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Opinion

The Duke Group Ltd (in liquidation) (**TDGL**)

12 April 2010

Opinion

1 I am asked to advise on three questions:

1.1 is it appropriate for the liquidator to proffer a fresh invitation to shareholders to submit proofs?;

1.2 what form should that invitation take?; and

1.3 what categories of shareholders might have admissible claims?

Background

2 The liquidator has dealt with nearly all the potential claimants under section 438(2) of the *Companies (South Australia) Code* on the basis that TDGL was insolvent. I am instructed that there remain only a few relatively minor outstanding claims under section 438(2). These claims should not prevent the liquidator from considering other claims under section 438(1) now that it is clear that TDGL has become solvent. It is now appropriate for the liquidator to invite a second round of proofs under s 438(1) of the *Companies (South Australia) Code*. As Barrett J stated in *Re Kershaw (as liquidator of EquiticorpTasman Ltd)* [2005] NSWSC 313; 54 ACSR 214 at [16]:

> … once a surplus emerges (in a sense I shall discuss presently) in a winding up that has proceeded according to the bankruptcy rules imported by s 438(2) of the Companies (New South Wales) Code, claims admissible under s 438(1) but originally precluded by s438(2) become cognisable in that winding up.

Moreover, Barrett J declared at [24] that '*claims that become admissible under s438(1) but were previously precluded by s438(2) must be recognised and dealt in full with before claims for post-liquidation interest are entertained*'. In my respectful opinion, this approach should be adopted in the present case.

The First Question

3 Against this background, it is necessary to determine whether the liquidator should proffer a fresh invitation to shareholders to submit proofs.

4 At the outset, it may be noted that CAMAC has taken the view that liquidators are not required to investigate whether shareholders have claims based on *Sons of Gwalia Limited v Margaretic* (2007) 81 ALJR 525.

5 CAMAC has reported that it does not consider that liquidators are currently under an obligation to search the company's share register to notify all shareholders merely because a claim for misleading or deceptive conduct arising out of a breach of the company's duty of continuous disclosure has been lodged by one or more persons. CAMAC believes that the onus should be on aggrieved shareholders to identify themselves and substantiate their claims: (CAMAC Report (December 2008), para 4.3, p72). CAMAC did not comment on allegations of misleading or deceptive conduct through direct dealings with shareholders.

6 These robust views are not supported by the authorities. The following principles emerge from the authorities:

6.1 A liquidator is obliged to enquire into all claims, he has a duty to ascertain '*by direct enquiry whether a claim is being pressed*'. The liquidator has a duty not merely to advertise but to *write to creditors of whose existence he is aware*: *Harry Gourdias Pty Ltd v Port Adelaide Freezers Pty Ltd* (1992) 7 ACSR 303.

6.2 A liquidator is not absolved of this responsibility by the failure of the creditor to respond to an advertisement where the liquidator is otherwise aware of that creditor's claim: *Harry Gourdias Pty Ltd v Port Adelaide Freezers Pty Ltd* (1992) 7 ACSR 303 at 306.

6.3 Therefore, a liquidator has a duty to write to the creditors of whose existence he knows, and who do not send in claims, and *ask them if they have any claim*: *Pulsford v Devenish* [1903] 2 Ch 625 at 631 per Farwell J.

6.4 A person claiming to be a creditor must provide sufficient particulars in the proof of debt to identify the existence of the debt. However, this requirement must be considered in the context of the pre-existing knowledge of the liquidator assessing the proof of debt: *Kammal v Jones as liquidator and chairman of a meeting of creditors of creditors of Ravenswood Resort Pty Ltd (in liquidation)* (2005) 56 ACSR 250.

