



# **FEDERAL COURT OF AUSTRALIA**

## **Corporations Law Nation-wide Seminar**

**2 April 2008**

## **Current Issues and Developments in Corporate Insolvency Law and Practice**

Seminar held “live” in the Sydney Registry of the Court and relayed simultaneously to all other Registries of the Court by videoconference.

## Contents

<b>Welcome:</b>	The Hon MEJ Black AC, Chief Justice, Federal Court of Australia .....	1
<b>Preface:</b>	The Hon Justice KE Lindgren .....	3
<b>Speaker Biographies:</b>	.....	5
<b>Seminar Presentations:</b>		
	Stephen Parbery.....	8
	Richard Fisher .....	19
	Michael Hughes.....	45
	Patrick Meaney.....	49
	Maree Blake .....	55
<b>Conclusion:</b>	The Hon Justice Roger Gyles AO .....	57

## **CURRENT ISSUES AND DEVELOPMENTS IN CORPORATE INSOLVENCY LAW AND PRACTICE SEMINAR**

**Address of welcome by the Chief Justice of the Federal Court of Australia,  
the Hon M E J Black AC**

**Wednesday, 2 April 2008**

Welcome to the Federal Court's first national video seminar on corporations law particularly relating to current issues and developments in corporate insolvency law and practice.

The importance of this topic and the interest that there is in it in the profession is illustrated by the fact that we have received nearly 700 acceptances - over 250 from New South Wales, over 150 from Victoria and substantial numbers from the other States and from the Territories. I am in Melbourne, welcoming an audience in Brisbane, Sydney, Melbourne, Hobart, Adelaide, Perth, Darwin and Canberra. In some Registries we have had to provide for the seminar to be screened in more than one courtroom.

This seminar reflects our Court's wish to interact with the profession in matters relating to our national commercial jurisdiction and also areas of public law. We have had national seminars before, particularly in Admiralty, but this is by far the largest so far.

Corporations law is national law. It disregards State and Territory boundaries. The Australian Securities and Investments Commission and, within its area of responsibility, the Australian Prudential Regulation Authority, are national regulators. Likewise the Takeovers Panel within its area of responsibility. So too, the Federal Court is national. It is a national superior trial and appellate court with general jurisdiction in all civil matters arising under federal law including of course, relevantly here, corporate legal disputes and proceedings. In addition to corporate insolvency, the Court has jurisdiction in respect of personal insolvency.

I commend those who have taken the initiative and planned this seminar, and, in particular, I thank our speakers and panellists. I hope that the seminar will be the first of a series of national seminars held by the Court in the area of corporations law and other areas of the Court's jurisdiction. A similar national meeting on new procedures for tax cases will be held shortly.

Justice Gyles will chair the seminar from Sydney, where he will introduce the speakers and outline the program. There will be opportunity for members of the audience nationally to interact with the speakers and the panel. The seminar will run for one and a half hours including a time for questions and comment.

Light refreshments will be served nationally - if one can serve light refreshments nationally - after the seminar.

Ladies and gentlemen, a very warm welcome to this exciting national seminar in corporate insolvency law and practice.

## **Preface to Papers and Notes**

The Committee that planned this nation-wide seminar on corporations law was myself and the following persons who were nominated by the bodies indicated:

Mr Greg Golding, Law Council of Australia

Mr Michael Murray, Insolvency Practitioners Association

Mr Patrick Meaney, Australian Prudential Regulation Authority

Ms Georgina Hayden/Mr Kim Turner, Australian Securities and Investments Commission

The two speakers were:

Mr Stephen Parbery of PPB, Chartered Accounts & Business Reconstruction Specialists

Mr Richard Fisher AM, General Counsel, Adjunct Professor, Graduate School of Government, University of Sydney

The three panellists were:

Mr Michael Hughes, Partner, Minter Ellison

Mr Patrick Meaney, General Counsel, Australian Prudential Regulation Authority

Ms Maree Blake, Director of Corporations and Insolvency, Australian Securities and Investments Commission

The planning committee did not intend that the two speakers and three panellists would provide written material for publication. They were informed that this was not intended when they were invited to participate. However, several people who attended the seminar asked if any notes would be distributed. Therefore, with some misgiving in view of the terms of the initial invitation to them to participate, I asked the speakers and panellists if they would, after all, agree to provide some brief notes. They graciously agreed, and this modest publication is the result.

I express my thanks to them and to Justice RV Gyles AO, who chaired the seminar, for his concluding observations.

I hope that nation-wide seminars in the area of corporations law will be held on a regular basis – perhaps every six to twelve months.

I thank the speakers and panellists, the other members of the planning committee, the relevant Judges in the respective District Registries, all of the District Registrars and staff in the various Registries for making the seminar a success.

Justice Kevin Lindgren  
Convenor  
Corporations Panel  
NSW District Registry  
Federal Court of Australia

## Speakers' Biographies

### STEPHEN PARBERY

Stephen Parbery has been involved in corporate reconstruction and insolvency for nearly 30 years. He was a founding partner of PPB in 1983 and has managed some of Australia's major corporate reconstructions and insolvencies.

Under Stephen's guidance, PPB has grown to be one of Australia's leading independent business reconstruction firms with offices in the major cities of Australia and New Zealand.

Stephen has played an active and leading role within his profession having sat on the national committee of the Insolvency Practitioners Association of Australia (IPAA) since 1996 and is a life member and past president of that organisation. He has taken an active part in insolvency law reform including advocating protection of employee entitlements in insolvencies prior to the introduction of the Government's General Employment Entitlements and Redundancy Scheme (GEERS).

As a senior practitioner in his field Stephen has been engaged by the Commonwealth Government to advise on the implications of major corporate collapses of Ansett Airlines, HIH Insurances and UMP/AMIL (a major medical defence organisation) and by the NSW Government as an administrator under the Local Government Act.

He has acted in some of the largest property corporate collapses in Australia.

### RICHARD FISHER

Richard Fisher AM is an Adjunct Professor in the Graduate School of Government at the University of Sydney and is the University's General Counsel. He is also a company director of listed public companies.

Prior to joining the University, Richard was a partner for some 25 years in Blake Dawson Waldron and is its immediate past Chairman of Partners. Richard's area of practice was corporate law with a focus on corporate re-organisation and insolvency.

Richard is presently an international consultant to the Asian Development Bank and was a Commissioner of the Australian Law Reform Commission.

His publications include *Corporate Insolvency Law* (LBC, 2000), and the Parts on *Receivers & Managers* and *Corporate Reorganisation* in *The Laws of Australia*. He holds the degrees of Master of Economics and Bachelor of Laws.

## MICHAEL HUGHES

Michael is recognised as one of Australia's leading insolvency and reconstruction lawyers.

Chambers & Partners Global Guide to the World's Leading Lawyers consistently recognises Michael as a "leading individual" (1<sup>st</sup> tier) and describes him as "highly experienced and extremely knowledgeable", "outstanding" and is valued "for the length of his exceptional knowledge of the law".

Peers also noted Michael's skills in litigation relating to the finance sector. *Which Lawyer*, the current edition of *International Financial Law Review 1000 – 2007*, and *Euromoney - World's Leading Lawyers 2006* all recognise Michael as one of Australia's leading insolvency lawyers.

With more than 17 years' experience, he has developed a specialist practice in insolvency and reconstruction law, security enforcement and commercial litigation. He spent 12 months working with a specialist insolvency practice in London.

A focus of Michael's practice is acting for banks and other credit providers in the enforcement of securities and the work out of problem loans. He advises on Australian Securities and Investments Commission and Australian Stock Exchange (ASX) investigations, involving claims of insider trading and market manipulation, and failures to comply with ASX Business Rules. He has also advised and acted for insolvency practitioners in the promotion of deeds of company arrangement and the recovery of company assets.

Michael is a member of the National Committee of the Insolvency Practitioners Association of Australia, and a former National Chairman of the Law Council's Insolvency and Reconstruction Committee. He qualified as an accredited mediator in 1993 and has promoted negotiated settlements of protracted bank and insolvency litigation.

## PATRICK MEANEY

Patrick has been General Counsel at the Australian Prudential Regulation Authority since August 2005. He was admitted as a solicitor in 1991 and worked as a senior lawyer in the Australian Securities and Investments Commission from 1993 to 2000 and with Blake Dawson Waldron from 2000 to 2002. He was Vice-President and Head of Listing Enforcement at the Hong Kong Stock Exchange between 2002 and 2005.

He holds Bachelors degrees with Honours in Political Science and Law, a Masters degree in Law and a graduate certificate in Applied Finance.

Prior to becoming a lawyer Patrick worked with the Department of Foreign Affairs and Trade and the Office of National Assessments.

## **MAREE BLAKE**

Maree Blake is Director of Corporations and Insolvency with the Australian Securities and Investments Commission, with three portfolios covering corporate governance, insolvency, and auditors and liquidators.

