Section 52
Trade Practices Act
and
Dealings in Securities

Report by Corporations Law Simplification Task Force

September 1996

Corporations Law Simplification Task Force

Dr Robert Eagleson, Consultant in Plain English, Mallesons Stephen Jaques

Mr Ian Govey, Principal Adviser, Business Law, Department of the Treasury

Ms Claire Grose, Partner, Freehill Hollingdale & Page

Mr Vince Robinson, First Assistant Parliamentary Counsel, Office of Parliamentary Counsel

Corporations Law Simplification Consultative Group

Mr Leigh Hall (Chair), Deputy Managing Director, AMP Investments Australia Ltd

Dr Robert Austin, Partner, Minter Ellison

Ms Jennifer Fear, Managing Director, Poynton Corporate Ltd

Mr Geoffrey Heeley, Company Director

Mr Chris Hoey, Chief Executive, Hardware Association of Queensland

Mr John Humphrey, Partner, Corrs Chambers Westgarth

Mr Robert Jeffery, Principal, Jeffery & Co

Mr Colin Johns OAM, National Councillor, The Pharmacy Guild of Australia

Mr Richard Kneebone, Company Secretary, ICI Australia Ltd

Mr Wayne Lonergan, Partner, Coopers & Lybrand

Mr Ted Rofe, Chair, Australian Shareholders' Association Ltd

Ms Jillian Segal, Special Counsel, Dunhill Madden Butler

Mr Jon Webster, Partner, Arthur Robinson & Hedderwicks

The reason for this report

The Corporations Law imposes a positive disclosure obligation and specific liability for fundraising and takeovers. Concern has been expressed in recent years that section 52 of the *Trade Practices Act 1974* conflicts with this regime. The same issue arises with the provisions of the State and Territory Fair Trading Acts corresponding to section 52.

In June 1995, the Corporations Law Simplification Task Force was asked to report on the application of section 52 of the Trade Practices Act to prospectuses and other aspects of dealings in securities. The Task Force was asked to prepare this report because of the particular relevance of the issue to its work on the fundraising and takeover provisions of the Corporations Law.

Contents

1. Executive summary 2
2. Consultation 4
3. The issue 5
4. Analysis 8
5. Recommendations 18
6. Appendixes

   A — List of submissions 21

   B — Analysis of current and proposed Corporations Law provisions 23

   C — Analysis of Trade Practices Act provisions 31

   D — Overseas regulation of securities dealings 35

1. Executive summary

The Task Force recommends that conduct in relation to fundraising, takeovers and other dealings in securities be governed by the Corporations Law and not by the provisions in Part V of the Trade Practices Act (which include section 52), nor by the equivalent provisions in the Fair Trading Acts of each State and Territory.

The Corporations Law imposes rigorous disclosure obligations for prospectuses and takeover documents, which are designed to ensure that all material information is obtained and disclosed to investors. Furthermore, the Law provides for:

- court injunctions and other remedial orders in relation to prospectuses or takeover documents which are false or misleading or which omit material matter (these remedies are available irrespective of the amount of care exercised in preparing the documents);

- heavy criminal penalties for issuing defective prospectuses or takeover documents (with a defence based on reasonable inquiry); and

- liability to compensate persons who suffer loss as a result of defective prospectuses or takeover documents (subject to reasonable inquiry and due diligence defences).

The Task Force proposals on fundraising and takeovers for the Third Corporate Law Simplification Bill retained this approach, but proposed that the general prohibition in section 995 against misleading or deceptive conduct in relation to dealings in securities be expressly confined to dealings other than those regulated under the specific provisions on prospectuses and takeover documents.

The essential effect of the proposed amendments of the Trade Practices Act would be limited. The existing liability to compensate for loss that arises from misleading or deceptive statements in a prospectus or takeover document which could not have been avoided even by making reasonable inquiries and exercising due diligence would be removed.

The Task Force recommendations are made following extensive consultation with interested parties about the current law and how it should be reformed.

The reasons for the Task Force recommendations are:

- The defences under the Corporations Law, which are based on making reasonable inquiries and ensuring due diligence, achieve a reasonable balance between the interests of investors and the interests of those raising capital.

- Applying the Trade Practices Act, which imposes liability regardless of the amount of care exercised, undermines the operation of these defences and upsets this balance.

- Investing in securities necessarily involves the voluntary assumption of risks which issuers cannot eliminate completely by making exhaustive inquiries.

- Excessive liability for those involved in fundraising and takeovers potentially increases the costs for Australian business of engaging in this conduct.