6.5 Regulation 120(2) provides, inter alia, that a liquidator must give notice in Form 130 to every person who, to the knowledge of the liquidator, claims to be a creditor of the company, and whose debt has not been admitted. Strictly speaking, this merely requires the liquidator to write to persons who, to his knowledge, are claiming to be creditors of the company and not to persons who happen to fall in categories who might have claims as creditors of the company. However, liquidators have general law duties to act impartially between creditors. A fiduciary must not act in such a way as to favour one class of creditors over another: *Re Lepine* [1892] 1 Ch 210 at 219; *Re Charteris* [1917] 2 Ch 379 at 388-389; *Re Mitchell* [1955] VLR 120 at 123; *Re Zimpel* [1903] WAR 181 at 174 (trustees). If there is a dispute between rival claimants, a fiduciary must remain neutral: *Alsop Wilkinson (a firm) v Neary* [1995] 1 All ER 431 at 435. Similar principles have been applied to company directors: *Whitehouse v Carlton Hotel Pty Ltd* (1987) 162 CLR 285 at 289. No doubt, these principles would also be applied to an official liquidator who, as an officer of the court, has fiduciary duties to all interested parties. The duty to act impartially requires the liquidator to go further than Regulation 120(2).

6.6 The liquidator is in certain circumstances obliged to inform creditors of the facts known to him. See *Re Autolook Pty Ltd* (1983) 8 ACLR 419 (dealing with understated claims). The liquidator is required by Regulation 137 of *The Companies (South Australia) Regulations* to give written notice of his intention to declare a dividend to any person who, to the knowledge of the liquidator *might claim to be* a creditor of the company. While this provision deals with the declaration of dividends, rather than proofs of debt, the two

issues are ultimately related. There is no point in taking a limited view of the liquidator's responsibilities in inviting proofs of debt but an expansive view of his responsibilities in declaring dividends. Ultimately, the liquidator is concerned about his obligations in relation to the distribution of the available assets. The proof of debt procedure is merely the first step in that procedure.

7 In the present case, the liquidator has a duty, not merely to place advertisements to invite claims by shareholders, but also to write to shareholders and former shareholders of whose existence he is aware. Even if shareholders or former shareholders do not respond to the liquidator's advertisements, he must write to these parties to inquire whether they have claims against TDGL. These parties are expected to provide sufficient particulars in their proofs of debt to identify the existence of their debt or claim.

8 In the present case, where the liquidator has obtained several opinions from senior counsel and other senior legal practitioners about the likely grounds on which shareholders and former shareholders might have a claim against TDGL, in my opinion, the liquidator cannot simply rely upon advertisements to invite proofs of debt. Indeed, this proposition is fortified by the directions given to the liquidator in relation to allotee shareholders.

9 In my opinion, therefore, the liquidator is entitled, and indeed obliged, to proffer a fresh invitation to shareholders (other than the Allottees) to submit proofs in the second round of proofs under section 438(1) of the *Companies (South Australia) Code*.

The Second Question

10 As mentioned earlier, it is clear from the authorities that the liquidator may not simply rely on advertisements to invite the proofs of debt by shareholders and former shareholders. The liquidator must write to any parties who he believes have potential claims against the company and who have no already had their claims determined under section 438(2) of the *Companies (South Australia) Code*.

11 CAMAC has recommended that shareholders' claims relating to the acquisition of shares should stipulate the following information:

11.1 the date or dates of acquisition;

11.2 the number of securities acquired on each occasion;

11.3 the consideration for the acquisition of the securities; and

11.4 the corporate misconduct relied upon, including the precise misrepresentation and any supporting evidence.

12 CAMAC has also suggested that the particulars of the claim be verified by a statutory declaration (Australian Government, Corporations and Markets Advisory Committee, *Shareholder Claims Against Insolvent Companies: Implications of the Sons of Gwalia decision* (CAMAC Report) (December 2008), para 4.4, p75).

13 As we have seen, the claimant's obligation to provide sufficient particulars in his proof of debt to identify the existence of his debt or claim is affected by the liquidator's pre-existing knowledge of the bases of the shareholders' claims. In the present case, the liquidator's pre-existing knowledge is relatively high because it is based on a thorough examination of the available books and records of TDGL, the opinions of senior counsel and senior practitioners, the judgment of Mulligan J and court directions in relation to the claims of Allottee shareholders under section 438(2) of the *Companies (South Australia) Code*.