Before joining ASIC in 2005, Maree specialised in insolvency and reconstruction for some 20 years, and was partner of a national insolvency firm. Maree's principal insolvency practice was in the secured market for major banking clients, however her insolvency appointments covered a wide range of assignments and market sectors.

Maree is a member of the Australian Institute of Company Directors and a Fellow of CPA Australia. She previously served on CPA's Queensland Division Public Practice and Disciplinary Committees, and continues to present sessions on Ethics for the Queensland Division of CPA Australia.

# **Current Issues and Developments in Corporate Insolvency Law and Practice**

**Stephen Parbery**

## **INTRODUCTION**

I feel somewhat overwhelmed speaking about aspects of Corporations Law to such an esteemed audience. Nonetheless hopefully with the help of Richard and others I can assist in imparting some views about practical difficulties faced by directors and practitioners advising directors and others under the current law.

## **RESTRUCTURING LARGE CORPORATIONS**

Under current law we have a ‘one size fits all’ law for insolvencies for large and complex Companies such as HIH , to small privately owned businesses which are primarily set up under corporate structures for the purpose of obtaining tax relief.

As a practitioner dealing across the spectrum I often find the current laws frustrating when attempting to maximise an outcome for stakeholders, because directors are sometimes forced to take action prematurely due to their or their advisors interpretation of the insolvent trading provisions of the Corporations Act.

I pose the question as to whether current legislation provides an appropriate balance between promoting good corporate behaviour and ensuring directors are willing to take sensible commercial risks.

The possibility of directors being exposed to personal liability by their actions in allowing a company to continue trading whilst insolvent impacts on corporate behaviour in a number of different ways:

In a positive sense:

- (1) It encourages directors to be aware of their company’s finances.
- (2) It may encourage directors to relinquish control and allow creditors to determine the company’s future.
- (3) It may allow creditors to improve their position by suing directors for recovery – although from the few cases run there is little evidence of that benefit. However the threat of action is often used to negotiate a better deal for creditors when negotiating deeds of company arrangements.

In a negative way:

- (1) Businesses are sometimes prematurely closed.
- (2) Workouts and restructuring can prove difficult because, directors, banks and advisors will not take the risk of trading a business on.

I would like to make a personal observation about behavioural differences of directors. In large corporations the behaviours of directors are often different to director's behaviour in small to medium enterprises.

### **LARGE CORPORATIONS**

- Often have independent directors who have limited personal financial exposure to the company but do have reputation risk if a company fails.
- Usually the directors have the benefit of external experts and internal staff and resources to be appropriately informed on the financial position of the company.
- The directors' actions are often under press scrutiny and market disclosure requirements with the threat of potential shareholder class actions for inadequate or misleading disclosure should the company fail.
- Often have large exposures to banks and banking syndicates who through their enquiries place directors in a position of becoming aware of loan covenant breaches and in turn causing the directors to suspect insolvency.

### **SMALL TO MEDIUM CORPORATIONS**

- Often the businesses are funded or capitalised through the directors pledging their personal assets including their family home. They usually provide personal guarantees to ensure supply from creditors. If the business fails they risk all of their personal assets and often face personal bankruptcy.
- Directors of such enterprises often have limited business education and limited access to internal or external experts to guide them.
- The Company's bankers show little interest in the financial details of the business because they often rely upon real property security to support their loans.

## THE BEHAVIOURAL DIFFERENCES

- Directors of large corporations which are in financial difficulty are likely to seek professional advice, such advice is usually conservative. More than likely rather than risk potential action for insolvent trading, or claims of misleading conduct, directors will seek relief from the insolvent trading provisions by appointing a voluntary administrator.

Although formal appointments such as Voluntary Administrations have certain advantages to assist in preserving ailing companies often there is damage caused to the goodwill of the business. This may be due to loss of supply contracts through contracts becoming void, loss of customer confidence and diminished staff morale. The impact of a formal appointment may dissipate the goodwill of the business and therefore may not be in the best financial interests of creditors or shareholders.

There are a number of examples in the past where with the benefit of hindsight directors appear to have jumped too early because of the threat of personal liability and reputation risk. However in recent times the pendulum of director behaviour may have swung back a little due to the extent of margin loans secured over shares provided to major shareholders in larger corporations and the conflicts that arise between the director's corporate duties and their own self interest.

- Directors of small to medium corporations who often have substantial personal financial exposure in the event of their business failing, will often continue trading a hopelessly insolvent company even after receiving professional advice to appoint administrators, because in their mind they have nothing to lose.

### **Should we have a two class system for large and small enterprises or should we consider expanding the defence provisions to insolvent trading to allow use of the current Business Judgement Rule under Section 180(2) of the Corporations Act or a variation thereof?**

From my experience directors of large corporations do behave differently when under financial pressure than directors of small to medium enterprises. Whether it is possible to have a two class system is difficult for me to assess but it is worthy of further debate to overcome the current difficulties of directors conflicts in dealing with the interests of stakeholders.

Rather than considering a two class system it may be worthy to explore how the current laws may be enhanced or changed to allow a restructuring process to take place across the board. In my opinion we need a mechanism which balances the need to protect creditors' interests and the right for the company to restructure without necessarily a formal appointment in the first instance. It would be sensible for the law to allow under certain circumstances for the directors and their advisors to implement a turnaround strategy on the basis of the prospect of preserving and enhancing business value without personal risk. Currently the risk of personal liability deters law abiding directors and advisors in becoming involved in turnaround or work out strategies.

In UK legislation a softer view prevails in relation to insolvent trading. It provides for a concept of “wrongful trading” whereby a director is liable if he or she ought to have concluded that there was no reasonable prospect of the company avoiding liquidation. They also have a harsh offence known as fraudulent trading- where directors continue to incur debt knowing they have no prospect of ever paying their debts.

Under UK law it is not unlawful to trade a company while it is insolvent. If the directors believe that the position will be turned around and that the creditors’ position will improve, their actions will only constitute wrongful trading when a point is reached when directors should have realised that the position of creditors would likely to deteriorate.

This difference in the law in the UK does allow directors some scope for what is known as a “prepack to administration” whereby assets are sold on a going concern basis prior to a formal appointment. There can be advantages in “pre-packs” to avoid diminished value from asset realisations caused by brand damage, contracts being voided and loss of key staff which often occurs after formal appointments. It is however open to abuse when asset sales are not at arms length and the sale is not adequately or widely marketed.

In Canada directors have the right to rely upon a Business Judgement Rule as a defence to insolvent trading. Practitioners with whom I have spoken to in Canada believe that they have a fair balance within their legislation to allow restructuring in “the Twilight Zone” because of the defence available under the Business Judgement Rule.

Some of the elements of the UK and Canadian legislation may be worthy for Australia to consider to give greater latitude to restructure a company by removing the defining point of insolvency in determining liability or extending that time forward.

In a recent submission to the Commonwealth Treasury, the IPA has recommended that by amending the Business Judgement Rule for suitable application to the insolvent trading regime may achieve the objective of director/creditor balance. The IPA recommends a “Financial Judgment Rule” by varying the existing Business Judgement Rule by:

- Removing the requirement for the director to not have a material personal interest in the subject matter of the judgment;
- Introducing a concept of a duty owed to creditors; and
- Making it dependent on the maintenance by the company of proper financial records.

In my view we need to consider these changes and create a mechanism which allows advisors and stakeholders to work with directors to allow turnaround strategies which will provide a better outcome than allowing businesses to collapse. Usually even in the worst run companies there are parts which are worth salvaging, the path to do that under the current legislation is problematic.

Even in the case of such matters as HHH and One Tel it is highly likely that with a more conducive turnaround regime parts of those businesses could have been salvaged for the benefit of creditors and other stakeholders.

The caution of course in seeking to change the balance is to overcome the risk of fostering misuse of legislation changes which encourages phoenix style activities.

## **UNCITRAL MODEL LAW AND CROSS BORDER INSOLVENCY**

If time permits I would also like to touch upon a further reason to support changes to our insolvent trading laws.

With a global economy and expanding cross border trading we now have many international companies with corporations acting in numerous jurisdictions. To ensure a more efficient regime of dealing with the insolvency of such international companies, many countries including Australia has adopted (or about to) UNCITRAL Model Law.

If Australia continues to have insolvency laws which on the face of it appear comparatively harsh in terms of directors' exposure to personal liability, we may end up out of step with many of our trading partners. This in turn may make it problematic in terms of lending covenants, turnaround strategies and attracting foreign companies to operate in Australia.

An example of this arose when the international milk company Parmalat ran into financial difficulty in Italy. This effectively caused banking covenants in the Australian subsidiary to be broken which in turn caused questions to be raised about the solvency of the Australian company. In this case the Australian banks were able to reach agreement with the local directors and were able to ensure the on going solvency of the local company. However it is concerning that this well run and viable company could have faced the consequences of a formal appointment if those technical breaches with its bankers were not rectified.

## **CONCLUSION**

In my view it is time to reconsider how we may improve the ability to restructure ailing businesses in a way which maximises the value for stakeholders through preserving all or parts of a business as a going concern.

