the investment banking industry in Australia. While these deficiencies are not systemic in nature, ASIC was concerned to find that some of the entities it reviewed had failed to implement adequate conflict management procedures, and placed an unreasonable level of reliance on their staff to identify, and then manage and disclose conflicts of interests. In particular, while many of the entities reviewed had some form of conflicts management procedure, most failed to fully and effectively implement, monitor and enforce them.

ASIC's review also suggested that the industry guidelines developed by the Securities and Derivatives Industry Association (SDIA) and the Securities Institute of Australia (SIA) have not been adopted as closely as intended. ASIC considers that there is still a risk that conflicts of interest will occur and will remain unmanaged. Even if fully implemented, ASIC does not believe that these industry guidelines adequately address the deficiencies identified in this report.

'There are some clear opportunities for improving the current practices to ensure conflicts are either avoided, or in circumstances where they cannot be avoided, appropriately disclosed and effectively managed', Mr Johnston said.

It is important that any policy or regulatory changes introduced domestically are consistent with international regulations, and represent a "best practice", principles-based approach.

'ASIC will undertake extensive consultation with government, industry and other regulators\* in order to develop an appropriate policy response based on the findings of this report. We anticipate that a policy proposal paper will set out high-level principles and guidance for Australian Financial Services (AFS) licensees generally about managing conflicts of interest, with more detailed guidance for providers of research reports. 'The paper will also provide guidance about what ASIC would expect of AFS licensees in complying with their obligations for managing conflicts of interest.

'The paper will address a request by the Federal Government to develop policy in response to a new conflicts management obligation on all AFS licensees that the Government proposes to introduce as part of the CLERP 9 law reform', Mr Johnston said.

ASIC expects to release the draft policy proposal paper soon after the introduction of draft legislation for CLERP 9.

\* ASIC acknowledges the assistance of the market regulatory authorities, the Australian Stock Exchange, and the Sydney Futures Exchanges, as well as the relevant industry associations, the Securities Institute of Australia, the Securities and Derivatives Industry Association, the Australian Banking Association, the Investment and Financial Services Association, and the International Banks and Securities Association, in undertaking this project.

For further information contact:  
Sean Hughes  
Director FSR Regulatory Operations  
Telephone: 03 9280 3646  
Mobile: 0411 549 026

(F) SUPERANNUATION SPONSORS

On 21 August 2003 ASIC announced a supplementary component to its annual financial report surveillance programme. Listed companies will have their financial reports reviewed for the disclosures required by Accounting Standard AASB 1028 'Employee Entitlements', in order to identify companies that are corporate sponsors of an employee defined benefit superannuation or pension plan(s).

ASIC will then assess the company's accounting policy applied to the deficit of that plan(s), for compliance with current accounting standards.

'Corporate sponsors must report their legal obligations for any liabilities that arise from a deficit in the defined benefit superannuation plans for their employees', ASIC Chief Accountant, Mr Greg Pound said.

'ASIC is aware that some sponsors believe that companies can choose to either recognise a liability in the financial statements or make the required disclosures in the notes to the financial report, on the grounds that AASB 1028 does not specifically require recognition of such liabilities.

'However, ASIC's view is that accounting standards in general, and relevant and reliable financial reporting, require the recognition of all legal liabilities. A liability arising from a deficit of a corporate sponsored defined benefit superannuation plan should be treated the same as any other liability under current accounting standards', Mr Pound said.

ASIC expects that each company which is the corporate sponsor of an employee defined benefit superannuation or pension plan(s) to carefully assess its individual arrangements and circumstances to determine whether it has a legal obligation for any deficit of the plan(s), including any in relation to an overseas subsidiary.

A liability should be recognised when the deficit is evidenced by :  
- an actuarial review in relation to a funding and insolvency certificate under the  
SIS regulations;  
- a legal obligation arising from the plan trust deed; or  
- employment contracts or other legal arrangements that establish the existence  
and amount of a liability.

In other circumstances the company should assess whether there is a contingent liability that needs to be disclosed. In some cases a company with a deficit in a plan will not need to recognise a liability if the specific circumstances surrounding the relationship of the company and the plan, and any legislative requirements, do not create a liability to the company.

'AASB 1028 requires disclosure of the accounting policy applied - so, if a company believes that it does not have a legal liability which should be recognised in its financial statements for a deficit in a plan, the reasons for this accounting policy and for the company not recognising the deficit must be disclosed', Mr Pound said.

'If disclosure under AASB 1028 is not clear about the specific circumstances for the accounting policy applied, or if it suggests that a legal liability has not been recognised, ASIC may seek further information from the company', Mr Pound said.

'Companies should be aware that if an issue is not satisfactorily resolved as a result of further ASIC enquiries, ASIC may take enforcement action', Mr Pound said.

ASIC's announcement is an elaboration of the announcement by ASIC in April 2003. At that time ASIC stated that in conjunction with Corporate Superannuation Association Inc (CSA), it would survey CSA members in relation to financial reporting related matters by sponsoring corporate employers.

The results of the survey can be found at [www.asic.gov.au](http://www.law.unimelb.edu.au/bulletins/www.asic.gov.au" \t "_new).  
For further information contact:

Greg Pound  
Chief Accountant  
Telephone: 03 9280 3309  
Mobile: 0413 050 353

3. RECENT TAKEOVERS PANEL MATTERS

(A) RESOLUTION OF PROCEEDINGS RELATING TO BREAKFREE LIMITED

On 14 August 2003 the Takeovers Panel advised that the proceedings (the proceedings) arising from the application (the Application) made by S8 Limited (S8) on 11 July 2003 in relation to the affairs of BreakFree Limited (BreakFree) have been resolved. The Proceedings were resolved following the termination by BreakFree on 12 August 2003 of certain agreements as contemplated by undertakings voluntarily provided by it to the Panel.

(1) Allegations concerning the Franchising Transactions

(a) The Franchising Transactions

S8 alleged that BreakFree's entry into certain sale and franchise transactions (the Franchising Transactions) amounted to unacceptable circumstances in accordance with the Panel's frustrating action guidance note because they could frustrate S8's announced takeover bid for BreakFree (S8 Bid).

The Franchising Transactions involved the sale by BreakFree of the management rights (Management Rights) to four of the holiday properties under its management. Each of the sales was subject to a condition precedent that the purchasers (the Franchisees) enter into a franchise agreement (together the Franchise Agreements) with BreakFree in relation to the Management Rights so that the relevant properties would continue to be operated under a BreakFree franchise.

After considering a number of submissions from the parties, the Panel decided that the following aspects of the Franchising Transactions required further investigation before the Proceedings could be determined:

(i) BreakFree's intention to include a right in the Franchise Agreements (which were still being negotiated during the Proceedings) which could result in the Management Rights being alienated by BreakFree without it retaining the benefit of the Franchise Agreements if the S8 Bid succeeded. BreakFree submitted to the Panel that the value of the Franchise Agreements had been a factor in determining the sale price for the Management Rights; and

(ii) the question of whether the Franchising Transactions were entered into in the ordinary course of BreakFree's business, and were arms length transactions.

The Panel requested that the parties provide it with further additional information in relation to these aspects.

(b) The resolution of the proceedings

Whilst indicating that it could, and would (if necessary), provide the additional information requested by the Panel, BreakFree responded by making a proposal which it believed would remove the need for further investigation of the matters identified by the Panel. BreakFree's proposal (which was provided voluntarily) was that it would provide undertakings to the Panel to use its best endeavours to terminate the Franchising Transactions within a timeframe set by the Panel.

BreakFree advised the Panel that it was proposing the resolution because of the additional time, costs and resources that would be required if the Proceedings were to continue, particularly in order to provide the additional information requested by the Panel. BreakFree was also concerned about the fact that the Panel's request for further information could result in the provision of confidential information of BreakFree to S8 (which is a competitor of BreakFree).

The Panel decided that if the Franchising Transactions were terminated there would be no need for it to conduct any further investigation, or to obtain any further information from the parties. Therefore, the Panel accepted the undertakings volunteered by BreakFree.

As contemplated by the undertakings, BreakFree terminated the Franchising Transactions (without any liability to, or obligation of, BreakFree arising as a result of those terminations) on 12 August 2003.

(2) Other allegations in the proceedings

The Panel decided that if there were any misleading aspects of BreakFree's announcements in relation to the properties under its management, they were resolved by BreakFree's ASX announcement of 18 July 2003.

The Panel did not conduct proceedings in relation to the allegations made by S8 concerning the acquisition of certain shares in BreakFree.

(3) Conclusion of the proceedings

In concluding this matter, the sitting Panel stressed the need for transactions which are entered into in the context of a takeover bid to comply with the letter and spirit of relevant Panel policies and to be fully and promptly disclosed to the market.

The Panel concluded the proceedings on the basis set out above. The Panel will post its full reasons for this decision on its website at [http://www.takeovers.gov.au/](http://www.takeovers.gov.au/" \t "_new) when they have been settled.

The sitting Panel for the proceedings was Kathleen Farrell (sitting President), Peter Cameron (sitting deputy President) and Meredith Hellicar.

(B) PANEL DECLINES APPLICATION FOR A DECLARATION OF UNACCEPTABLE CIRCUMSTANCES IN RELATION TO POWERTEL LTD (NO 3)

On 8 August 2003 the Takeovers Panel declined the application by the Roslyndale syndicate for a declaration of unacceptable circumstances and orders regarding the current bid by TVG for all of the ordinary shares in PowerTel Ltd.