14 In my opinion, this relatively high level of knowledge requires the liquidator to write to possible claimants, not merely to invite proofs of debt, but also to outline the possible grounds on which the shareholders and former shareholders may have claims against TDGL. The liquidator's letter to shareholders and former shareholders should also indicate in general terms what type of particulars he needs to determine whether to admit or reject the proofs of debt. It should also recommend that shareholders obtain independent legal advice about their formal proofs of debt before lodging them with the liquidator.

The Third Question

15 The possible claimants fall into three broad categories:

15.1 Allottees;

15.2 Transferees; and

15.3 Subscribers.

16 The liquidator has received advice that there may be sub-categories of shareholders who may have claims based on inferred reliance and even shareholders who have non-reliance claims. Let us take each of these categories in turn.

The Allottees

17 I am instructed that all the Allottees have been dealt with under section 438(2) of the *Companies (South Australia) Code* because their claims arose in relation to a bipartite contract with TDGL. In theory, Allottees might have a separate claim for unliquidated damages for misleading or deceptive conduct under section 438(1) of the *Companies Code*, now that TDGL is solvent.

18 However, this separate claim would be futile if, as I am instructed, the Allottees are unable to prove that they suffered any loss or damage as a result of the misleading or deceptive conduct. If they are actually better off as a result of the transaction, then they have no claim under section 52 of the *Trade Practices Act* 1974 (Cth) or its counterpart, section 56 of the *Fair Trading Act* 1987 (SA).

19 The liquidator has already determined that the Allottees have no provable debt under section 438(2) because they cannot prove that they have suffered loss or damage. This determination is equally relevant to their claims based on section 438(1). Hence, the Allottees should not be admitted to proof under section 438(1). Indeed, in my opinion, it is not necessary for the liquidator to advertise for further proofs from Allottees or to write to Allottees inviting proofs under section 438(1). They have no

provable claims under section 438(1) because an essential element of that claim is missing. It is not just that they cannot prove loss or damage; rather, their problem is that it is clear that they suffered no loss or damage. They were better off as a result of the transaction.

The Subscribers

20 Subscribers fall in a different category and different principles apply to their claims. In considering the claims of Subscribers under section 438(1) of the *Companies (South Australia) Code*, the liquidator must consider whether they suffered loss or damage as a result of misleading or deceptive conduct. It is established that loss or damage for the purposes of section 82 of the *Trade Practices Act* 1974 (Cth) can arise where a breach of section 52 leads to a failure to act, as distinct from positive action in reliance on the misleading or deceptive conduct: *Gates v CML Assurance Society Ltd* (1986) 160 CLR 1 at 13; *Sellars v Adelaide Petroleum Ltd NL* (1994) 179 CLR 332 at 348; *Kaze Constructions Pty Ltd v Housing Indemnity Australia Pty Ltd* (1990) ATP 40-417. But where there is a claim for loss or damage suffered by refraining from taking an opportunity to avoid it (for example by selling shares), the plaintiff must prove not only that the opportunity (to sell) was available but also that he would have taken the opportunity if the breach of contravention of section 52 had not occurred: *Gates v City Mutual Life Assurance Society Ltd* (1986) 160 CLR 1 at 13-14; *Zoneff v Elcomm Credit Union Ltd* (1990) ATPR 41-058 at 51-745 - 51-746. In other words, the Subscribers would have to prove that they had the opportunity to sell their shares for more than the value of the shares in the liquidation and that they would have sold their shares if the misleading or deceptive conduct had not occurred.

21 It will be difficult for Subscribers to provide particulars that will fortify their claims if they allege that they suffered loss or damage merely be refraining from selling their shares. Nevertheless, they should be advised by the liquidator that they are required to provide such proof if they wish their claim to be admitted to proof.

22 Some Subscribers may have suffered loss or damage by *selling their shares* in reliance on the misleading or deceptive conduct of TDGL or its directors. This is a matter that warrants further investigation. Subscribers in this category should be invited to provide particulars of their claims so that they can be assessed by the liquidator.