The recommendations made by the IPA in allowing a defence for insolvent trading under a modified version of the Business Judgement Rule in my view would provide a mechanism to balance the interest of creditors and directors when companies fall into financial difficulty.

Current Issues and  
Developments in Corporate  
Insolvency Law and Practice

By Stephen Parbery  
Managing Partner  
April 2008

**PPB**



CHARTERED ACCOUNTANTS  
AND BUSINESS  
RECONSTRUCTION SPECIALISTS



**PPB**

**Restructuring large corporations**

- "One size fits all" law
- Inhibits insolvency practitioner's ability to maximize returns for stakeholders
- Directors forced to take premature action



## Restructuring large corporations

Does the current legislation strike the correct balance between promoting good corporate behavior and allowing directors to take sensible commercial risks?

- Positives
  - Encourages directors to be aware of company's finances
  - May encourage directors to relinquish control and allow creditors to determine the company's future
  - May allow creditors to improve their position by suing directors for recovery
- Negatives
  - Businesses sometimes prematurely closed
  - Workouts and restructuring can prove difficult because directors, banks and advisors will not take the risk of trading a business on first

## Restructuring large corporations

Features of large corporations

- Independent directors who have limited personal financial risk but significant reputation risk if a company fails
- Directors have the benefit of external experts and internal staff and resources to be appropriately informed
- Directors actions under press scrutiny and market disclosure requirements
- Often have large exposures to banks/banking syndicates. Bank's inquiries often lead to directors suspecting insolvency.

## Small to medium corporations

### Features of small to medium operations

- Often the businesses are funded or capitalised through the directors pledging their personal assets, including the family home. If the business fails they risk all of their personal assets and often face bankruptcy.
- Directors often have limited business education and limited access to internal and external experts.
- The company's bankers often show little interest because they often rely on real property security.



## Behavioral differences – Large v. Small to Medium

### Large Corporations

- When in financial difficulty directors are likely to seek professional advice, and rather than risk potential action for insolvent trading (or claims for misleading conduct) are likely to seek relief by appointing a voluntary administrator.
- Appointment of a voluntary administrator often leads to significant damage to the goodwill value of the business and therefore is often not in the best financial interests of creditors or shareholders.



## Behavioral differences – Large v. Small to Medium

### Small to medium corporations

- Directors often have substantial personal financial exposure in the event of the business failing and will often continue trading a hopelessly insolvent company (even after receiving professional advice to appoint administrators) because in their mind they have nothing left to lose.

## Should we have a two class system, or expand the defences to insolvent trading, or a variant thereof?

- From my experience directors of large corporations do behave differently when under financial pressure than directors of small to medium enterprises.
- Rather than considering a two class system, it may be useful to explore how the current laws can be enhanced to facilitate the restructuring process across the board.
- We need a mechanism which balances the need to protect creditors' interests and the right for the company to restructure without a formal appointment.
- The Law should allow directors and advisors to implement a turnaround strategy that has the reasonable prospect of preserving and enhancing business value without personal risk.
- Currently, the risk of personal liability deters law abiding directors and advisors from becoming involved in turnaround or workout strategies.

## UK and Canadian Legislation

In UK legislation a softer view prevails:-

- Concepts of 'wrongful trading' and 'fraudulent trading'
- Not unlawful to trade on an insolvent company if the directors reasonably believe that the business' position will be turned around and that the creditors' position will be improved.
- Some elements of the UK and Canadian legislation may be worthy for us to consider

## IPA submission on amendments to the insolvent trading regime

- The IPA has recommended that by amending the Business Judgment Rule for suitable application to the insolvent trading regime the objective of director/creditor balance can be achieved.
- The IPA recommends a "Financial Judgment Rule" which is an amendment of the existing Business Judgment Rule by:-
  - Allowing a director to have a personal interest in the subject matter of the judgment;
  - Introducing a concept of a duty owed to creditors; and
  - Making it dependent on the maintenance by the company of proper financial records.

### UNCITRAL Model Law and cross boarder insolvency

- Ensures a more efficient regime of dealing with insolvency of companies conducting business in many different jurisdictions.
- Australia is about to adopt the UNCITRAL Model Law
- Our insolvency laws are comparatively harsh in terms of the personal liability of directors, which is out of step with our trading partners. We should address this.



### Conclusion

- Time to reconsider legislation impacting on restructuring ailing companies
- Recommend a modified version of the Business Judgment Rule



## Current Issues and Developments in Corporate Insolvency Law and Practice

**Richard Fisher AM**  
**General Counsel**  
**Adjunct Professor, Graduate School of Government**  
**UNIVERSITY OF SYDNEY**

### 1. Introduction

The invitation to speak at this Seminar came with what might be described as a smorgasbord of topics which I could address. The three to which I would like to give some attention are:

- (a) the position of directors of large corporations as against small to medium-sized corporations in relation to restructuring;
- (b) the 2007 amendments to the insolvency provisions of the *Corporations Act 2001* (Cth); and
- (c) cross-border insolvency.

### 2. The position of Directors of Larger Corporations

So far as this topic is concerned, it enables me to explore again an issue which I addressed in a paper published in last year's *Insolvency Law Journal*; namely the impact of the continuous disclosure regime on the development of a restructuring proposal for a public listed company, see (2007) 15 *Insolv LJ* 23. At the time the article was written, the business pages of the press had not been filled with news of companies such as Allco, Centro, and MFS. Rather, it was prompted by what seemed to me to be the broader implications of the decision in *Sons of Gwalia*.

As I said in the article:

*“While the decision in Sons of Gwalia is of interest for its own sake, it raises for more general consideration the question: what are the disclosure obligations of a company and, particularly, a listed public company? The answer to that question, it is submitted, identifies a tension which exists between compliance with those obligations and maintaining sufficient confidence in a financially troubled company while efforts are made to restructure its affairs outside of the environment of a formal insolvency administration.*

*A company's publicly available information will not only affect the market for its shares, it will also have an impact on the relationship between the company and its financiers, suppliers and employees. Where a company is in financial difficulty, the maintenance of those relationships will be critical to its continued operation and such a consideration has a particular relevance where efforts are*

*being made to restructure its affairs. Accordingly, there may be a need to balance the company's disclosure obligations on the one part and the maintenance of its commercial connections on the other. That "balancing act" is likely to be made more difficult if its directors and others are personally liable in damages where there is a breach of the company's disclosure obligations."*

To remind you, the Continuous Disclosure Rule is as follows:

***"General rule***

*3.1 Once an entity is or becomes aware of any information concerning it that a reasonable person would expect to have a material effect on the price or value of the entity's securities, the entity must immediately tell ASX that information."* (emphasis added)

The exceptions to that rule are:

***"Exception to rule 3.1***

*3.1A Listing rule 3.1 does not apply to particular information while all of the following are satisfied.*

*3.1A.1 A reasonable person would not expect the information to be disclosed.*

*3.1A.2 The information is confidential and ASX has not formed the view that the information has ceased to be confidential.*

*3.1A.3 One or more of the following applies.*

- It would be a breach of a law to disclose the information.*
- The information concerns an incomplete proposal or negotiation.*
- The information comprises matters of supposition or is insufficiently definite to warrant disclosure.*
- The information is generated for the internal management purposes of the entity.*
- The information is a trade secret."*

Those rules are given legislative force by s 674 of the *Corporations Act*.

Of significance to directors of public listed companies when formulating a reconstruction proposal is the need to understand the operation of the continuous disclosure regime. When does an obligation under the regime arise? Addressing that question will require an understanding of matters such as:

- What amounts to “information” for the purpose of the regime?
- When is that information “material” and sufficiently “certain”?
- Has there already been “partial disclosure” of that information?
- Is the information already available “incomplete”?

For the purposes of my remarks today, I only wish to address the following:

- (a) what constitutes “*material*” information.
- (b) when is information sufficiently “*certain*” to require disclosure; and
- (c) when will there have been “*partial*” disclosure of information so as to require its more general disclosure.

Additionally, I wish to consider the possibility of “*opting out*” of the continuous disclosure regime.

**(a) Material Information**

For the continuous disclosure rules to apply, the relevant information concerning the company must be material in the sense that a reasonable person would expect it to have a material effect on the price of the company’s shares.

In Ford’s *Principles of Corporations Law* [10.310] it is said:

“ [a]n omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote ...there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the “total mix” of the information made available.

It might be observed by way of comment that, in the reported cases, the courts appear to have been assisted, when assessing the materiality of the relevant information, by recourse to what actually happened to the market for the shares in the company once that information was released. One consequence of that circumstance is that the reported decisions are not replete with statements of principle to which reference might be made when attempting to make an assessment of the materiality of a particular piece of information in advance of its release.

While it may be the case that general statements of principle of what constitutes materiality are not to be found in the cases, it has been held that if information which comes to hand significantly affects the accuracy or currency of information which is already generally available, disclosure of that information must be made: *GPG (Australia Trading) Pty Ltd v GIO Australian Holdings Ltd* (2001) 40 ASCR 252.