PowerTel has two major shareholders, WilTel Communications Group (WilTel) and DownTown Utilities (DTU). WilTel holds 33% of the ordinary shares and also holds preference shares which WilTel may convert into ordinary shares, after which WilTel would hold 47% of the ordinary shares. WilTel is also owed $24 million by PowerTel. DTU holds 35% of the issued ordinary shares.

(1) TVG's Bid for PowerTel

On 3 July 2003, TVG Consolidation Holdings SPRL (TVG) made a bid to acquire all of the ordinary shares in PowerTel for 3.85 cents each. On Friday 25 July, the bid was conditional on TVG receiving 47% acceptances and on WilTel converting its preference shares into ordinary shares and selling the debt owed to it by PowerTel to TVG for $1 (the Debt Condition).

On 25 July, WilTel made an irrevocable offer to PowerTel to release the debt for a payment of $10 million by PowerTel to WilTel, on condition that TVG waive the Debt Condition and accelerate payment for acceptances under the bid. On 26 July, TVG waived the Debt Condition and announced that it would accelerate payment for acceptances.

(2) Roslyndale's application

The application related to the effect on TVG's bid of the waiver of the Debt Condition. Roslyndale argued that by waiving the condition, TVG gave WilTel a benefit which was not offered or given to any other holder of ordinary shares in TVG, and which was likely to induce WilTel to accept its bid, leading to unacceptable circumstances.

Roslyndale's application was based on the submission that the waiver was a breach of section 623 of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default). That section relevantly prohibits a bidder from giving a benefit to some offeree shareholders and not to all of them, if the benefit is likely to induce the offeree shareholders to whom it is given to accept the bid.

Whether or not such a breach occurred, it could have led to unacceptable circumstances, if offeree shareholders did not all have an opportunity to share in a benefit which TVG gave to WilTel in connection with its bid, contrary to the principle in paragraph 602(c) of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default), that all holders of shares in the class for which a takeover bid is made should have reasonable and equal opportunities to participate in the benefits received under the bid by any shareholder in that class.

(3) The decision

The Panel rejected a central part of these submissions, namely that the waiver resulted in WilTel receiving a benefit which was not available to other ordinary shareholders. Roslyndale submitted that the waiver of the condition was a benefit to WilTel, because it enabled WilTel to accept TVG's bid for its shares in PowerTel, without prejudicing its ability to deal with its other assets (relevantly, the debt owed by PowerTel to WilTel). Because there was no condition affecting any other shareholder in a similar way, no other shareholder was given a comparable benefit.

The Panel decided that that for a shareholder to be able to accept the bid for their shares and also deal with their other assets is a benefit which WilTel shares with all other ordinary shareholders in PowerTel (if it is properly a benefit at all), because the terms of the bid do not restrain any other shareholder from dealing with their assets other than PowerTel shares.

Rather than giving WilTel a benefit, the waiver in effect removed a detriment which TVG's original bid had sought to impose on WilTel, restoring equality between WilTel and all other shareholders in accessing the benefits under the bid.

(4) The price of the debt

The Panel also considered whether WilTel would receive a benefit in which other shareholders could not share if, as seems likely, the successful close of the bid would be followed by the repayment of the WilTel debt for $10 million. Roslyndale did not submit that the WilTel debt was worth less than $10 million, or that TVG had offered or agreed to give WilTel a benefit by arranging for PowerTel to buy the debt for $10 million. Other parties provided evidence that the value of the debt, in a transaction such as TVG's bid, is not less than $10 million.

In reliance on that evidence, the Panel decided that there was no basis for a conclusion that even if the WilTel debt was repaid for $10 million, WilTel would receive a net benefit in which other shareholders cannot share ie that the $10 million WilTel would receive for the debt would exceed the value of the debt accepted by the parties.

The sitting Panel was Teresa Handicott (sitting President), Chris Photakis (sitting Deputy President) and Carol Buys.

4. RECENT CORPORATE LAW DECISIONS

(A) EXTENDING LIMITATION PERIOD FOR RECOVERY OF PREFERENCES

(By Charlie Grover, Mallesons Stephen Jaques)

Greig & Duff as Liquidators of Australian Building Industries P/L (in liq) v Australian Building Industries P/L (in liq); Greig & Duff as Liquidators of Australian Building Industries P/L (in liq) v Stramit Corporation P/L [2003] QCA 298, Supreme Court of Queensland, Court of Appeal, Williams and Jerrard JJA and Fryberg J, 18 July 2003

The full text of the judgment is available at [http://cclsr.law.unimelb.edu.au/judgments/states/qld/2003/july/2003qca298.htm](http://cclsr.law.unimelb.edu.au/judgments/states/qld/2003/july/2003qca298.htm" \t "_new)

(1) Introduction

Greig and Duff were liquidators of Australian Building Industries Pty Ltd (ABI). Stramit Corporation Pty Ltd (Stramit) was a significant supplier of ABI. The liquidators claimed that ABI had made preferential payments to Stramit in 1997, and sought to recover $1,426,655.72 from Stramit pursuant to section 558FF of the Corporations Law. However, the statutory limit of 3 years within which preferential payments could be recovered under section 588FF(3) had expired by the time the liquidators instituted the proceedings.

(2) Background

This case effectively concerned three appeals - one by the liquidators and two by Stramit.

On 7 September 2000, Mullins J granted the liquidators an ex-parte order to extend time within which application may be brought (to 11 September 2001). On Stramit's application, this order was set aside by Chesterman J on 16 May 2002 "in so far as it applies to Stramit Corporation Ltd" on the ground of denial of natural justice, since Stramit had not been given notice of the proceedings. The liquidators appealed to the full court, seeking to effectively reinstate Mullins J's order (Appeal 1).

The liquidators successfully sought orders joining Stramit to the proceedings which extended the time within which an application under section 588FF(1) could be brought, and a consequential order extending time for commencing proceedings against Stramit pursuant to section 588(3)(b). Stramit appealed to the full court (Appeal 2).

On 10 September 2001 the liquidators commenced an action pursuant to section 588FF(1) to recover ABI's alleged preference payments to Stramit. On 23 May 2002, Stramit applied to summarily dismiss the claim. Mullins J dismissed Stramit's application, from which Stramit appealed to the full court (Appeal 3).

(3) The decision

(a) Appeal 1

Failure to give notice - mere procedural irregularity?

The liquidators argued that section 1322(2) of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) (then the Corporations Law) cured the procedural irregularity of failing to give notice. There was no substantial injustice caused by the order extending time which could not be remedied by the court. The full court held that:  
"there is more than a mere procedural irregularity where a party has been denied a hearing. But even if denying an affected party a right to be heard does constitute a "procedural irregularity" for the purposes of s1322, then the authorities referred to [Cameron v Cole and Craig v Kanssen] would clearly establish that such irregularity had caused "substantial injustice".

No loss of existing vested rights?

The liquidators also argued that Stramit did not lose any vested right (as a result of the order extending the limitation period) until an action was actually brought (therefore there was no denial of natural justice). The full court held that Stramit's existing right to rely on the limitation period defence was lost once the order extending time was effective.

Which creditors must be given notice?

The liquidators argued that it is inequitable to give notice only to creditors who have been sufficiently identified. If notice is required at all, it should be given to all creditors from whom recovery might be sought, which would be impracticable. Therefore, in fairness, no notice should be given to anyone. The full court held that any creditor sued outside the 3 year limitation period must have been made a party to the application for an order extending time.

Undue delay?

The liquidators argued that the court should not exercise its discretion to set aside Mullins J's order extending time because Stramit had unduly delayed its application. The full court held that delay is not a bar to setting aside an order in the absence of due notice, or where the person affected by the order was not given a reasonable opportunity to appear and present his case.

Other exemption pursuant to section 588FF(3)?

Williams JA (in dicta) and Jerrard JA found that section 588FF(3) does not authorise ex parte applications without any identification of persons against whom an application may ultimately be made for an order in section 588FF(1)(a)-(j). Therefore, at least as a general rule, the court has no power to grant a blanket exemption of time pursuant to section 588FF(3) on an ex parte application.

(b) Second Appeal

Section 81 of the [Supreme Court of Queensland Act 1991 No. 68 (Qld)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=12829" \t "default) provides that a new party may be added to the proceedings despite the expired limitation period. The full court distinguished between an application to amend an existing cause of action commenced within the time limit, by adding new causes of action against an existing defendant, and an application to amend an application for an extension of time to add a new party outside of three year time period. The latter type of amendment (as in the present case) was held to be outside the scope of section 81. The full court also held that there is no general power to make an order extending time limit under section 588FF(3) relying on section 1322(4)(d) of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default).

(c) Third appeal

Since the liquidators ultimately were unable to extend the time, Stramit had a valid (limitation period) defence to recovery of preferential payments and was given a judgment in its favour.

(B) EFFECT ON TRUSTS OF LIQUIDATION OF TRUSTEE COMPANIES AND CLAIMS BY PERSONS CLAIMING TO BE TRUSTEES

(By David Felman, Freehills)

Chalker v Barwon Coast Committee of Management Incorporated and the State of Victoria [2003] VSC 286, Supreme Court of Victoria, Gillard, J, 7 August 2003

The full text of the judgment is available at:

[http://cclsr.law.unimelb.edu.au/judgments/states/vic/2003/august/2003vsc286.htm](http://cclsr.law.unimelb.edu.au/judgments/states/vic/2003/august/2003vsc286.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)

(1) Introduction

This was an appeal from a Master of the Court, who on 2 April 2003, ordered that the proceeding be forever stayed on the ground that the proceeding was brought by plaintiffs who had no authority or capacity to bring the proceeding.