The Transferees

23 The first category of Transferees is Transferees who acquired shares in Kia Ora or TDGL from third parties prior to the WUL Takeover and retained them until the date of liquidation and suffered a loss through a diminution in the value of their shares as a result of the WUL Takeover in late 1987 and the Reverse Takeover in June 1988. They would appear to be in the same boat as the Subscribers. In order to establish their claims they must prove that they had the opportunity to dispose of their shares and that they refrained from taking that opportunity because of the misleading information. In my opinion they cannot establish their claims on the basis of inferred reliance or reliance by another party (no reliance). They can only prove their claim by establishing that they refrained from selling their shares because they actually relied on the misleading or deceptive conduct of TDGL or its directors. This will be very difficult to prove.

24 The second category of Transferee is Transferees who acquired shares *after* the WUL Takeover or after the Reverse Takeover and retained them until the liquidation of TDGL. They suffered a loss as a result of the diminution in the value of their shares as a result of the Reverse Takeover. They would have a valid claim if they could show that they actually relied on a misleading representation made to them by TDGL or its directors when then entered into their contracts to acquire shares in TDGL from third parties. If they can show that they relied on misleading information published by Kia Ora, TDGL or its directors before they acquired their shares, then they have a valid claim. It should not matter whether the misrepresentation was made specifically to them as long as they acted on the misleading information. Even Transferees who sold their shares at a loss before the liquidation would have a valid claim is they could prove actual reliance. It is sufficient if the misrepresentation was merely a non-trivial cause of their acquisition of their shares.

25 In the absence of a direct misrepresentation to these Transferees, they cannot rely upon inferred reliance because the court will not infer that they entered into the contract to acquire their shares from the third parties as a result of the misleading or deceptive conduct of Kia Ora/TDGL or its directors.

26 It is even less likely that these Transferees will be able to establish a non-reliance claim under section 52 of the *Trade Practices Act* 1974 (Cth). The fact that misrepresentations were *made to other parties* does not have a sufficiently direct, causal link with the losses suffered by these Transferees. It is pressing the no-reliance cases too far to argue that they would not have suffered their loss unless the takeovers proceeded.

27 The onus is on the Transferees to show that the misleading or deceptive conduct of Kia Ora or its directors caused the other shareholders (or at least 90% of them) to accept the takeover offer. The misleading or deceptive conduct may have played *some* part in inducing *some* of the shareholders to accept the takeover offer but can it be confidently asserted that it played some part in inducing all of the shareholders to accept the takeover offer?

28 In *Janssen-Cilag Pty Ltd v Pfizer Pty Ltd* (1992) 37 FCR 526 Lockhart J held that the right to recover loss or damage under section 82 of the *Trade Practices Act* 1974 (Cth) is not confined to persons who rely on the representations which constitute contraventions of section 52. But the loss or damage must directly result from or be caused by the respondent's conduct (at p530). The respondents' conduct must be a '*real or direct or effective cause*' (p530) of the plaintiff's loss or damage.

29 This principle has been readily applied in cases of passing off and misleading advertising. It was also applied in relation to a misrepresentation to the Queensland Government by one participant in a mining joint venture. The misrepresentation induced the Government to refuse to renew the plaintiff's Authority to Prospect: *Pacific Coal Pty Ltd v Idemitsu Queensland Pty Ltd* (1992) ATPR (Digest) 46-094 at -53, 362. As Ryan J concluded 'common sense would indicate that the representations played at least some part in inducing the Government to take those decisions'.

30 While Justice Lockhart clearly recognised in *Janssen-Cilag Pty Ltd v Pfizer Pty Ltd* (1992) 37 FCR 526 that there is no absolute requirement of reliance on the part of the

applicant, all applicants still retain the onus of proving the requisite element of directness or proximity necessary to constitute causation at law: *Hayne v Top Slice Deli Pty Ltd* (1995) 17 ATPR (Digest) 46-147 at 52,152.

31 Australian law may be ready to accept that reliance by a shareholder on a person or persons who had themselves relied on misleading representations by a company or others may be sufficient causation in the case of corporate misstatements or non-disclosure. But it is not clear that Australian law is ready to accept a form of presumed reliance by Transferees on other persons who had themselves relied on misleading representations. This is one step too far. It would be tantamount to accepting a 'fraud on the market' theory, which Australian courts have steadfastly refused to recognise. See M Duffy, *Fraud on the Market: Judicial Approaches to Causation and Loss from Securities Nondisclosure in the United States, Canada and Australia* [2005] MULR 20 at 29. It is pertinent to recall Lockhart J's comment in *Janssen-Cilag Pty Ltd v Pfizer Pty Ltd* (1992) 37 FCR 526 at 531:

> For a person to recover under the section he must suffer loss or damage by reason of or as a result of the contravention. *There is nothing unduly wide about that*. (Emphasis added).