Reference might also be made to *ASIC v Plymin* (2003) 175 FLR 124; 46 ACSR 126, which was an insolvent trading case. However, in the course of his judgment, Mandie J recorded an expression of view by ASIC that a letter from the company's bankers converting its facilities to facilities which were repayable on demand was information of a kind that was liable to be disclosed under the discontinuous disclosure regime. Moreover, that was a view on which the company's solicitors agreed. While it does not appear from the report of the decision in that case, I take it that the effect of the bank's communication was to change the characterisation of the company's facilities with its banker as appearing in the company's published accounts.

As well as the reported decisions, the notes to Listing Rule 3.1 exemplify what might amount to material information. Included among the examples given in those notes is "a change in the entity's financial forecast or expectation."

Beyond that, Guidance Notes to the Listing Rules provide two examples of a change in a company's financial circumstance which are said to require disclosure and which would be pertinent in the case of a company seeking to organise a restructure. Those examples are:

*"On reviewing management accounts part way through a half year period, X Ltd becomes aware that actual revenues and profits for the period will vary from one or more of the following to a material extent.*

- *The financial results for the previous corresponding period.*
- *Forecast projections contained in any prospectus.*
- *Projections and indications previously provided to the market in relation to the half-year period.*

and

*On reviewing management accounts part way through a half year period, X Ltd becomes aware that it will incur a large trading loss for the half year. Due to projected revenues from contracts expected to be completed in the second half year, X Ltd still expects to achieve full year results broadly in line with that of the previous full year."*

**(b) Certainty of Information**

A further issue which will impact upon the obligation to disclose is the degree of certainty attached to the relevant information. In that regard it is to be noted that one of the exceptions to the obligation to make disclosure is that it does not attach where “*the information comprises matters of supposition or is insufficiently definite to warrant disclosure*”. That said, the information must also be confidential and be such as a reasonable person would not expect the information to be disclosed.

Time does not permit an exploration of the factual circumstances which arose in each of:

- *Randall v Aristocrat Leisure Ltd* (unreported, Supreme Court of NSW, Einstein J, 8 June 2004); and
- *ASIC v Southcorp Ltd (2)* (2003) 48 ACSR 187.

However, they each illustrate circumstances where there was sufficient doubt attending the so-called “*certainty*” of the information for its disclosure not to be required.

These decisions are particularly pertinent to the management of a financially troubled company. Clearly, if the deteriorating financial performance of the company is such as to significantly impact the publicly available information concerning its financial forecast or expectation, that is a circumstance that will enliven its obligations under the continuous disclosure regime. However, if an outcome of any negotiations directed towards an informal workout would result in the modification of its obligations, e.g., to pay interest or to repay principal with a consequential impact on its forecast financial performance or its balance sheet, as the case may require, that may create sufficient uncertainty about its actual financial performance to relieve the company of any obligation under the continuous disclosure regime.

**(c) “Partial disclosure” of information**

What I have characterised as “*partial disclosure*” of information might arise in the circumstance where, even if the relevant information might not otherwise be required to be disclosed under the continuous disclosure regime (as was the case in *ASIC v Southcorp Ltd* (supra)), the disclosure of that information to a section of the market may require its more general publication.

A company in financial difficulty seeking to negotiate an informal workout would ordinarily enter into detailed discussions with its financiers. A necessary element of those discussions would be disclosure of a complete picture both of the company’s existing position and its plans and prospects. While it was not decided in *Southcorp*, the parties to those proceedings accepted that, without more, “*partial disclosure*” of that kind imposes an obligation under the continuous disclosure regime to give such material a general currency in circumstances where the knowledge of that material may have an impact on

the market. Similarly, Gyles J in *GPG v GIO* (supra) raised an issue that AMP had been put into a privileged position so far as concerned its access to detailed information about GIO's financial circumstances. However, it is submitted that, leaving aside what, in any event, is a duty on the part of a banker to maintain confidentiality in respect of its customer's affairs, it would be desirable in the circumstances under consideration to reinforce the company's entitlement to rely on the confidentiality exception to the disclosure regime and have the parties to the workout negotiations execute a "confidentiality agreement". Such an agreement would stipulate that the parties to it could only use the information gained in the course of those negotiations for the purpose of formulating an out-of-court settlement with the company.

**(d) "Opting out" of the continuous disclosure regime**

Under the ASX Listing Rules there are two bases, other than by way of removing the shares from the Official List, upon which the market for a company's shares can be halted. There can be either a trading halt or a suspension. A trading halt must be limited to no more than a full day's trading. A company's shares may be suspended from quotation at the request of the company made under Listing Rule 17.2, which provides:

*ASX may at any time suspend an entity's securities, or a class of the, from quotation at the request of the entity. ASX may require the request to be in writing. ASX is not required to act on the entity's request. The entity must tell ASX each of the following.*

- *Its reasons for the suspension.*
- *How long it expects the suspension to last.*
- *The event it expects to happen that will end the suspension.*
- *That it is not aware of any reason why its securities should not be suspended.*
- *Any other information necessary to inform the market about the suspension, or that ASX asks for.*

It should be noted that Listing Rules 3.1 is not limited in its application so as to relieve a company from its obligations under the Rule if trading in its shares is suspended. Accordingly, if it is decided that an application to suspend the company's shares should be made pending the outcome of negotiations by it for an informal workout, application might also be made for relief from the continuous disclosure rules. To the extent that such an application requires the ASX to be taken into the company's confidence, it would not appear to be disadvantageous as the ASX can require an explanation of the reason for a request that trading in the company's shares be suspended. All of that said, no such waiver ever appears to have been granted and, it is submitted, would not be likely to be granted, not least because there can continue to be off-market dealings in the company's shares.

Be that as it may, insofar as a request for a trading halt and relief from the continuous disclosure regime in these circumstances might be thought to raise issues of policy, those issues are tested by an enquiry as to whose interests the continuous disclosure rules are intended to protect. Shortly stated, it is the company's shareholders and those trading in the company's shares. To the extent that there is a concern for the interests of the company's creditors, it is submitted that they are adequately protected by matters such as the provisions of the *Corporations Act* that facilitate the liquidation of insolvent companies and impose a liability upon directors for so-called insolvent trading.

ASIC has also published *Policy Statement 95: Disclosing Entity Provisions Relief*, which applies not only to public listed companies but also to unlisted disclosing entities. In the case of listed entities, it might be noted that ASIC is unlikely to grant relief to the company of its disclosure obligations if the ASX has indicated that it would not grant a waiver of the Listing Rules.

#### **(e) Conclusion**

Where directors of a public listed company wish to pursue an informal workout, there may be a balancing act. That act will require the company to accommodate both its obligations under the continuous disclosure regime and the need to maintain the integrity of its business while pursuing an informal resolution of its financial difficulties.

In undertaking that act, some basic suggestions are offered for consideration:

1. Retain an expert to assess whether information which becomes available during the workout negotiation would be such, having regard to information already available, as to have a material effect on the company's share price.
2. In relation to such information, assess the degree of its certainty when determining whether it should be published.
3. Further, in relation to such information, review the extent to which it has become available on a selective basis to third parties who are not bound by an obligation of confidence when determining whether it should be published.
4. So far as concerns parties to those negotiations, their participation should be conditioned by them undertaking a confidentiality agreement.
5. Also, in relation to such information, assess the extent to which failure to publish the information may involve the company in misleading and deceptive conduct having regard to information concerning the company which is already publicly available, when determining whether it should be published.
6. Assess whether the information that is being considered for publication may be affected by the outcome of the negotiations for an informal workout to ascertain

whether that exception to the operation of the continuous disclosure rules might apply.

7. Give consideration to applying for both the company's shares being suspended from trading and for relief from the ASX to comply with the continuous disclosure rules.

### **2007 Amendments to the Corporations Act – some “Non-Reform”**

One of the significant amendments made in 2007 to the insolvency provisions of the *Corporations Act* involved the introduction into the liquidation procedure of a mechanism by which the liquidator or liquidators of a group of companies could “pool” their administrations. Equally significant was the last minute decision by the then Federal Government not to proceed with the introduction of a like reform into the voluntary administration regime. As a matter of practice, it must be doubted that that circumstance has any or any significant consequences where deeds of company arrangement are being proposed for the companies in the group. However, prior to that point, the proposed reforms would have had utility. That said, it is another circumstance where the provisions of Section 447A of the *Corporations Act* might be called in aid to support an application modifying the operation of Part 5.3A. Of course, unlike I think all of the reported cases, such an application would almost certainly involve trespassing to some degree upon the rights of creditors of each of the various companies in the group, at least to the extent that they would ultimately be entitled to differential dividends.