(2) Facts

In 1994, the plaintiffs, Messrs Chalker, were interested in leasing premises from Barwon Coast Committee of Management (the "first defendant") and the State of Victoria (the "second defendant") to conduct a restaurant on the foreshore at Ocean Grove.

Mr Chalker Senior established a unit trust as the vehicle to lease the premises and operate the business. On 26 August 1994, a deed was executed by a company called Chalky's on the Dunes Pty Ltd ("Unit Trust Trustee") as trustee of the Chalky's in the Dunes Unit Trust ("Unit Trust"). Caveron Pty Ltd also executed the deed in its capacity as trustee of the Chalker Family Trust. Caveron Pty Ltd, in its capacity as trustee of the Chalker Family Trust, held all the units in the Unit Trust. The Chalker Family Trust was a typical discretionary family trust. The plaintiffs were discretionary beneficiaries.

The Unit Trust Trustee executed the lease. However, by April 1996, there was a dispute with the landlord and rent was in arrears. In April 1996, a notice to quit was served on the Unit Trust Trustee and the lease was terminated. On 22 July 1996, an administrator was appointed to the Unit Trust Trustee and on 22 August 1996, a liquidator was appointed. The company was de-registered on 22 November 2000 pursuant to the Corporations Law.

On 29 January 2001, the plaintiffs, Messrs Chalker, instituted proceedings against the defendants. They purported to bring the proceedings on their own behalf and also as trustees on behalf of the Unit Trust. Subsequently, they abandoned the claim in their own name. It was common ground between the parties that Messrs Chalker were not the trustees of the Unit Trust on 29 January 2001.

On 23 December 2002, a meeting was held of Caveron Pty Ltd which claimed to be the sole unit holder and beneficiary of the unit trust. It resolved to appoint the two plaintiffs as trustees of the Unit Trust. In addition, the plaintiffs in their capacity as the new trustees of the Unit Trust purported to ratify the proceedings.

(3) The defendants' contention

The defendants contended that at the time when the proceeding was instituted, the plaintiffs were not trustees of the Unit Trust, were not authorised by the Unit Trust or its trustees to bring the proceeding and therefore lacked capacity to do so. Accordingly, the defendants argued that the proceeding was a nullity and any purported ratification was ineffective.

(4) Who was the trustee of the Unit Trust?

Gillard J analysed who was the trustee of the Unit Trust at the following relevant dates.

(a) At the inception of the lease

His Honour found that Chalky's on the Dunes Pty Ltd was trustee of the trust from its inception and it entered into the lease.

(b) Upon appointment of the liquidator

Gillard J then analysed what effect, if any, the appointments of the administrator and subsequently the liquidator, had upon the trustee. In particular, the Court was concerned with the effect on the legal estate held by the trustee on behalf of the Unit Trust.

Clause 19.2 of the Trust Deed provided that:

"If the Trustee goes into liquidation or ceases to carry on business… the Trustee shall forthwith give notice in writing to all Unit holders of that entry into liquidation… and shall convene a meeting of unit holders. The Trustee shall be deemed to have resigned effective on that date of such liquidation… and by Special Resolution at a meeting of Unit holders a new Trustee shall be appointed."

The plaintiffs argued, based on clause 19.2 of the Trust Deed, that the Trustee was deemed to have resigned upon the appointment of the liquidator. Gillard J rejected this argument. His Honour held that clause 19.2 "provides the machinery whereby a trustee is deemed to have resigned but only after notice is given and a meeting of unit holders by special resolution has appointed a new trustee". On the facts, the Unit Trust Trustee had not given notice to the unit holder, nor did it convene a meeting of unit holders. Accordingly, the Unit Trust Trustee was not removed and no new trustee was appointed upon the appointment of the liquidator. Gillard J concluded that the Unit Trust Trustee remained the owner of the legal estate which it held for the benefit of the Unit Trust.

(c) On de-registration of the Unit Trust Trustee

ASIC de-registered the company on 22 November 2000 pursuant to section 509 of the Corporations Law. By reason of section 601AD of the Corporations Law, on de-registration all the company's property vests in the Australian Securities and Investments Commission (ASIC). Under sub-section (3), ASIC takes only the same property rights that the company itself held. If the company held particular property subject to a security or other interest or claim, ASIC takes the property subject to that interest or claim.

Gillard J therefore concluded that the legal estate held by the Unit Trust Trustee company prior to its de-registration was held thereafter by ASIC. No application was made to the court to appoint a new trustee and no steps were taken pursuant to the Unit Trust Deed to appoint a new trustee. Accordingly, at the date of issue of the writ, being 21 January 2001, ASIC held the legal estate of the Unit Trust for the benefit of the beneficiary under the Unit Trust Deed. The only property comprised in the legal estate was the cause of action (if any) which the Unit Trust Trustee had on behalf of the Unit Trust against the defendants.

Gillard J concluded that neither plaintiff was the trustee of the Unit Trust when the proceeding was commenced. They had no right to bring the proceeding. In short, two persons who were neither a beneficiary nor a trustee of the Unit Trust had purported to bring a proceeding in their own name as trustees when there was a trustee who held the legal estate.

His Honour distinguished this case from cases involving a proceeding brought in the name of a trustee without authority. In addition, his Honour felt that the present case was not one where the trustee refuses to bring the proceeding.

(5) Was ratification available?

The plaintiff relied upon the principles of ratification. However, Gillard J rejected this argument. His Honour noted that the principle applies where a writ is issued without authority and the nominal plaintiff adopts the writ or ratifies its issue. Here, the nominal plaintiffs did not have a cause of action. The proceeding was brought by persons alleging they were the holders of the legal estate. However, on no view were the plaintiffs the holder of the legal estate. The trustee at the time, ASIC, was not a party, was unaware of the proceeding and did not ratify anything.

In conclusion, Gillard J was of the view that the plaintiffs never had any authority or capacity to bring the proceeding against the defendants either in their personal capacity or as trustees of the Unit Trust. The proceeding was a nullity from the beginning and could not be cured.

(C) DIRECTORS' DUTIES - FIDUCIARY DUTIES AND DERIVATIVE PROCEEDINGS

(By Ann Blake, Articled Clerk, Freehills)

Charlton v Baber [2003] NSWSC 745, New South Wales Supreme Court, Barrett J, 15 August 2003

The full text of the judgment is available at:

[http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2003/august/2003nswsc745.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2003/august/2003nswsc745.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)

(1) Facts

Mr Charlton and Mr Baber were founding directors of Newcastle Auto Air Pty Limited ("NAA"). Each held 50% of the issued share capital. Mr Charlton later ceased to be a director but remained a shareholder while Mr Baber continued as the sole director of the company. NAA encountered financial difficulties and entered into voluntary administration under Part 5.3A of the [Corporations Act (2001) (Cth)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) on 19 July 2002. It later passed into creditors voluntary winding up on 15 August 2002 under section 446A and the administrators were appointed as liquidators.

Mr Charlton, in his sole capacity as shareholder, sought leave to bring derivative proceedings on behalf of NAA to have the company pursue certain claims which he asserted arose out of what were breaches of the duties owed to NAA by Mr Baber as director of the company. Mr Charlton also sought to pursue the same claims against Mr Baber on the basis that fiduciary duties were owed to him personally as a shareholder.

(2) Are fiduciary duties owed to shareholders personally?

The defendants argued that the claim brought personally by Mr Charlton should be struck out pursuant to Part 15 rule 26(1) of the [Supreme Court Rules](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=11562" \t "default) which provides that the Court may strike out any part of a pleading where it discloses no reasonable cause of action or defence, has a tendency to cause embarrassment or delay to the proceedings, or is otherwise an abuse of the process of the Court. Justice Barrett held that Mr Charlton's allegations must be taken at face value and that Part 15 rule 26 of the [Supreme Court Rules](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=11562" \t "default) is only to be used in obvious cases and is not to be used for extended inquiry into the merits of the case.

Ultimately the Court did grant the defendant's application to strike out Mr Charlton's claim that fiduciary duties were owed to him personally. The Court followed the decision of the New South Wales Court of Appeal in Brunninghausen v Glavanics (1999) 46 NSWLR 538 that fiduciary duties having identical content cannot be owed to both the company and to one or more of its shareholders in relation to the same subject matter. Fiduciary duties are owed to the company, and to the extent that they exist at all, fiduciary duties owed by directors to shareholders, can be recognised only where they 'would not compete with' any duty owed to the company. Any parallel duties in a corresponding form are not owed to any shareholder, although particular circumstances may give rise to a particular duty owed by a particular director to a particular shareholder(s).

On the facts, Mr Charlton had pleaded that the fiduciary duties owed to the company were owed to him in precisely the same terms as the fiduciary duties owed to NAA, totally at odds with the decision in Brunninghausen. If any such duty is pleaded, it must be pleaded specifically and in such terms as to be circumscribed and defined by allegations of fact giving rise to some form of relationship involving ascendancy or influence and vulnerability such as in Chan v Zacharia (1984) 154 CLR 178 and Breen v Williams (1996) 186 CLR 71. On this basis Mr Charlton's statement of claim was struck out as it failed to disclose a reasonable cause of action and was embarrassing to the defendants in that they were not informed of the matters to which the alleged fiduciary duty was said to arise.

(3) Derivative proceedings and leave to proceed against a company in liquidation

Mr Charlton sought leave to bring proceedings on behalf of NAA pursuant to section 237. An issue arose as to whether, since Part 2F.1A was introduced by the [Corporate Law Economic Reform Program Act 1999](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=18039" \t "default), statutory derivative proceedings may be instituted in relation to a company that is in the process of being wound up. Barrett J held that sections 236(3) and 237 apply to proceedings brought on behalf of the 'company' which as defined in the Act, extends to a company in liquidation. Section 237(3), which refers to decision making by directors, does no more than cause a rebuttable presumption to arise as one of the matters to be considered by the Court under section 237(2).