32 In the present case, it is difficult to find the necessary direct causal link between the representation to the third party and the loss or damage to the claimant. No doubt, some Transferees relied on the misrepresentations by TDGL or its directors but their reliance did not inevitably cause the other Transferees to suffer loss or damage. In my opinion, recognising non-reliance claims would be an unduly wide interpretation of the causation requirement

33 It may be true as paragraph 101.5 of the DMAW advice to liquidator (dated 18 July 2008) asserts:

> the claimant (transferees) suffered a direct loss in the value of shares held by reason of the takeover which was consequential upon the reliance by the voting shareholders upon the misleading information.

34 But it is difficult to agree with the conclusion that:

> The conduct is sufficiently causative of the loss because the voting shareholders are taken to have been induced to act by virtue of the information and this, inevitably and without any further act on the part of the claimant, resulted in a diminution in the value of his shares.

35 It might be different if the shares of the Transferees were compulsorily acquired as a result of a 90% approval vote in favour of the takeover by parties who relied upon the misleading information or who, the court might infer, relied upon the misleading information. This is a highly contentious point and it would not, in my opinion, be advisable for the liquidator to determine proofs of debt on this basis.

36 Inferred reliance is less contentious. The courts are often prepared to find that reliance can be inferred from the fact that a misrepresentation was made to a party to induce him to enter into a transaction and the party does, in fact, enter into the transaction. In other words, if the claimants can prove that a misleading representation was made to them and they took shares in TDGL after that

misrepresentation was made, the court will be prepared to infer reliance. And so should the liquidator.

37 In summary, the liquidator should accept proofs of debt based on actual or inferred reliance but should not accept proofs of debt based on no-reliance or the reliance of third parties in the absence of a definitive ruling of a court. Directors do not amount to a judicial determination raising an estoppel binding on other parties: *Re Blackbird Pies (Management) Pty Ltd (No 2)* [1970] QWN 14; *Re TTC (SA) Pty Ltd* (in liq) formerly Tom the Cheap SA Pty Ltd (1983) 7 ACLR 784; 6 ACLC 914. But directions will protect the liquidator against allegations of a breach of duty: *Re Atkinson* [1971] 612 at 615-616; *Re Lemon Tree Passage & Districts RSL and Citizens Club Co-operative Ltd* (1988) 6 ACLC 24 at 27; 11 ACLR 796.

38 Judicial directions will protect the liquidator against any claims that he has breached his duties in adjudicating upon proofs but they do not determine substantive rights and they cannot prevent a non-reliance claimant from litigating the issue or appealing against a rejection of his proof of debt.

39 The liquidator has received legal advice that he should reject the claim by DHL as a Transferee of shares from the Abbott interests contemporaneously with the Reverse Takeover because '*DHL has not established that it suffered any loss by reason of the acquisition of the shares from the Abbott interests*' (see page 7, paragraph 32 of the Memorandum of Advice provided by DMAW on 18 July 2008). The implication is that the shares held by the Abbott interests were worthless and that DHL suffered no loss because the cash paid by TDGL to DHL pursuant to the Reverse Takeover Agreement was used to finance the acquisition by DHL of the shares of the Abbott interests. If this was so, then DHL appear to have suffered no loss or damage as a Transferee and its proof under section 438(1) should be rejected. This is a matter that warrants further investigation but this reasoning appears to be sound.