A similar but not precisely the same issue was identified as a possibility by the High Court in *Australasian Memory Pty Ltd v Brian* (2000) 34 ACSR 250. That possibility was adumbrated as a consequence of making an order under section 447A and it was said (at 259):

*“Whether there would be no power to make an order under Section 447A(1) [in that kind of case], or whether there would be an insuperable discretionary obstacle to its making, are points we need not examine.”*

It is submitted that such a limitation of the extensive power conferred by section 447A, in the sense of there being no power, would not be warranted, not least by reference to their Honours’ own words (at 256):

*“Cogent reasons must be advanced, then, if the power given by the general words of Section 447A(1) is to be read down”.*

However, it is accepted that there may be an “insuperable discretionary obstacle” to the making of such an order. It is submitted that an enquiry as to whether there was such an obstacle would be sensibly informed by the considerations that apply when a court is assessing whether or not to terminate a pooling determination made by a liquidator or liquidators of a group of companies; section 579A(1), *Corporations Act*. Those grounds include:

*“(d) effect cannot be given to the pooling determination without injustice or undue delay; or*

- (e) *the pooling determination would materially disadvantage an eligible unsecured creditor who is an applicant for the order; or*
- (f) *the pooling determination would be oppressive or unfairly prejudicial to, or unfairly discriminatory against, an applicant for the order who is an eligible unsecured creditor of a company in the group; or*
- (g) *the pooling determination would be contrary to the interests of the creditors of the companies in the group, considered as a whole;*

### 3. Cross-border insolvency

The third topic which I wish to address concerns the recent adoption into Australian law of the UNCITRAL Model Law on Cross-Border Insolvency. A detailed exposition of that Law is not possible in the time available. However, it has a number of crucial features:

#### (a) **Automatic Access to Australian Courts for Foreign Representatives.**

Article 9 provides:

*“A foreign representative is entitled to apply directly to a court in this State.”*

Foreign representative is defined by Article 2 to mean:

*“ “Foreign representative” means a person or body, including one appointed on an interim basis, authorised in a foreign proceeding to administer the reorganisation or the liquidation of the debtor’s assets or affairs or to act as a representative of the foreign proceeding”*

The immediate consequence of the stipulation is that, say, the English liquidator of a company which also has a presence in Australia will be relieved of the tedious procedure of applying first to the English High Court for a Letter of Request addressed, say, to this Court asking that it act in aid of the English liquidator. Rather, the English liquidator has standing to apply directly to this court for that assistance.

Moreover, Article 11 provides that:

*“A foreign representative is entitled to apply to commence a proceeding under Australian law if the conditions for commencing such a proceedings are otherwise met.”*

Other provisions are made for the recognition of both foreign representatives (Article 12) and foreign creditors (Articles 13 and 14) in Australian insolvency administrations. However, these provisions would not seem to significantly affect the position as it has operated to date.

**(b) Application for Recognition of Foreign Proceedings.**

Article 15 authorises a Foreign Representative to apply either to this Court or a Supreme Court for recognition of the foreign proceedings in Australia. That application must be supported by either a certified copy of the decision commencing the foreign proceeding and appointing the foreign representative or a certificate from the foreign court affirming the existence of the foreign proceeding and of the appointment of the foreign representative.

Additionally, the application must be supported by a statement which identifies all of the foreign proceedings in respect of the debtor.

Foreign proceeding is defined in Article 2 as follows:

*“a collective judicial or administrative proceeding in a foreign State, including an interim proceeding, pursuant to a law relating to insolvency in which proceeding the assets and affairs of the debtor are subject to control or supervision by a foreign court, for the purpose of reorganisation or liquidation”*

Provided that:

- (i) the application is in respect of a “foreign proceeding”;
- (ii) the applicant is a foreign representative;
- (iii) the evidentiary requirements to support the application to which a reference has been made above are satisfied; and
- (iv) the application is made either to this court or to a supreme court.

the application shall be granted.

The stipulation for mandatory recognition of all foreign insolvency proceedings is to be contrasted with the arrangements now found in Section 29 of the *Bankruptcy Act* and Section 581 of the *Corporations Act* which are to the effect that recognition is only required to be given to a foreign insolvency proceeding which has been instituted in a prescribed country. Otherwise, the Court has discretion as to whether recognition will be granted. It might be noted that those provisions will continue to apply except to the extent of any inconsistency; cl 21 and 22, *Cross-Border Insolvency Bill*, 2008.

**(c) Interim Relief.**

Article 19 provides that “*where relief is urgently needed to protect the assets of the debtor or the interests of creditors*” interim relief of a kind which is similar to the appointment of a provisional liquidator under the *Corporations Act* or an interim trustee under the *Bankruptcy Act*.

**(d) Recognition as a Foreign Main Proceeding or as a Foreign Non-main Proceeding.**

A foreign main proceeding is defined by Article 2 to mean “*a foreign proceedings taking place in the State where the debtor has the centre of its main interests.*” By contrast, a foreign non-main proceeding is a foreign proceeding, other than a foreign main proceeding taking place in a State where the debtor has an establishment being a place of operations where the debtor carries out a non-transitory economic activity with human means and goods or services.

Additionally, paragraph 3 of Article 16 stipulates that:

*“In the absence of proof to the contrary, the debtor’s registered office or habitual residence in the case of an individual, is presumed to be the centre of the debtor’s main interests.”*

Thus far in both Europe (under the European Union Bankruptcy Regulation) and the United States (under Chapter 15 of the United States Bankruptcy Code), it is the identification of the “*centre of main interest*” of a debtor which has agitated the most activity before the courts. The principle European case is *In re Eurofood IFSC Ltd* (2006) ECR I-3813, which is a decision of the European Court of Justice. Since that decision, there has been two significant decisions in the United States; *In re SPhinX Ltd* (2007) 371 BR 10 (being a decision of the United States District Court) and *In re Bear Stearns High-Grade Structured Credit Strategies Master Fund, Ltd* (2007) 374 BR 122 (being a decision of Lifland J).

Whilst the decision in *SPhinX* is a decision of the District Court and the decision in *Bear Stearns* is that of a Bankruptcy Judge, it is submitted that the latter decision should be preferred, reflecting, as it does, the considered views of Mr Justice Lifland who is, in my respectful opinion, one of the most distinguished Judges sitting in Bankruptcy in the United States.

So far as concerns the identification of a debtor’s centre of main interest, there are two passages from the judgment in *Bear Stearns* which are relevant:

*“The Bankruptcy Code does not state the type of evidence to rebut the presumption that the COMI is the debtor’s place of registration or incorporation. Various factors could be relevant to such a determination, including: the location of the debtor’s headquarters; the location of those who actually manage the debtor (which, conceivably could be the*

*headquarters of a holding company); the location of the debtor's primary assets; the location of the majority of the debtor's creditors or of a majority of the creditors who would be affected by the case; and/or the jurisdiction whose law would apply to most disputes.”;*

and

*“The Petitioners’ own pleadings provide the evidence to establish that the Funds’ COMI is in the United States, not the Cayman Islands. The only adhesive connection with the Cayman Islands that the Funds have is the fact that they are registered there. Section 1516(c) presumes that the COMI is the place of the debtor’s registered office but only “[i]n the absence of evidence to the contrary.” See 11 U.S.C. § 1516(c). The Verified Petitions have demonstrated such evidence to the contrary: there are no employees or managers in the Cayman Islands, the investment manager for the Funds is located in New York, the Administrator that runs the back-office operations of the Funds is in the United States along with the Funds’ books and records and prior to the commencement of the Foreign Proceeding, all of the Funds’ liquid assets were located in the United States. Although two of the three investors in the High-Grade Fund are also registered Cayman Islands companies, Mr. Whicker, one of the JPL’s testified that both are Bear Stearns entities which appear to have the same minimum Cayman Islands profile as do the Funds. The sole investor in the Enhanced Fund is a U.K. entity. See Transcript of Hearing dated August 27, 2007 at 23. The investor registries are maintained and located in the Republic of Ireland; accounts receivables are located throughout Europe and the United States; counterparties to master repurchase and swap agreements are based both inside and outside the United States but none are claimed to be in the Cayman Islands. Moreover, there apparently exists the possibility that prepetition transactions conducted in the United States may be avoidable under U.S. law. Accordingly, the presumption that the COMI is the place of the Fund’s real seat and therefore their COMI is the United States, the place where the Funds conduct the administration of their interests on a regular basis and is therefore ascertainable by third parties, (see Council Reg. (EC) No. 1346/2000, ¶ 13; see also *In re Eurofood IFSC Ltd.*, supra, at ¶ 32) and, more specifically, is located in this district where principal interests, assets and management are located.*

**(e) Effect of Recognition of Foreign Proceedings.**

The significant point of distinction between recognising a foreign proceeding as a main proceeding as opposed to a non-main proceeding is reflected in the effect of such recognition and the powers exercisable by the foreign administrator.

Where a proceeding is recognised as a foreign main proceeding, then Article 20 provides that:

- “(a) *Commencement or continuation of individual actions or individual proceedings concerning the debtor’s assets, rights, obligations or liabilities is stayed;*
- (b) *Execution against the debtor’s assets is stayed;*
- (c) *The rights to transfer, encumber or otherwise dispose of any assets of the debtor is suspended.”*

Additionally, the foreign administrator may commence proceedings to claw back the benefit of antecedent transactions such as preferences, uncommercial transactions and unfair loans; Article 23. Interestingly, there is no corresponding authority to commence proceedings for breach of the insolvent trading provisions.