(4) Meaning of 'best interests' of the company - section 237(c)(2)

Under section 237(c)(2) it must be in the best interests of the company that leave be granted for an applicant to bring a derivative action. Barrett J considered the meaning of the words 'best interests' and determined that 'best interests' is an expression concerned with a person's separate and independent welfare. What the supposed victim would have done to protect his own position must be taken into consideration. As NAA was in the process of being wound up, the best interests of the company must be taken to be the best interests of the creditors. In bringing a derivative action Mr Charlton's actions would seek to increase the assets available to the liquidators to meet creditors claims and so could clearly be regarded as being within the best interests of the company. (The Court noted that Mr Charlton's name did not appear on a list of unsecured creditors which formed part of the administrator's report. As a shareholder only, Mr Charlton would receive nothing from the derivative action unless the winding up yielded more than what was owed to the creditors.)

Barrett J also noted that just because some of the claims that Mr Charlton sought to pursue were for small amounts, this of itself did not preclude the actions from being in the best interests of the company so long as some potential benefit could be foreseen.

(5) Decision on derivative actions

Under section 237(2) all of the criteria must be met before the Court can grant leave to a plaintiff to bring a derivative action. The court has no discretionary leeway to act otherwise. Leave for Mr Charlton to bring derivate proceedings on behalf of NAA was granted as to some claims and refused as to others on this basis.

Leave was granted in relation to a dividend payment made to Mr Baber's wife to whom he had caused NAA to issue a B class share. However no dividend payment was made to Mr Charlton on his ordinary shares and he had not been informed of, nor did he consent to, the payment of the dividend on Mrs Baber's B class share. Under the NAA constitution, dividends must be paid on all shares other than those expressly deprived of dividend rights.

The Court also granted leave to bring a derivative action in relation to the leased premises from which NAA conducted its business. When the lease expired the Baber family trust took a lease for the premises which was extended to cover the adjoining premises as well. NAA then took a sublease for the original premises from the trust at a rent which was more than that paid by the trust under the head lease. As such Mr Baber and his family interests derived a profit at the expense of NAA.

Mr Charlton claimed that loans made to another company were made on uncommercial terms but he failed to show what the terms actually were. With the lack of information the Court was unable to determine whether there was a serious question to be tried.

It was also claimed that the remuneration paid to Mr and Mrs Baber was excessive. However in his pleadings Mr Charlton failed to show why the payments were excessive and so once again the Court was unable to determine whether there was a serious question to be tried and so the section 237(2) claim failed for not meeting all requirements.

(D) POOLING IN VOLUNTARY ADMINISTRATION

(By Stephen Magee)  
ACN 004 987 866 Pty Ltd v Humphris [2003] FCA 849, Federal Court of Australia, Goldberg J, 13 August 2003

The full text of the judgment is available at:  
[http://cclsr.law.unimelb.edu.au/judgments/states/federal/2003/august/2003fca849.htm](http://cclsr.law.unimelb.edu.au/judgments/states/federal/2003/august/2003fca849.htm" \t "_new)

Administrators of a group of companies were allowed to set up a pooling arrangement for the group's assets and liabilities.

(1) Background

The group consisted of five companies. It conducted a retail business through four of those companies. Those companies employed their own staff and leased their own premises. However, all stock was ordered and supplied by the fifth company, Hilton's Stores Pty Ltd. Hilton's Stores Pty Ltd also operated what was effectively the group's only trading account, and, in addition, made all the group companies' wages and rent payments.

Administrators were appointed to the group. They discovered that there were no intercompany loan accounts. This meant that, if each company were to be treated as a separate administration, the administrators would have to recreate intercompany loan accounts. They would also have to work out a method for distributing funds between the group's companies. The administrators came to the conclusion that this course of action was commercially impracticable, given the size of the group's assets and liabilities. Accordingly, they proposed a pooling arrangement.

(2) The pooling arrangement

The pooling arrangement was based on the following elements:  
- each company would enter into a deed of assignment and novation under which it would assign all its assets and liabilities to Hilton's Stores Pty Ltd (which would assume the liabilities)  
- each company would execute a deed of company arrangement which mirrored the deed of assignment and novation.

This was similar to an arrangement that Finkelstein J declared to be proper in Mentha v GE Capital (1998) 16 ACLC 1,032.

The administrators applied to the Federal Court for a direction that it was proper for them to execute the deed of assignment and novaton.

(3) Information to creditors

Goldberg J said that, as a matter of principle, it was appropriate to have pooling arrangements where the affairs of a group were so intermingled that creditors could be said to have been dealing with the group as a whole, rather than its individual companies.

However, his Honour was also aware of the fact that pooling would not necessarily affect all creditors equally. Because all creditors would share in the pooled assets on a pro rata basis, there was the possibility that some creditors would be worse off than if they proved against the assets of one particular company in the group (and that other creditors would be better off).

He thought that, where a pooling proposal is to be made to creditors, that outcome should be included in the information provided to them before they vote on the proposal. He noted that that had not been done in this case. However, the circumstances of the case excused that failure. This was because the cost and expense of recreating each individual company's accounts would have eliminated any significant return to creditors of the individual companies. In other words, no creditor would have been better off proving against a specific company than against the group as a whole.

Accordingly, the Court ordered that it was proper for the administrators to enter into the deed of assignment and novation.

(E) THE TAX COMMISSIONER'S ADVANTAGE IN INSOLVENT ADMINISTRATIONS

(By James Mayne, Clayton Utz)

Deputy Commissioner of Taxation v Dexcam Australia Pty Ltd (in liq) [2003] FCAFC 148, Federal Court of Australia, Full Court, Ryan, Finn and Dowsett JJ, 30 June 2003

The full text of this judgement is available at [http://cclsr.law.unimelb.edu.au/judgments/states/federal/2003/june/2003fcafc148.htm](http://cclsr.law.unimelb.edu.au/judgments/states/federal/2003/june/2003fcafc148.htm" \t "_new)

In this decision the Full Federal Court held that the Australian Taxation Office (ATO) could validly set off tax credits (which were accumulated by Dexcam during the currency of a deed of company arrangement) against other tax debts (accumulated before Dexcam entered into voluntary administration). This set-off was held to be valid despite the fact that Dexcam had entered into a deed of company arrangement in which the ATO was a participating creditor.

(1) PPS system

In the days before Pay As You Go (PAYG) withholding, there were two separate and distinct systems- the Pay As You Earn (PAYE) system for employees and the Prescribed Payments System (PPS) for independent contractors.

It was almost inevitable that tax deducted under the PPS system during an income year would not equal the tax actually payable. If tax deducted exceeded tax payable for an income year this gave rise to a credit under section 221YHF(1) of the [Income Tax Assessment Act 1936](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=6606" \t "default) (the "1936 Act). Under section 221YHG(1) of the 1936 Act that credit becomes a debt due and payable to the taxpayer by the Commissioner.

(2) Chronology

On 11 June 1996 Dexcam's Administrator was appointed pursuant to section 436A of the Corporations Law. On 12 August 1996 the Administrator, Dexcam and two directors of Dexcam entered into a deed of company arrangement. The Commissioner thus became a "Participating Creditor" for the purposes of the deed of company arrangement. On 21 August 1996 the Commissioner submitted a proof of debt to the Administrator for debts arising up until 11 June 1996 (the "pre-deed debts").

During the period April to October 1997, Dexcam's income tax returns for the 1993 to 1996 income years were lodged. The Commissioner made assessments and Dexcam became entitled to credits for PPS deductions and also became entitled to be paid interest by the Commissioner in respect of those years. The Commissioner applied or set off the PPS credits and interest credits firstly against tax assessed to be payable for the 1993-1996 income years and then in part reduction of the pre-deed debts.

At the time the income tax returns were lodged and the credits were applied by the Commissioner, Dexcam was insolvent and the Commissioner was aware of that fact.

(3) Interaction between corporations and tax legislation

Dexcam successfully argued in the Federal Court before Heerey J (Dexcam Australia Pty Ltd (in Liq) v Deputy Commissioner of Taxation [2002] FCA 820) that any priority the Commissioner may have had for the payment of tax debts was abolished by section 222ARA of the 1936 Act.

At the relevant time, section 222ARA of the 1936 Act stated that "to avoid doubt, this Part is not intended to limit or exclude the operation of Chapter 5 of the Corporations Law in so far as that Chapter can operate concurrently with this Part".

Heerey J decided that the provisions relating to the recovery of tax could no longer be said to stand outside the general statutory regime relating to the insolvency of individuals and companies including those relating to set-offs.

(4) Taylor's case

The case of Taylor v Deputy Commissioner of Taxation (1987) 16 FCR 212 concerned the interpretation of section 221H(2)(b) of the 1936 Act. That provision provided that where an employer had made deductions of tax from the wages of an employee, the Commissioner could credit the excess of the sum of those deductions against, amongst other things, "any other tax payable by the employee". The taxpayer tried unsuccessfully to argue that an amount of tax payable from an earlier income year had been suspended by the operation of the [Bankruptcy Act 1966 (Cth)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=6559" \t "default).

Heerey J distinguished Taylor's case and found that "the Commissioner was to be treated the same as any other creditor" of Dexcam.