40 41. The final group of Transferees are those shareholders who acquired shares after the WUL Takeover and in whole or in part before the Reverse Takeover and who retained those shares until the liquidation. These Transferees may have provable debts under section 438(1) of the *Companies (South Australia) Code* on the basis of actual or inferred reliance on misleading statements by or on behalf of TDGL. But, once again, non-reliance claims should not be admitted without a declaration or definitive ruling from a court. The Transferee claimants might be extended to include Transferee shareholders who disposed of their shares at a loss before the liquidation of TDGL but they must prove actual or inferred reliance before their claims can be admitted

Conclusions

41 It is not necessary for the liquidator to adjudicate further on the claims of Allottees because there is sufficient evidence that they have suffered no loss or damage. The claims of Allottees should not be admitted under section 438(1) of the *Companies (South Australia) Code*.

42 Most Subscribers will be unable to provide proof that they would have sold their shares but for the misleading or deceptive conduct. However, the liquidator should write to the Subscribers advising them the particulars of claim he requires from them.

43 Some Subscribers may have sold their shares before the liquidation. If they lodge a proof of debt they will have to prove that they suffered a loss as a result of misleading or deceptive conduct by or on behalf of TDGL. This matter warrants further investigation but suffice it to say that these Subscribers will have difficulty proving causation.

44 Transferee shareholders will have the usual problems proving actual reliance but they can establish their claim on the basis of inferred reliance. They must, however, prove that they were aware of the misrepresentation, even if it was made to other parties.

45 The liquidator should not admit no-reliance claims without a court ruling because a direct causal link is not established between the misleading or deceptive conduct and the loss or damage suffered by the parties who are unable to claim on the basis of actual or inferred reliance.

46 It appears that the liquidator would be justified rejecting the claim by DHL under section 438(1) on the basis that no loss was incurred in acquiring the Abbott interests. While this conclusion appears to be sound it should be rigorously tested against the facts or assumptions on which it is based.

47 Transferee shareholders who acquired shares after the WUL Takeover and before the Reverse Takeover and who retained these shares until liquidation may be admitted to proof under section 438(1) only on the basis of actual or inferred reliance (but not no-reliance).

48 Transferee shareholders who sold their shares at a loss before the liquidation may also be admitted to proof on the basis of actual or inferred reliance if the misleading representation was made to them.

49 The liquidator could seek directions from the court as to the procedure he should follow in the second round of proofs under section 438(1) of the *Companies (South Australia) Code*. It is likely that these directions will be similar to the directions given in relation to the first round of proofs involving the Allottees. However, in this application the liquidator could seek directions as to whether it would be sufficient for him to advertise locally and internationally (including in Frankfurt) and write to all shareholders (other than Allottees) at their last known address according to the company's records inviting them to submit formal proofs of debt containing the information recommended by CAMAC and verified by statutory declaration. Directions could also be sought as to whether the liquidator should draw the shareholders' attention to possible claims they may have against the company and the information he will require in order to adjudicate upon such claims. This is a delicate issue because the liquidator is not expected to act as advocate of the claims of certain creditors at the expense of others. At all times he must act in a neutral, impartial manner in dealing with creditors. However, any directions will not amount to a determination of any questions arising in relation to the proofs of debt. The directions will protect the liquidator against any allegations of a breach of duty. They will not resolve any disputes that may later arise if proofs of debt are rejected. Such disputes would normally be dealt with as appeals from the liquidator's decisions in adjudicating upon the proofs.

50 The range of directions sought from the court could be expanded to cover the following matters raised in this Opinion:

50.1 whether Allottees need to be invited (by advertisement and individual notices) to submit proofs of debt in the second round under section 438(1);

50.2 whether it is correct that Subscribers will be required to prove that they had an opportunity to sell and that they refrained from taking that opportunity because of misleading or deceptive conduct of TDGL or its directors;

50.3 whether the right to prove will be restricted to those Transferees who can show actual or inferred reliance on a misleading representation ;

50.4 whether the liquidator should accept the proposition that certain Transferees (the non-reliance claimants) are entitled to prove simply because they happen to be shareholders who suffered loss or damage as a result of the takeovers even if they did not rely on a misrepresentation;

50.5 whether the liquidator would be justified in rejecting the DHL claim as transferee of shares from the Abbott interests on the information currently available to him;

50.6 the court might be reluctant to give directions on all these issues because some of them (eg 50.5) involve questions of fact but there is no harm in asking.