By way of contrast, the foreign administrator of a foreign non-main proceeding must apply to the Court for there to be a stay of proceedings or a suspension of the right to dispose of assets; Article 21. Moreover, the foreign administrator must satisfy the Court that that relief relates to assets that, under Australian law, should be administered in the foreign non-main proceeding; Article 21(3). Similarly, if the foreign administrator of a foreign non-main proceeding is to institute proceedings to claw back the benefit of antecedent transactions, the Court must be satisfied that that action also relates to assets that, under Australian law, should be administered in the foreign non-main proceeding; Article 23(2).

**(f) Corporate Groups.**

One criticism which might be made of the Model Law is that it deals with single entities rather than corporate groups. Without seeking to diminish the significance of that criticism, it is equally the case that the Model Law, at least by Article 11, gives the foreign administrator of the group’s parent company standing to begin proceedings in Australia for the purpose of asserting control over any of its subsidiaries which were either incorporated here or which carried on business here. Moreover, to the extent that there may be a competition for control of the administration of any of those subsidiaries, the mechanism for identifying the “*main proceeding*” in relation to that subsidiary provides a means for resolving that competition.

**(g) Conclusion.**

This review of the UNICITRAL Model Law has been necessarily cursory. However, its important aspects are:

- (a) it facilitates recognition of cross-border insolvencies;
- (b) it facilitates the protection of a multi-national debtor’s assets by means similar to those which already obtain under Australian law in respect of domestic insolvencies;

- (c) empowers the foreign administrator to institute proceedings to recover the benefit of antecedent transactions and otherwise to institute or maintain proceedings in this country; and
- (d) leaves open the possibility, subject to the Court being satisfied that Australian creditors are adequately protected, of the foreign administrator assuming general responsibility for the administration of the debtor's estate in this country.



## **FEDERAL COURT OF AUSTRALIA**

### **CURRENT ISSUES AND DEVELOPMENTS CORPORATE INSOLVENCY LAW & PRACTICE**

Richard Fisher AM  
Adjunct Professor, Graduate School of Government

3 April 2008

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## **INTRODUCTION**

1. The position of directors of large corporations as against small to medium-sized corporations in relation to restructuring;
  2. The 2007 amendments to the insolvency provisions of the *Corporations Act 2001* (Cth); and
  3. cross-border insolvency.
-



## The Position of Directors of Larger Corporations

### Implications of Continuous Disclosure Regime

The Continuous Disclosure Rule is as follows:

- “3.1 *Once an entity is or becomes aware of any information concerning it that a reasonable person would expect to have a material effect on the price or value of the entity’s securities, the entity must immediately tell ASX that information.*”
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## The Position of Directors of Large Corporations

### Implications of Continuous Disclosure Regime

#### Exceptions to the Rule

- “3.1A *Listing rule 3.1 does not apply to particular information while all of the following are satisfied.*
- 3.1A.1 *A reasonable person would not expect the information to be disclosed.*
- 3.1A.2 *The information is confidential.*
-



## The Position of Directors of Large Corporations

3.1A.3 *One or more of the following applies.*

- *It would be a breach of a law to disclose the information.*
- *The information concerns an incomplete proposal or negotiation.*
- *The information comprises matters of supposition or is insufficiently definite to warrant disclosure.*
- *The information is generated for the internal management purposes of the entity.*
- *The information is a trade secret.”*



## The Position of Directors of Large Companies

### Implications of Continuous Disclosure Regime

**Critical questions for Directors include:**

1. What constitutes “*material*” information?
2. When is information “*sufficiently certain*” to require disclosure?
3. When will there have been “*partial*” disclosure of information so as to require its more general disclosure?
4. Is it possible to “*opt out*” of the regime?



## The Position of Directors of Large Corporations

### Implications of Continuous Disclosure Regime Material Information

- If information which comes to hand significantly affects the accuracy or currency of information which is already generally available, disclosure of that information must be made: *GPG (Australia trading) Pty Ltd v GIO Australian Holdings Ltd* (2001) 40 ACSR 252.
- Conversion of company's bank facilities to being repayable on demand; *ASIC v Plymin* (2003) 46 ACSR126.
- Notes to Listing Rule 3.1 and Guidance Notes.



## The Position of Directors of Large Corporations

### Implications of Continuous Disclosure Regime

#### Certainty of Information

- *Randall v Aristocrat Leisure Ltd* (unreported Supreme Court, NSW, Einstein J, 8 June 2004); and
- *ASIC v Southcorp Ltd (2)* (2003) 48 ACSR 187.



## The Position of Directors of Large Corporations

### Implications of Continuous Disclosure Regime

#### *“Partial Disclosure”* of Information

*“Partial disclosure”* of information might arise in the circumstance where, even if the relevant information might not otherwise be required to be disclosed under the continuous disclosure regime (as was the case in *ASIC v Southcorp Ltd*), the disclosure of that information to a section of the market may require its general publication.

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## The Position of Directors of Large Corporations

### Implications of Continuous Disclosure Regime

#### *“Opting Out”* of the Regime

- Listing Rule 17.2 provides for suspension of trading.
  - Listing Rule 3.1 is not limited in its application to shares being traded.
  - Application for Listing Rule 3.1 not to apply during suspension of trading?
-



## The Position of Directors of Large Corporations

### Implications of Continuous Disclosure Regime

#### Conclusion

1. Retain an expert to assess whether information which becomes available during the workout negotiation would be such, having regard to information already available, as to have a material effect on the company's share price.
- 



## The Position of Directors of Large Corporations

2. In relation to such information, assess the degree of its certainty when determining whether it should be published.
  3. Further, in relation to such information, review the extent to which it has become available on a selective basis to third parties who are not bound by an obligation of confidence when determining whether it should be published.
  4. So far as concerns parties to those negotiations, their participation should be conditioned by them undertaking a confidentiality agreement.
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## The Position of Directors of Large Corporations

5. Also, in relation to such information, assess the extent to which failure to publish the information may involve the company in misleading and deceptive conduct having regard to information concerning the company which is already publicly available, when determining whether it should be published.
  6. Assess whether the information that is being considered for publication may be affected by the outcome of the negotiations for an informal workout to ascertain whether that exception to the operation of the continuous disclosure rules might apply.
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## The Position of Directors of Large Corporations

7. Give consideration to applying for both the company's shares being suspended from trading and for relief from the ASX to comply with the continuous disclosure rules.
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## 2007 Corporations Act Reforms

### A Non-Reform - Pooling for VA

- Availability of s 447A.
  - Implications of *Australasian Memory Pty Ltd v Brien*.
  - Discretionary considerations.
- 



## Cross – Border Insolvency

### UNICITRAL Model Law

#### 1. Automatic Access to Australian Courts for Foreign Representatives.

Article 9 provides:

*“A foreign representative is entitled to apply directly to a court in this State.”*

Article 11 provides:

*“A foreign representative is entitled to commence a proceeding under Australian law if the conditions for commencing such a proceeding are otherwise met.”*

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## Cross – Border Insolvency UNICITRAL Model Law

### 2. Application for Recognition of Foreign Proceedings

Provided that:

- (i) the application is in respect of a “*foreign proceeding*”;
- (ii) the applicant is a foreign representative;
- (iii) the evidentiary requirements to support the application to which a reference has been made above are satisfied; and
- (iv) The application is made either to this Court or to a Supreme Court.

the application **shall** be granted.

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## Cross – Border Insolvency

### UNICITRAL Model Law

#### Interim Relief

Article 19 provides that “*where relief is urgently needed to protect the assets of the debtor or the interests of creditors*” it is possible to obtain interim relief of a kind which is similar to the appointment of a provisional liquidator under the *Corporations Act* or an interim trustee under the *Bankruptcy Act*.

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## Cross – Border Insolvency

### UNICITRAL Model Law

#### Recognition as a Foreign Main Proceeding or as a Foreign Non-main Proceeding

A foreign main proceeding is “a foreign proceedings taking place in the State where the debtor has the centre of its main interests.”

A foreign non-main proceeding is a foreign proceeding in a State where the debtor carries out a non-transitory economic activity with human means and goods or services.

Paragraph 3 of Article 16 stipulates that:

*“In the absence of proof to the contrary, the debtors registered office or habitual residence in the case of an individual, is presumed to be the centre of the debtor’s main interests.”*



## Cross – Border Insolvency

### UNICITRAL Model Law

#### Recognition as a Foreign Main Proceeding

“Centre of main interest” decisions:

- In re *Eurofood IFSC Ltd* (2006) ECR I-3813;
- in re *SPhinX Ltd* (2007) 371 BR 10;
- In re *Bear Stearns High-Grade Structured Credit Strategies Master Fund, Ltd* (2007) 374 BR122.