The Full Federal Court found that Taylor's case was not distinguishable. The only material difference between the provisions was that the relevant provision in Taylor's case expressly treated "tax...that...may become due and payable" as "tax payable". Section 221YHG of the 1936 Act does not expressly do this. The liquidators argued therefore that the expression "amount payable" in section 221YHG of the 1936 Act meant an amount immediately payable. If that was the meaning to be ascribed to the expression, then the credits could not be set-off against an amount where the recovery of that amount was barred by a deed of company arrangement executed pursuant to the Corporations Law. The Full Federal Court did not adopt this narrow interpretation of the expression "amount payable".

(5) Comment

This case was, in part, a difficult exercise in statutory interpretation. In the end, the Full Federal Court looked to what the legislation was asking the Commissioner to do, rather than looking to the effect of the Commissioner's actions. Clearly the legislature intended that the [Insolvency (Tax Priorities) Legislation Amendment Act 1993](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=27990" \t "default) would remove the Commissioner's priority in insolvent administrations. In argument the liquidators of Dexcam apparently placed great emphasis on the extrinsic materials for the Act including the second reading speech and explanatory memorandum. After careful analysis, the Full Federal Court concluded that the legislature had not succeeded in its objectives, and applied Taylor's case.

Although the Full Federal Court did not expressly state it, it seems that considerable weight was given to the word "shall" in section 221YHG of the 1936 Act. The Court thus interpreted the provision as an absolute duty or an obligation imposed on the Commissioner, rather than a duty which was subject to the Corporations Law. In deciding that the provisions of the 1936 Act should prevail over the Corporations Law, Ryan and Dowsett JJ looked to the plain words of section 222ARA of the 1936 Act and concluded that "the adoption of section 222ARA demonstrates a clear intention that in the event of inconsistency between Ch 5 [of the Corporations Law] and Part VI [of the 1936 Act], Part VI was to prevail."

With respect, this would appear to be the correct approach to statutory interpretation. Using extrinsic materials before looking to the words of the enacted legislation is putting the cart before the horse.

The comments relating to statutory interpretation notwithstanding, the decision appeared to turn principally on a question of focus. In critiquing this decision, the question to be asked is whether the Full Federal Court should have been focussing on the statutory framework or on how the Commissioner should be treated in relation to the deed of company arrangement. The fact that the Full Federal Court focussed on the statutory framework has created an exception to the normal operation of insolvency laws and empowers the Commissioner in a way that might not have been expected by insolvency practitioners.

(F) MISLEADING AND DECEPTIVE CONDUCT UNDER SECTION 52 OF THE TRADE PRACTICES ACT

(By Sarah d'Oliveyra, Phillips Fox)

Metalcorp Recyclers Pty Ltd v Metal Manufactures Limited, [2003] NSWCA 213, New South Wales Court of Appeal, Handley JA, Hodgson JA and Gzell J, 5 August 2003

The full text of the judgment is available at:

[http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2003/august/2003nswca213.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2003/august/2003nswca213.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)

(1) Background

This case arose out of a claim of misleading and deceptive conduct, in contravention of 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 TPA'). Section 52 of the TPA provides: 'A corporation shall not, in trade or commerce, engage in conduct that is misleading or deceptive, or is likely to mislead or deceive.'

Metalcorp Recyclers Pty Ltd ('the Appellant') brought the claim against Metal Manufactures Limited ('the Respondent') in respect of conduct following the Appellant's delivery of 77 tonnes of scrap copper cathode ('the copper') to the Respondent.

On 1 February 2001, the Appellant took initial delivery of the copper from its supplier, CJ Trade Consultants ('CJT') in good faith and in turn delivered it to the Respondent pursuant to an agreement of sale. However, the copper was the property of Western Mining Corporation ('WMC') and had been stolen by unidentified third persons from a stock yard on 26 January 2001. The Respondent took delivery of the copper on 1 February 2001 and inspected it for quality the following day.

At 9am on 2 February 2001, a conversation ('the critical conversation') took place between the Appellant and the Respondent, whereby the Respondent told the Appellant that:

(a) the copper had been inspected; and

(b) that the Appellant had made a short delivery.

The Respondent did not dispute the quality of the copper. Accordingly, the Appellant made payment to CJT for the initial supply of the copper by way of a cheque made out for $254,164.74. It allegedly did so upon the assumption that the Respondent had accepted delivery of the copper. In this regard, it is important to note that the Appellant and Respondent had conducted business with one another for a period of approximately 10 years. Under the established course of business, deliveries of copper by the Appellant were quarantined by the Respondent for a period of 1 to 3 days, until inspected and accepted. Although never invoked in the 10 year period, there was a procedure for dealing with quality disputes arising from inspection.

In March 2001, the Respondent refused to pay the Appellant for the copper on the basis that it had been stolen from WMC. The Appellant was unable to recover the money it had paid to CJT on 2 February 2001 (having obtained default judgment against CJT for the recovery of the price that proved fruitless) and therefore brought a claim against the Respondent in respect of that amount plus interest.

(2) The basis of and circumstances surrounding the claim

The Appellant claimed that at the time of the critical conversation, the Respondent had inspected the copper and was aware that it had probably been stolen from WMC. The Appellant further claimed that the Respondent's failure to inform the Appellant of its belief that the copper had been stolen and that the Appellant would probably not be paid amounted to misleading and deceptive conduct, in contravention of section 52 of the TPA.

At trial, before Gamble ADCJ of the District Court of New South Wales, evidence was adduced to the following effect:

(a) That the sale of the copper was negotiated by the Appellant and the Respondent between 29 and 31 January 2001.

(b) That on 30 January 2001, a representative of WMC contacted a representative of the Respondent to inform him, inter alia, that 150 tonnes of their new copper cathode had been stolen on 26 January 2001. The Respondent's representative subsequently mentioned his continuing negotiations with the Appellant for the purchase of the copper.

(c) Following his conversation with the WMC representative, the Respondent's representative contacted WMC's private investigator and agreed to inspect the copper following delivery by the Appellant.

The Respondent denied that it had inspected the copper prior to the critical conversation. However, at trial, evidence was given of contemporaneous statements of the Respondent's representative to WMC, the police and his colleagues, which indicated that he had in fact inspected the copper provided by the Appellant prior to the critical conversation. This finding was supported by the critical conversation itself, in which the Respondent's representative expressly stated that he had inspected the copper and inquired about the short delivery.

(3) Findings of the District Court

Gamble ADCJ dismissed the Appellant's claim at first instance. She was not satisfied by the evidence of the Appellant or the Respondent in relation to the matters discussed above. However, she concluded that the Appellant's conduct in all the circumstances was 'unreasonable'. First, she considered the Appellant's payment to CJT before expiry of the maximum 3 day quarantine period to have been based on an unreasonable assumption that the Respondent would accept the copper despite the fact that the normal time for rejection had not passed. Secondly, she considered that the Appellant had ignored 'warning signs' that the copper may have been stolen. In this regard, Gamble ADCJ relied on a discussion between the Appellant and CJT, whereby the Appellant queried the short delivery and CJT informed the Appellant that 20 tonnes of the copper had been stolen overnight.

(4) Appeal to the New South Wales Court of Appeal

On appeal, Handley JA considered all of the evidence that was adduced at trial, notably the evidence relating to the Respondent's contemporaneous statements regarding its inspection of the copper. Handley JA considered that the court was properly entitled to find that the Respondent had inspected the copper before the critical conversation. Furthermore, he concluded that in all of the circumstances, the Respondent's conduct during the critical conversation was misleading and deceptive.

(5) Silence: relevant to determining a contravention of section 52

The Appellant had claimed that the Respondent's 'silence' amounted to misleading and deceptive conduct. Handley JA made reference to Clark CJ's decision in Demagogue Pty Ltd v Ramensky (1992) 39 FCR 31 ('Demagogue'), and stated that: 'In the absence of some positive duty to speak, silence can only be misleading or deceptive against a background of other facts known to both parties which make what is actually said so incomplete that it conveys a misrepresentation'.

On the evidence before him, Handley JA considered the Respondent to have been aware that the copper might have been stolen and that the Appellant may not have had title to it, nor an enforceable right to receive payment in respect of it. Set against the background of a longstanding business relationship built upon mutual trust, Handley JA considered that the Respondent had no reason to believe that the Appellant was knowingly dealing with stolen copper. However, the Respondent did not alert the Appellant to the fact that the copper might have been stolen. Furthermore, the Respondent represented to the Appellant that the only problem with the copper was that a short delivery had been made. In these circumstances, Handley JA concluded that during the critical conversation, the Respondent led the Appellant to believe that the copper had been inspected, there was no dispute as to the quality of the copper, and that delivery had been accepted.

This misleading and deceptive conduct on behalf of the Respondent was considered to have caused loss to the Appellant in the amount paid by it to CJT. Contrary to Gamble ADCJ's finding at trial, Handley JA found that the Appellant would not have made payment to CJT if the Respondent had told the Appellant that:

(a) it was awaiting advice from WMC as to whether the delivery formed part of the stolen copper; or

(b) simply that the delivery had not been accepted, thereby alerting the Appellant that there was a problem with the delivery.

Further, Handley JA considered that the Appellant sustained that loss in reliance on the Respondent's representation that it had accepted delivery of the copper.

Hogson JA and Gzell J agreed with Handley JA's judgment. Accordingly, the appeal was allowed with costs, Gamble ADCJ's judgment was set aside and judgment was entered for the Appellant for the amount paid to CJT together with pre-judgment interest from 2 February 2001 until the date of judgment of the NSW court of Appeal.

(6) Practical implications

While treating silence as a circumstance in which to assess whether certain conduct is misleading or deceptive, it could be said that this case has the practical implication of imposing a positive duty of disclosure in business relationships characterised by mutual trust and confidence.

(G) WHETHER A RECEIVER IS LIABLE TO EMPLOYEES IN CONTINUED EMPLOYMENT FOR ANNUAL LEAVE, LONG SERVICE LEAVE AND RETRENCHMENT ENTITLEMENTS

(By Michael Jackson, Phillips Fox)

McEvoy v Incat Tasmania Pty Ltd [2003] FCA 810, Federal Court of Australia, Finkelstein J, 1 August 2003

The full text of the judgment is available at:

[http://cclsr.law.unimelb.edu.au/judgments/states/federal/2003/august/2003fca810.htm](http://cclsr.law.unimelb.edu.au/judgments/states/federal/2003/august/2003fca810.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)

(1) Background

The Incat group of companies ('the Group') design, construct and sell catamarans. The Group was funded by the National Australia Bank by various means including interlocking guarantees from, and a floating debenture charge over the assets of, each company in the Group. Following a default, the bank appointed David McEvoy ('the Plaintiff') as receiver and manager for the Group. Some employees were retrenched but most were kept on to allow the group to continue its operations. The debt was subsequently recovered and the receiver retired. However, the Plaintiff retained around $17 million to satisfy the outstanding obligations incurred during the course of receivership.

In this application, the receiver sought to have determined whether the employees who were kept on, and who received their wages and leave entitlements as and when they fell due, were entitled to any further amounts. The employees in question argued that their entitlement to priority should be determined as if their contracts of employment had come to an end.

Finkelstein J stated that the resolution of the issue was a matter of construction of section 433 of the [Corporations Act 2001](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) ('Act'). Section 433 provides that the receiver must pay certain debts or amounts in priority to the claims of the debenture holder including "any debt or amount that in a winding up is payable in priority to other unsecured debts" pursuant to paragraphs 556(1)(e) ["wages… payable by the company in respect of services rendered to the company by employees"], (g) ["all amounts due… in respect of leave of absence"] and (h) ["retrenchment payments payable to employees of the company"].

(2) Judgment

(a) The effect of the appointment of a receiver on a contract of employment.

Finkelstein J stated that it is generally accepted that the appointment of a receiver by the court terminates the contract of employment. His Honour reasoned that a court appointed receiver does not operate the concern on behalf of the company, but rather adverse to it. However, in cases where a receiver who is the company's agent is privately appointed, Finkelstein J held that the contract of employment is not terminated. His Honour listed three exceptions to this rule: (1) where the appointment is accompanied by the sale of the company's business; (2) where the receiver enters into a new contract of employment which is inconsistent with the employee's old contract; and (3) where the continuation of the employment contract is inconsistent with the role of the receiver.

(b) Consideration of case law

Finkelstein J considered three cases that examined the operation of section 433 and its predecessors in relation to annual and long service leave. However, his Honour did not find them altogether helpful.

The first two cases considered by Finkelstein J were Love v Image Centre Pty Ltd (unreported, Supreme Court of New South Wales, Young J, 13 February 1991) ('Love') and Whitton v ACN 003 226 886 (Controller Appointed) (In Liq) (1996) 42 NSWLR 123 ('Whitton'). However, Finkelstein J declined to follow Love or Whitton as neither case considered the effect of section 558 of the Act.

Section 558(1) dictates that when determining priorities in the winding up of a company, the position of an employee is to be determined as if his services had been terminated. The date of deemed termination in a compulsory winding up is when the order is made and, in a voluntary winding up, when the resolution for winding up is passed. His Honour stated that it follows that in a winding up, leave entitlements (including those which at law continue to accrue) must be treated as having fallen due upon commencement of the winding up.

The third case examined by Finkelstein J, Re Office-Co Furniture Pty Ltd (Receivers and Managers Appointed) [2002] 2 Qd R 49 ('Re Office-Co'), dealt with the applicability of section 558(1) to a receivership. However, His Honour stated that Re Office-Co was unhelpful as the Court made no reference to the history of the section.

(c) The appropriate construction of section 433 of the Act

Finkelstein J stated that the construction question is whether the phrase "any debt or amount that in a winding up is payable in priority to other unsecured debts" (as contained section 433), simply refers to the 'debts and claims' mentioned in section 556(1) or, rather, whether the phrase refers to those debts and claims as expanded, when necessary, by the application of the deeming provision in section 558(1).

Finkelstein J found the answer to the question of construction to lie in the legislative history of section 558(1) of the Act. His Honour stated that "The history persuades me that the only purpose for section 558(1) was to ensure that employees would not in a winding up lose priority for annual and long services leave which was still accruing but had not yet fallen due at the commencement of the winding up. In the absence of the amending legislation (and the introduction of the deeming provision), the employees whose employment was about to come to an end as a result of the winding up would be disadvantaged when compared with employees whose rights had accrued as they would miss out on the benefits which they were intended to be given. I can discern no intention that the same benefit should be given to employees of a company in receivership, whose employment may survive the receivership. It could not be said that they would suffer in the same way as an employee whose company was unable to pay its debts in full".

Finkelstein J accepted that this construction of 558(1) does not take into account the position of employees whose employment is terminated by the receiver. His Honour stated that subject to the possibility of those employees having claims against the receiver under section 419, their situation can only be remedied by Parliament.

In the case at hand, the employees relied on section 419(1) as an alternate source of liability on the receiver to pay accrued annual leave and long service leave entitlements as well as any retrenchment entitlements which may have accrued since the receivers appointment. Section 419(1) provides that "A receiver, or any other authorised person, who, whether as agent for the corporation concerned or not, enters into possession or assumes control of any property of a corporation for the purpose of enforcing any charge is, notwithstanding any agreement to the contrary, but without prejudice to the person's rights against the corporation or any other person, liable for debts incurred by the person in the course of the receivership, possession or control for services rendered, goods purchased or property hired, leased, used or occupied".

His Honour stated that, on the present state of the authorities, he could not find the receiver liable under section 419(1). In this regard, Finkelstein J referred to the judgment of Dillion LJ in Nicoll v Cutts [1985] BCLC 322 where it was held that "the appointment out of court under powers in a debenture of a receiver, who is to be the agent of the company, normally has no effect on the company's contracts, and ordinary contracts of service will not be affected. The company remains the employer". Finkelstein J stated that the same view was taken by Lehane J in Sipad Holding DDPO v Popovic (1995) 14 ACLC 307 at 310.

(3) Declaration

Finkelstein J declared that:  
(a) Section 433 of the Act does not oblige the Plaintiff to pay annual leave, long service leave and retrenchment entitlements to (or on behalf of) employees of Group, to whom such entitlements were accruing, but were not yet due and payable.  
(b) Section 419 of the Act does not oblige the Plaintiff to pay annual leave, long service leave and sick leave entitlements to employees of the Group, to whom such entitlements were accruing, but had not become due and payable during the Plaintiff's appointment as receiver and manager of the Group.

(H) RELIANCE BY INSURER ON AN EXCLUSION CLAUSE IN A DIRECTORS INSURANCE POLICY BEFORE A FINDING OF DISHONESTY

(By Sarah Turner, Mallesons Stephen Jaques)

Silbermann v CGU Insurance Limited; Rich v CGU Insurance Limited; Greaves v CGU Insurance Limited [2003] NSWCA 203, New South Wales Court of Appeal, Beazley JA, Hodgson JA, Tobias JA, 25 July 2003

The full text of the judgment is available at:

[http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2003/july/2003nswca203.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2003/july/2003nswca203.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)

(1) Background

The plaintiffs (the Insured) are former directors of One.Tel Limited. Each bought proceedings seeking a declaration the defendant (CGU) was obliged to indemnify them, and advance them the costs of defending themselves, in an investigation by ASIC, two proceedings bought by ASIC, examinations under the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) and other proceedings, under a Directors & Officers Liability Insurance Policy (the Policy).

Clause 3 of the Policy relevantly provided:  
"This Policy does not provide an indemnity against any Claim made against any Director or Officer:…

3.1 Dishonesty & Fraud  
brought about by, contributed to by or which involves:

(1) the dishonest, fraudulent or malicious act or omission or other act or omission committed with criminal intent of such Director or Officer,

(2) such Director or Officer having improperly benefited in fact from securities transactions as a result of information that was not available to other sellers and/or purchasers of such securities; or

(3) such Director or Officer having gained in fact any personal advantage to which he/she was not legally entitled.

However, this exclusion shall only apply to the extent that the subject conduct has been established by a judgment or other final adjudication adverse to the Director or Officer."

In refusing to indemnify the Insured, CGU relied, inter alia, upon Clause 3.1 of the Policy.

McClellan J, at first instance, ordered the separate resolution of three questions to determine whether the defendant was able to rely upon that particular defence:

(a) Whether, on the true construction of Policy, absent a final adjudication adverse to the Insured, CGU can rely on Clause 3.1.

(b) Whether under the Policy CGU is entitled to seek a final adjudication adverse to the Insured and thereby exclude liability under Clause 3.1 in the same proceedings in which the Insured makes a claim for indemnity.

(c) Whether Clause 3.1 of the Policy excludes liability on the part of CGU to pay claims by the Insured for indemnity for Defence Costs under certain other provisions of the Policy.

McClellan J answered each question in the affirmative and the Insured sought leave to appeal. On appeal, the Court addressed the questions proposed by McClellan J as set out below.

(2) Decision on appeal

(a) Whether, on the true construction of the policy, absent a final ajudication adverse to the Insured, CGU can rely on clause 3.1

The Insured argued a final adjudication was a condition precedent to reliance on the exclusion in Clause 3.1; it could not be that the Policy allowed CGU to sit back and await the resolution of an inadequately funded defence to criminal charges.