## Cross – Border Insolvency

### UNICITRAL Model Law

#### Effect of Recognition of Foreign Proceedings.

Where a proceeding is a foreign main proceeding, then:

- “(a) Commencement or contribution of actions is stayed;*
- (b) Execution against the debtor’s assets is stayed;*
- (c) The rights to dispose of assets is suspended.”*

Proceedings to claw back the benefit of antecedent transactions may be commenced.

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## Cross – Border Insolvency

#### Effect of Recognition of Foreign Proceedings

- Administrator of a foreign non-main proceeding must apply to the Court for there to be a stay of proceedings or a suspension of the right to dispose of assets.
  - Administrator must satisfy the Court that that relief relates to assets that, under Australian law, should be administered in the foreign non-main proceeding.
  - If proceedings to claw back the benefit of antecedent transaction are to be commenced, the Court must be satisfied that that action also relates to assets that, under Australian law, should be administered in the foreign non-main proceeding.
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## Cross – Border Insolvency

### UNICITRAL Model Law

#### Corporate Groups

- Article 11 gives foreign administrator authority to begin proceedings in Australia for the purpose of asserting control over any subsidiary either incorporated here or which carries on business here.
  - Competition for control of the administration of any subsidiary can be resolved by the mechanism for identifying the “*main proceeding*”.
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## Cross – Border Insolvency

### Conclusion

UNICITRAL Model Law:

- (a) facilitates recognition of cross-border insolvency;
  - (b) facilitates the protection of the debtor’s assets;
  - (c) empowers the foreign administrator to institute proceedings; and
  - (d) leaves open the possibility of the foreign administrator assuming general responsibility for the administration of the estate in this country.
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**SPEAKERS NOTES FOR NATIONWIDE SEMINAR ON CORPORATIONS LAW  
-FEDERAL COURT  
-2 APRIL 2008  
Michael Hughes  
Partner - Minter Ellison**

At the recent *7th Annual Practice Insolvency Conference* Matthew Brine presented a paper setting out the Treasury's current thinking on future directions in insolvency regulation. In it he said that the 2007 reform package will not be (in his words) '*Revisited in the near term. Rather, we need to allow some time for these reforms to be bedded down*'.

That backdrop is important, because it means that the challenge of adapting our current laws to accommodate the turn around or rescue culture about which Steve Parbery and Richard Fisher have spoken, will again largely fall to the courts.

In the limited time available, I would like to make some comments about that and try to crystal ball gaze on the kinds of applications that are likely to be made by insolvency practitioners, including under section 447A.

By way of perhaps official recognition, insolvency practitioners welcome and appreciate the support and assistance that is be provided by the court, which is commonly engaged in applications of a kind I have just mentioned, but also for general directions and the like. The limits of what the court can do and in particular its desire to leave matters of a purely commercial nature to the insolvency practitioner is well understood. The extent to which the court will be asked to be more '*hands on*', particularly because of the UNCITRAL reforms about which Richard has spoken will be interesting.

Our economy has changed very much over the last 15 years. The legal underpinnings for raising capital (both debt and equity) are more complex and have a more direct relationship with retail investors than ever before. Promoting a rescue culture therefore involves a careful balancing act between the interests of very diverse stakeholders.

So what kinds of applications do I see being made?

The first concerns the restrictions imposed by lenders by Part 5.3A which only permits them to enforce their security, when it covers all or most of the assets and then only during the decision period. The additional exceptions are where the voluntary administrator consents or the Court's leave has been granted.

This issue will I think be played out against the backdrop of more recent lending practices where loans are often made not to a group, but to individual companies within it, which have been incorporated specifically to pursue a particular venture. These borrowers are sometimes described as bankruptcy remote, because they are intended to have no other liabilities, and for this reason there might be no charge, with the security being limited to the property and other assets which is being developed.

Plainly this was the lenders' bargain.

However, even where the lender does have all assets security, a practice has emerged of lenders not enforcing their security during the decision period, but instead asking for the voluntary administrator's consent purportedly under section 440B to enforce their security after it ends. These consents are of doubtful legal value for a number of reasons, so if the same outcome is to be achieved, there will be a need for the intervention of the court, as occurred in the voluntary administration of the Australian Capital Reserve/Estate Property Group.<sup>1</sup> The commercial context of that matter was further complicated by the fact that the lender in question was itself in administration (representing the interests of the retail note holders), rather than a large financial institution able to take a commercial approach to such matters; although in the current environment I do not see those circumstances as unique.

I raise this issue because practitioners often see value in there being some agreed extension in the decision period, so that the often multiple lenders into a complex group have more time in which to get comfortable that there is at least as good a chance of the lender getting their debt repaid by waiting for a global solution to be investigated and promoted by the voluntary administrator,

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<sup>1</sup> Australian Capital Reserve Limited (Administrators Appointed) v High Tower Investments Pty Limited (Administrators Appointed); in the matter of High Tower Investments Pty Limited (Administrators Appointed) [2007] FCA 1028.

than pushing for the separate enforcement of their own security either with the benefit of such a consent or the leave of the Court.

I concede that the reforms' extension of the decision period from 10 to 13 business days from the time when the lender gets notice of the voluntary administrators' appointment, should go some way to address this issue – and would I submit be a factor for the Court to take into account in its own consideration of the issue – but I do not think it will go away.

The second is in the area of so-called '*ipso facto*' clauses.

In nearly all cases, there will be contracts to which the company is a party which is critical to its ongoing viability. Putting to one side the issue of leases or loan agreements, it might be a corporation whose sole business is to run the outsourced operation of some other concern. Again, this is a common feature of the contemporary economy. The appointment of a voluntary administrator might be the only event on which the counterparty can rely to affectively terminate the contract, and award it to someone else. The voluntary administrator may be able to secure working capital to enable the company to continue to perform all of its obligations under that contract. On the face of it, it therefore seems unfair that the counterparty can exploit the appointment, and terminate the contract, possibly for its own commercial benefit.

Even if it does not do so, the ability to do it, can substantially hamper the voluntary administrator's ability to sell the business and be confident that the contract can be assigned to the purchaser, on the same terms.

It is I think a large leap (to put it mildly) to expect the court to make an order under section 447A, to any effect vary the operation of Part 5.3A insofar as an individual particular corporation is concerned so that the counterparty is no longer able to rely on a clause of this kind which was always a part of its bargain.

Nevertheless, it may not be a large leap for the court to be asked to grant relief, in the nature of relief against forfeiture to grant an injunction to restrain the termination of the contract, perhaps for a limited period of time, in the circumstances I have just described, namely that the contract

is in all other respects being performed and will continue to be performed during the course of the voluntary administration.

The third and final area on which I wish to mention is that of the likely intersection of the laws relating to the winding up of corporations, and those concerning the windings up of trusts. It might be thought that there is nothing new here legally, and this may well be the case, but the point I wish to highlight is the recent proliferation of trusts and sub trusts as vehicles which raise capital, pursue ventures or hold assets in a corporate group.

In the same vein, the Court will be aware through dealing with schemes of arrangements that in some case a shareholder will not only hold a share in a listed corporation, but an interest in an asset holding (trust) fund, to which that share has been stapled. The responsible entity will itself be a subsidiary of the listed vehicle. The corporation and the fund will often borrow money from different lenders for different purposes. In some case, the fund may have itself lent funds to the listed entity.

In the context of Richard's discussion about pooling, ordinary creditors of the corporation may have dealt with it on the basis that it had recourse to the assets of the fund. And there will be common directors and employees giving rise to issues of conflict of interest and the like.

The comment I make here, is that if there is to be an insolvency of such a group, I can readily see the Court being asked to take a role, especially in resolving issues as between competing interests, and in connection with the fund.

As I said earlier, insolvency practitioners welcome and appreciate the support and assistance that is be provided by the court, and the issues I have just highlighted suggest to me at least that it will be being called upon again and more often in the not too distant future.