CGU argued allegations of dishonesty made by it should be assumed to be true; it must be open to CGU to agitate defences it has available and the Policy as a whole granted a discretion whether to advance Defence Costs in any event. It was argued that it was open to the Court to consider Defence Costs and other Claims against the Policy separately.

The majority of the Court, dismissing the appeal, did not qualify their affirmative answer to this question. The majority decided that CGU was entitled to refuse indemnity where the Claim was bought about by a dishonest act or omission on the part of the Insured and was also entitled to refuse payment of Defence Costs.

The majority relied upon the fact that under the Policy, costs only became Defence Costs when, with the prior written consent of CGU, they had actually been incurred. Accordingly, CGU had a discretion whether to indemnify Defence Costs prior to a final adjudication. The final paragraph in 3.1 simply made it plain CGU could only sustain its denial of indemnity if the relevant final determination was made.

Hodgson JA, in a minority decision, divided his answer to this question into two parts, dealing with Defence Costs separately. Hodgson JA decided in the affirmative, that Clause 3.1 could be relied on in the sense that it could be raised as a defence in insurance proceedings, but qualified his affirmative answer by deciding Clause 3.1 did not provide a valid justification for refusing indemnity regarding Defence Costs unless and until a final adjudication adverse to the relevant director was obtained.

To the extent Hodgson JA upheld the appeal and answered the question in the negative, he dissented from the majority judgment of the Court.

(b) Whether under the policy CGU is entitled to seek a final adjudication adverse to the Insured and thereby exclude liability under clause 3.1 in the same proceedings in which the Insured makes a claim for indemnity

The Insured contended any entitlement of CGU to seek a final adjudication adverse to them was offensive to CGU's duty of good faith.

The Court held there was nothing in the Policy to prevent CGU attempting to establish reliance on Clause 3.1, as long CGU had reasonable grounds for seeking to rely on the exclusion.

(c) Whether clause 3.1 of the policy excludes liability on the part of CGU to pay claims by the Insured for indemnity for defence costs under certain other provisions of the policy

The Insured argued the Policy provided for two distinct types of indemnity, one against Claims and the other against Defence Costs, and Clause 3.1, construed according to its natural and ordinary meaning, was not intended to exclude Defence Costs; if there was an ambiguity, the Policy should be read strictly against CGU.

The Court considered that the Policy did not draw a sharp distinction between two types of indemnity. The primary indemnity was against any Loss arising out of any Claim and Loss was defined to include Defence Costs. The Defence Costs were thereby caught by the exclusion.

(3) Conclusion

Leave to appeal was granted in each case, but the appeals (by 2:1) were dismissed with costs.

Pursuant to a similarly worded policy, an insurer may be entitled to refuse indemnity, including payment of defence costs, where the claim has been bought about by a dishonest act or omission of the part of the Insured prior to a final adjudication of whether such conduct has actually taken place.

(I) WHEN IS THE ENFORCEMENT OF A GUARANTEE UNCONSCIONABLE?

(By Arthur Escamilla, Blake Dawson Waldron)

Motek Kranz and Mansville Pty Ltd v National Australia Bank Ltd [2003] VSCA 92, Supreme Court of Victoria, Court of Appeal, Winneke P, Charles and Eames JJA, 25 July 2003.

The full text of the judgment is available at:

[http://cclsr.law.unimelb.edu.au/judgments/states/vic/2003/july/2003vsca92.htm](http://cclsr.law.unimelb.edu.au/judgments/states/vic/2003/july/2003vsca92.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)

This case concerned whether it would be unconscionable for the National Australia Bank Ltd (the "bank") to enforce a guarantee given by Motek Kranz and Mansville Pty Ltd (together, the "appellants").

In the course of dismissing the appeal, the court examined and applied the case law surrounding the principles laid down in Commercial Bank of Australia Limited v Amadio (1983) 151 CLR 447 ("Amadio") and Garcia v National Australia Bank Ltd (1998) 194 CLR 395 ("Garcia"). Charles JA delivered the leading judgement; Winneke P and Eames JA, agreed.

(1) Facts

Tom Lefkovic was granted an advance to acquire a private placement of shares. The shares were to be acquired by a shelf company and the proceeds of the sale were to be used to pay off the debt of a company controlled by Lefkovic. The venture included the sale of those shares after a holding period, at what was expected to be a substantial profit.

Lefkovic, anxious to secure the deal, approached his brother-in-law, Motek Kranz, and asked him to provide further security for the loan. Kranz relied on Lefkovic, who had been his accountant and business adviser for some 12 years. Kranz, through his company Mansville Pty Ltd ("Mansville"), was a joint owner of a property, and after the substance of the transaction was explained to him he agreed to provide that property as security. Kranz executed a guarantee and mortgage in support in his personal capacity and as director of Mansville. Lefkovic defaulted on the loan and the bank sought to enforce the guarantee.

(2) Issues

The appellants submitted that the single issue in the appeal was unconscionability, saying that the trial judge took an unduly narrow approach to equitable principles and the decision in Garcia.

(3) Legal principles

(a) Garcia

The appellants argued that the principles in Garcia were applicable given that there was a relationship of trust and confidence between Kranz and Lefkovic of which the bank knew or should have been aware. It was claimed that Kranz reposed great trust in his brother-in-law, who was also his accountant.

His Honour stated that the principles in Garcia would make it unconscionable for a bank to enforce a guarantee given by a volunteer if it has not explained the situation to the guarantor and does not know that an independent person has done so, if the bank knows that there was a relationship of trust and confidence between the guarantor and the debtor whose debt has been guaranteed. On the facts, his Honour concluded that given the limited extent of the information available to the bank, the bank did not know and should not be taken to have assumed that there was a relationship of trust and confidence between Kranz and Lefkovic, so as to bring into play the principles acted on in Garcia.

Charles JA, obiter, disagreed with the trial judge's application of the principles applied in Garcia as the trial judge tried to confine their application to "the most intimate of family relationships", which in Charles JA's view was not justified. However, on the facts established in evidence, this finding was of no relevance to his Honour's conclusion that no error was to be found in the trial judge's decision.

(b) Amadio

The second limb of the appellants' argument claimed that the arrangement between the bank and Lefkovic was a speculative and unusual transaction fraught with risk, and that these matters were known to the bank. Accordingly, the bank was obliged to ensure that the appellants were warned of the speculative and risky aspects of the transaction and failed to give the appellants any appropriate warning.

Among other cases, his Honour considered the case of Amadio, where the court dealt with the situation where one party makes unconscionable use of a superior position or bargaining power to the detriment of a party suffering from some special disability or is placed in some special situation of disadvantage. Charles JA stated that the position of special disability or disadvantage in which the surety is placed must have been known or evident to the bank, or something which the bank ought to have known, before it would become unconscionable for the bank to enforce the guarantee and mortgage against the appellants. After examining the evidence Charles JA concluded that the bank did not know that the guarantors occupied a situation of special disadvantage in relation to the transaction, that a reasonable person would not have suspected that they were in any such situation, and that the bank did not take unfair advantage of its position by entering into the transaction.

(4) The English concept of "put on inquiry"

Eames JA made reference to the English approach of constructive notice developed by the House of Lords in the case of Royal Bank of Scotland Plc v Etridge (No 2) [2002] 2 AC 773. According to this case, if a bank is not to be required to evaluate the extent to which its customer has influence over a proposed guarantor, the only practical way forward is to regard banks as "put on inquiry" in every case where the relationship between the surety and the debtor is non-commercial. The creditor must always take reasonable steps to bring home to the individual guarantor the risks he is running by standing as surety. His Honour recommended the adoption of this principle in Australia; he stated that it provides the commercial and broader community with readily understood and easily applied principled to govern transactions with guarantors.

(J) APPROVAL OF A SCHEME OF ARRANGEMENT BETWEEN UNITED ENERGY LIMITED AND ITS MEMBERS

(By Carla Alviano, Blake Dawson Waldron)

In the Matter of Section 411 of the [Corporations Act 2001 (Cth)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) and In the Matter of United Energy Limited (ACN 064 651 029) and In the Matter of a Proposed Scheme of Arrangement Between United Energy Limited and its Members [2003] VSC 266, Supreme Court of Victoria, Gillard J, 23 July 2003

The full text of the judgment is available at:

[http://cclsr.law.unimelb.edu.au/judgments/states/vic/2003/july/2003vsc266.htm](http://cclsr.law.unimelb.edu.au/judgments/states/vic/2003/july/2003vsc266.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)

This proceeding concerned United Energy Limited seeking the Court's approval of its members' endorsement of the Scheme of Arrangement for Power Partnership to acquire 100% of its issued shares.

(1) Facts

On 23 April 2003, United Energy Limited agreed with AMP Henderson Global Investors Limited, Alintagas Limited and Aquila Inc that it would propose a Scheme of Arrangement to its members to allow Power Partnership, a current member with 57% of United Energy's total shareholding, to acquire the remaining 43% of the shares for a cash consideration of $3.15 per share. An order to convene a meeting of United Energy Limited shareholders to vote on the scheme was made by Hanson J of the Victoria Supreme Court on 30 May 2003. The Scheme was subsequently agreed to by the statutory majority of United Energy Limited's members, other than Power Partnership, in a meeting on 10 July 2003. The present proceeding pertained to United Energy seeking the Supreme Court's approval, before Gillard J, of the members' decision and to ensure that the shareholders' meeting had been properly convened.

On 11 July 2003, Master Evans declared that the meeting of United Energy Limited's shareholders had been properly and duly convened and that the resolution pertaining to the Scheme of Arrangement had been duly passed. However, four members opposed the validity of the meeting and appeared before the Court in this proceeding. Therefore, Gillard J found it necessary to consider whether the meeting had been properly conducted.

(2) Gillard J's decision

(a) The re-opening of the poll after it had been declared closed

Three of United Energy Limited's members raised a concern that an irregularity had occurred in the shareholders' meeting when the Chairman declared the poll closed and then, upon realising that he and the other directors had not yet cast their proxy votes, withdrew the closure and lodged the outstanding proxies. The members contended that this irregularity affected the legality of the meeting and, thus, it had not been properly held. Gillard J stated that a Chairperson's powers during a meeting are very broad and that he has a wide discretion in relation to the conduct of the meeting, although he believed that a Chairperson should seek to act fairly, in good faith and should give reasonable opportunity to the members for debate.

Gillard J believed that the Chairman, in acting as he did in allowing the previously unentered votes to be included in the count, acted in an appropriate manner. His actions did not cause prejudice to any member, and were in accordance with common sense. To repeat the whole voting process would have involved substantial delay and money wastage. Therefore, it was declared that the meeting had been properly held, despite the re-opening of the voting period.

(b) The meeting was not properly conducted

One member, Mr Doherty, submitted that the Chairman had not properly conducted the meeting of shareholders. Doherty claimed that another member, Mr Sidaway, sought to move a resolution that an adjournment in the meeting should occur to allow members present to partake of refreshments. The Chairman refused to put the motion to a vote. Gillard J held that this occurrence was not a matter of substance and it did not affect the validity of the meeting.

Another member, Mr Haines, submitted that numerous other defects in the conduct of the meeting rendered its validity questionable. Haines argued that the whole Scheme of Arrangement and its subsequent proceedings were a 'scheme' which minority shareholders were being forced to accept. Gillard J rejected this argument and stated that the Corporations legislation permits Schemes of Arrangement to exist which allow a statutory majority of shareholders to vote upon a proposal presented to them, and that this was nothing more than an ordinary democratic process.

It was furthermore submitted by Mr McCallum, a third member, that the final vote was not valid as it should have been accepted by at least a 90% majority of shareholders. Gillard J stated that this would have been the case if Chapter 6 of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) regarding takeovers was to apply, but that there was no compulsion to utilise the Chapter 6 process and the company had resolved to use the Chapter 5 process. His Honour observed that ASIC had presented a notice to the Court stating that it was satisfied that a Scheme of Arrangement had not been entered into for the purpose of avoiding the operation of Chapter 6. Therefore, a 90% majority did not need not be reached in order for the Scheme to be accepted.

Finally, it was contended by the members that individual shareholders had not been consulted by the two independent directors or the independent expert about their recommendation that the members of United Energy Limited approve the Scheme of Arrangement. Gillard J held that there was nothing in the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) which required such consultation with members and, furthermore, it would have been an impossibility, especially considering the number of shareholders of United Energy Limited. In the case of the independent expert, it would have been inappropriate for the expert to talk to shareholders and be influenced by their views; as an independent expert, it must make its own decision based on the material before it.

(c) Court's role

Gillard J concluded by stating that the Court's jurisdiction on such an application was supervisory and, thus, it was reluctant to interfere with the considered decision of the majority, since it is they that could best determine what was commercially advantageous in the circumstances. Furthermore, the Court was satisfied that all the statutory provisions relating to Schemes of Arrangement and Hansen J's orders had been complied with. Accordingly, the Court approved United Energy Limited's Scheme of Arrangement to allow Power Partnership to acquire 100% of its shares.

(K) EXTENSION OF TIME GRANTED TO REGISTER CHARGE IN RESPECT OF COMPANY IN ADMINISTRATION

In the matter of Daisytek Australia Pty Ltd (Administrators Appointed) [2003] FCA 768, Federal Court of Australia, Gyles J, 24 July 2003  
The full text of the judgement is available at:  
[http://cclsr.law.unimelb.edu.au/judgments/states/federal/2003/july/2003fca768.htm](http://cclsr.law.unimelb.edu.au/judgments/states/federal/2003/july/2003fca768.htm" \t "_new)

(1) Summary  
The court exercised its discretion under section 266(4) of the [Corporations Act 2001](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) ("Act") on the application of a chargee, to extend the period for lodgment of notice of a charge in relation to a company in respect of which an administrator had been appointed under Part 5.3A of the Act and where liquidation or entry into a deed of company arrangement was inevitable. The extension of the lodgment period was made on certain terms and conditions.

(2) Background  
Daisytek Australia Pty Ltd ("Daisytek") carried on a business of selling computer equipment supplies. On or about 22 November 2002, GE Capital Finance Pty Ltd ("GE") entered into a facility agreement with Daisytek (as borrower) and Daisytek Australia (Queensland) Pty Ltd ("Daisytek Queensland") (as guarantor) to provide working capital to finance Daisytek's business.

On 22 November 2002, Daisytek and Daisytek Queensland each granted a fixed and floating charge in favour of GE. Notification of the charge against Daisytek Queensland was lodged in December 2002. However, GE's solicitors at the time failed to lodge notification of the charge against Daisytek within the period required by the Act.

On 16 May 2003, the directors of Daisytek resolved, in accordance with section 436A of the Act, that Daisytek was insolvent or was likely to become insolvent at some future time and appointed administrators pursuant to Part 5.3A of the Act.  
GE applied for the extension of time to lodge the notice of the charge against Daisytek under section 266(4) of the Act.

Relevantly, section 266(1) of the Act provides that where an administrator of a company is appointed, a registrable charge on property of the company is void as a security on that property unless a notice in respect of the charge was lodged under section 263 or 264 (as the case requires) within the relevant period, or at least 6 months before the critical day.

Section 266(4) of the Act provides that if the Court is satisfied that the failure to lodge notification of the charge within the required period time was accidental or inadvertent, or is not of a nature to prejudice the position of creditors or shareholders, or that on other grounds it is just and equitable to grant relief, then on the application of the company or any person interested, the Court may exercise discretion to extend the period for the lodgment of the notification of the charge.

The administrators notified the creditors and shareholders of GE's application and invited either direct appearance or the lodging of submissions with the administrators. A major supplier of Daisytek, Hewlett Packard Australia Pty Ltd ("HP"), was the only party that contested the orders.

Gyles J held that the charge against Daisytek was void against the administrators from the date of their appointment. In this case, his Honour was satisfied that the failure to lodge the notice in respect of the charge was both accidental and inadvertent within the meaning of section 266(4). Accordingly, the issue before the Court was whether the Court should exercise its discretion to extend the notification period, and if so, on what terms and conditions.

(3) Judgment  
Gyles J stated that this was the first time that the Court had considered an application pursuant to section 266(4) in the context of a company in administration. In discussing the legislative intent behind section 266(1), his Honour referred to an established principle of company law that once liquidation has commenced, one creditor should not be assisted by the Court to improve its position over other creditors.

Gyles J discussed the history of the relevant provisions and noted the former practice in Australia (and is still the position in the United Kingdom) that refused the extension once winding up commenced, on the basis of the crystallisation of the rights of unsecured creditors and the policy behind section 266(1) - that void securities should not disturb insolvent administration.

His Honour referred to a number of decisions dealing with the principles that should guide the exercise of his discretion to grant a time extension for notification of the charge in the present case and concluded that once winding up occurs, he would have no difficulty in requiring the secured creditor to make a positive case for extension. This was based on the reasoning that the provisions for notification of a security are for the protection of the public which deals with the company.

Gyles J held that the approach should be the same where there is the intervention of administration and where it is inevitable that some form of insolvency administration will follow from the appointment of the administrator. His Honour stated that it is clear from section 266(1) that the security is avoided by the scheme administrator in the same way as against a liquidator.

Counsel for GE submitted that:

(a) apart from the default itself, GE did not commit any other 'faults';  
(b) GE did not prejudice creditors beyond the occasion of the default itself and no creditor had claimed actual prejudice arising from the failure to register the charge; and  
(c) the extension of time would not cause practical detriment to unsecured creditors.  
While accepting that there was no fault on the part of GE, other than the default itself, Gyles J found that the grant of an extension of time affects the interest of unsecured creditors generally and that it is not possible in an application of this kind to require close proof of actual prejudice. Further, his Honour found that practical detriment to unsecured creditors could not be precisely determined as this depended on the future resolution of issues of fact and law and the result of the realisation of assets and assessment of liabilities.

The Court ultimately exercised its discretion to extend the time for lodgment of the notification of the charge against Daisytek, subject to certain conditions proposed by GE to alleviate prejudice to the unsecured creditors of Daisytek.

5. CONTRIBUTIONS

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

6. SUBSCRIPTION TO THE BULLETIN

To subscribe to the Corporate Law Bulletin or unsubscribe, please send an email to "[cclsr@lawlex.com.au](mailto:cclsr@lawlex.com.au)".

7. DISCLAIMER

No person should rely on the contents of this publication without first obtaining advice from a qualified professional person. This publication is provided on the terms and understanding that (1) the authors, editors and endorsers are not responsible for the results of any actions taken on the basis of information in this publication, nor for any error in or omission from this publication; and (2) the publisher is not engaged in rendering legal, accounting, professional or other advice or services. The publisher, authors, editors and endorsers expressly disclaim all and any liability and responsibility to any person in respect of anything done by any such person in reliance, whether wholly or partially, upon the whole or any part of the contents of this publication.

[**Click here**](http://research.lawlex.com.au/) to change your profile   
LAWLEX welcomes users' suggestions for improving this service. Please contact [Customer Service.](mailto:alert@lawlex.com.au)

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

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