# Insolvency Seminar - Panel Presentation on Disqualification under APRA Administered Legislation

## Patrick Meaney

### 1. Why is it relevant to Insolvency?

- Disqualification is relevant to the pre-administration conduct of directors, officers, auditors and actuaries of APRA regulated institutions
- Most APRA disqualifications to date have related to concealing information from APRA about the financial position of APRA regulated institutions:
  - HIH
  - Zurich
  - Gen Re
- Directors and officers of entities in financial distress are often in denial about the seriousness of the problem which may result in resort to devices that mislead the regulator
  - professional advisers may wittingly or unwittingly be parties to such subterfuge
- The risk of disqualification is a deterrent to directors, officers and advisers engaging in such conduct

### 2. The Old Regime

- Administrative decisions with an internal and external review (AAT)
- Disqualifications are permanent
- Grounds for disqualification different across Acts

### **3. The Financial Sector Legislation Amendment (Review of Prudential Decisions) Bill 2008**

- Has passed the House and Senate
  - Will go back to House in May for third reading and should get assent in June

#### **a. Nature of Disqualification Orders**

##### **(i) Period of Time**

- “for a period the Court considers appropriate”
  - cf under existing regime disqualification is permanent or until revoked
  - addresses “proportionality” issue

##### **(ii) Roles Disqualified from**

- Directors and senior managers of:
  - ADIs
  - general insurers
  - NOHCs of ADIs or general insurers
- Directors and executive officers of life companies
- Senior managers of a foreign ADI
- Senior managers or agents of foreign insurers
- Trustees and responsible officers of:
  - Trustees
  - Investment Managers
  - Custodians

Auditors of:

- ADIs
  - ADI NOHCs
  - general insurers
  - life insurers
  - RSA providers
  - Superannuation entities
- Actuaries of:
    - General insurers
    - Life insurers
    - Superannuation entities

**b. Procedure for Disqualification**

- Only APRA can apply to the Federal Court for a disqualification order under all industry Acts
  - Except disqualifications relating to ATO regulated institutions will remain administrative
- Under the Banking Act, the Insurance Act, the SIS Act and the Life Insurance Act any person can be subject to a disqualified order
  - although as a practical matter there would be no utility in seeking to disqualify an unqualified person from being an actuary or auditor
  - the point is that it is not necessary for the individual to have been working in the relevant industry for them to be disqualified under that legislation
- If a disqualification order is made, APRA must:
  - notify the individual and any regulated institution for which the person acts in the relevant capacity; and
  - publish a notice in the Gazette

### c. **Grounds for Disqualification**

#### (i) The Banking Act, Insurance Act, and Life Insurance Act

- the grounds for disqualification are that:
  - the person is not a fit and proper to act in the relevant capacity; and
  - the disqualification is justified.
- In relation to fit and proper the Court may take into account:
  - the relevant fit and proper standards and any relevant fit and proper regulations; and
  - anything else the Court considers relevant
- In relation to whether the disqualification is justified the Court may have regard to:
  - in respect of disqualification from acting as a director, senior manager etc.,
    - the person's conduct in relation to the management, business or property of any corporation;
  - in respect of disqualification from acting as an auditor or actuary,
    - the person's conduct in relation to the functions or duties of an auditor or actuary under the relevant Act.

#### (ii) The Superannuation Industry (Supervision) Act (**only APRA regulated**)

- The grounds for disqualification from acting as a **trustee or responsible officer of a trustee, investment manager or custodian** are firstly:

- contravention(s) by the person of the SIS Act or the Financial Sector Collection of Data Act and the nature, seriousness or number of the contravention(s) warrant disqualification; or
  - for persons who are or were responsible officers of trustees, custodians or investment managers:
    - the relevant corporation contravened SIS or FSCODA while the person was a responsible officer and the nature, seriousness or number of the contravention(s) warrant disqualification;
  - the person is otherwise not fit and proper to act in the relevant capacity; and
- secondly that the disqualification is justified
    - and in deciding this may have regard to the individual's conduct in relation to the management, business or property of any corporation.
- The grounds for disqualification from acting as **an auditor** of a superannuation entity are:
    - the person has failed to carry out or adequately or properly perform duties:
      - under SIS, the FSCODA or regulations or
      - any other acts required by a law of the Commonwealth to be performed by an auditor; or
    - is otherwise not fit and proper to be an approved auditor for the purposes of the Act.

(iii) The Retirement Savings Act

- an auditor can be disqualified for:
  - failing to carry out or adequately perform duties under the RSA, the FSCODA or regulations or an other acts required by a law of the Commonwealth to be performed by an auditor; or
  - otherwise not being fit and proper to be an approved auditor for the purposes of the Act.

(iv) In Summary

- APRA could apply to the Court for a single proceeding to disqualify a person from being a director or senior manager under all four industry Acts simultaneously in respect of conduct in only one industry
- APRA could disqualify an auditor under SIS and RSA for conduct under other 3 Acts but not vice versa
  - unless done under the otherwise not fit and proper head

FEDERAL COURT CORPORATIONS LAW SEMINAR  
2 APRIL 2008

Maree Blake, Director Corporations and Insolvency, ASIC

**The comments in this paper represent the author's views  
and are not necessarily the views of ASIC**

Thank you Judge for the opportunity to be part of today's panel.

By reference to the presentation by Steve Parbery, I would like to offer some comments, rather than any concluded view, on the developing debate regarding application of the business judgement rule to the insolvent trading provisions, and also some observations on possible drivers to that suggestion.

The debate appears to be directed towards facilitation of genuine restructuring/workout situations, which are more likely to involve the larger corporate sector than the SME sector, and have more relevance and application in less buoyant market conditions such as those currently being experienced.

I agree with Steve's comments regarding the various distinctions between large enterprises and the SME sector – in practical terms, there are significant differences.

In regard to the SME sector, and as Steve has noted, most directors in that sector have all their personal assets secured to their financier/major trade creditors, and have everything, but in a sense nothing more, to lose from continuing to trade even when the situation is irretrievable. In such cases, it is inevitably too late for a genuine restructure.

Matters undertaken by ASIC in relation to insolvent trading, involve criminal prosecutions requiring the dishonesty factor, or civil penalty proceedings involving serious contravention. Such matters are quite different to the circumstances of a genuine restructure situation, and the business judgement rule would have no role. It therefore seems unlikely that the debate on an extension of the business judgement rule to insolvent trading is being driven by the actions of the corporate regulator.

We are left then, on one hand, with the suggestion of a need for more flexibility to conduct workouts probably most applicable to the larger corporate sector, and on the other, directors perceiving increasing potential exposure, for example, from class actions and litigation funding.

An important consideration in the debate would be the overall financial and economic benefits that should come from preserving and maximising business value and returns through a rehabilitation process. There has also been some recent commentary as to whether or not there should be regulation of litigation funding.

So perhaps it is timely and beneficial for discussions regarding any extension of the business judgement rule to insolvent trading, to be expanded to a strategic and holistic consideration of all relevant factors - the principal drivers, genuine corporate rehabilitation needs, current legislation, benefits of the suggested changes, and importantly, the interests of the various stakeholders/beneficiaries, including unsecured creditors particularly where complex circumstances are present.

In regard to the business judgement rule and insolvency, I would like to offer a comment relating to establishing a state of insolvency. A genuine restructure process, particularly in the larger corporate sector, will need to have in place the ongoing support of its financiers, and often, also its principal creditors. While recognising the position for directors in difficult financial circumstances, I query whether insolvency would be able to be established in circumstances where continued trading was with the ongoing support of financiers and principal creditors, as would usually be the case in a genuine restructure process. If, in such circumstances, insolvency was unlikely to be established, would the business judgement rule defence be needed or add value?

As Steve said, we currently have characteristically distinct corporate sectors, and a one size fits all legislation. I would suggest that in the context of the business judgement rule debate, there may be 3 distinct sectors to be considered – the small enterprise sector which has been characterised, the large corporates which have significant infrastructure and the ability to access the best professional advice, and a middle sector, which is significant in business terms but may not have the infrastructure and financial capacities of a large corporate – perhaps it is that sector where the perceived need for more protection from the insolvent trading provisions is most prevalent.

Thank you

## Conclusion

We have received an informative and stimulating series of contributions. The topic was broad, and each speaker had a different perspective.

The first principal speaker was Mr Stephen Parbery, a very experienced insolvency practitioner with accountancy qualifications and background. He explored the differences between large corporations, on the one hand, and small to medium corporations, on the other, concerning potential insolvent trading. He raised the issue as to whether there should be a two tier system of insolvent trading provisions, and whether the defence to insolvent trading should include a business judgment rule or something similar. He referred to United Kingdom and Canadian provisions. He also commented on the significance of the adoption by Australia of the UNCITRAL Model Law on Cross-Border Insolvency.

The other principal speaker was Mr Richard Fisher, a lawyer of great experience in this area who is presently General Counsel and Adjunct Professor at the Graduate School of Government, University of Sydney. He explored the effect of the continuous disclosure rule upon the directors of public listed companies when formulating a reconstruction proposal. He then dealt with the 2007 Amendments to the *Corporations Act* that introduced “pooling” in liquidation but not in voluntary administration. He discussed the possible application of s 447A(1) so far as the latter was concerned. He also examined some important aspects of the UNCITRAL Model Law on Cross-Border Insolvency.

The first commentary was by Mr Michael Hughes, a partner of Minter Ellison. He elaborated on three issues: the restrictions imposed on lenders with security by Pt 5.3A; “*ipso facto*” clauses; and the intersection of the winding up of companies and the winding up of trusts.

Mr Patrick Meaney, who has been General Counsel at the Australian Prudential Regulation Authority since 2005, was the next commentator. He discussed the disqualification of directors, officers, auditors and actuaries of institutions regulated by APRA. He particularly analysed the impending change of regime pursuant to the Financial Sector Legislation Amendment (Review of Prudential Decisions) Bill 2008, providing for disqualification on application by APRA to the Federal Court.

The last commentator was Ms Maree Blake, the Director Corporations and Insolvency at the Australian Securities and Investments Commission. She has an accountancy background in the private sector. She concentrated upon various aspects of the possible application of the business judgment rule to insolvent trading provisions, particularly in relation to “workouts”.

Justice Roger Gyles AO