- If a choice has to be made between the Corporations Law and the Trade Practices Act regimes, the overall level of investor protection under the Corporations Law is preferable to that provided under the Trade Practices Act.

- Duplication between regulators would be avoided by giving the Australian Securities Commission (ASC) sole responsibility for conduct in relation to securities dealings.

- The Corporations Law regime is consistent with international practice.

2. Consultation

In August 1995, the Task Force sought the views of peak consumer, business and professional organisations and relevant regulatory agencies on the interaction between section 52 of the Trade Practices Act and the Corporations Law in relation to fundraising, takeovers and other aspects of dealings in securities.

On the basis of this preliminary consultation, a Task Force proposal was released in November 1995, proposing that conduct in respect of fundraising, takeovers and other dealings in securities be governed by the Corporations Law, and not by section 52 and associated provisions of the Trade Practices Act (and the corresponding provisions of the State and Territory Fair Trading Acts). This proposal, which dealt also with possible reforms to improve the fundraising provisions of the Corporations Law, was circulated widely for public comment.

Submissions on the proposal to deal with the overlap between section 52 and the Corporations Law were received from the organisations and individuals listed at Appendix A. Support for the proposal was expressed by business, securities markets participants, the legal and accounting professions, the ASC and the Australian Stock Exchange. Organisations opposing the proposal were the Australian Competition & Consumer Commission (ACCC), some State and Territory agencies which administer the Fair Trading Acts and the Australian Consumers' Association.

In addition to receiving written submissions, the Task Force discussed the proposal with a number of organisations, including the ACCC and the ASC.

3. *The issue*

The issue examined in this report is whether fundraising, takeovers and other dealings in securities should be regulated under the Trade Practices Act and the State and Territory Fair Trading Acts, as well as by the Corporations Law. (For convenience, references in this report to the Trade Practices Act usually apply also to the Fair Trading Acts.)

How investors are protected

The regimes under the Corporations Law and the Trade Practices Act operate in significantly different ways.

The central focus of the regulatory approach for fundraising under the Corporations Law is to ensure full disclosure of the information people need to make informed investment decisions. To this end, the Corporations Law:

- imposes a positive disclosure obligation in the form of a prospectus containing all the information necessary to make an informed assessment of the assets and liabilities, financial position, profits and losses and the prospects of the entity;
- specifies that the information required is that known to a range of persons who are involved in the preparation of the prospectus and that which they could find by making reasonable inquiries; and
- imposes liability on those persons to compensate investors who suffer loss.

By directly linking the disclosure obligation and liability, the Corporations Law provides a strong incentive for the people involved in preparing a prospectus to disclose all material information. A range of defences is provided in relation to actions for damages, which vary in content depending on the role performed by the persons in preparing the prospectus. The most significant of the defences are based on making reasonable inquiries and exercising due diligence. The people who engage in the conduct necessary to establish the defences are in turn likely to ascertain the matters required to be disclosed and avoid making false or misleading statements.

Regardless of the amount of care taken in preparing prospectuses, in order to prevent investors from being given documents which contain materially false or misleading statements or omit material matters:

- the ASC is able to issue administrative ‘stop orders’ in relation to prospectuses which do not meet the disclosure requirements; and

- the courts are able to grant injunctions to restrain the circulation of non-complying prospectuses.

Disclosure of information is also required as part of the regulation of takeovers and compulsory acquisitions. Again, the regime involves positive disclosure obligations coupled with a liability regime which includes defences in relation to actions for damages.

A more detailed analysis of the relevant Corporations Law provisions on fundraising and takeovers is set out in Appendix B.

Section 52 of the Trade Practices Act prohibits corporations from engaging in misleading or deceptive conduct in trade or commerce. In contrast to the Corporations Law provisions dealing with fundraising and takeovers, section 52 does not impose a duty of disclosure.[1] Further, unlike the Corporations Law liability provisions, a contravention of section 52 can result in liability for damages, in the absence of fault or knowledge and even where due diligence has been exercised.[2]

The existence of this strict liability under the Trade Practices Act is the core of the concern about the conflict with the Corporations Law. As a consequence of this strict liability under the Trade Practices Act, the defences set out in the Corporations Law dealing with liability for damages in relation to fundraising and takeovers do not serve their intended function. People who take reasonable precautions to comply with the disclosure requirements, which give them defences under the Corporations Law, may nonetheless find themselves liable for damages under the Trade Practices Act.

A more detailed analysis of the relevant Trade Practices Act provisions is set out in Appendix C.

The regulatory regimes for fundraising and takeovers in the main comparable overseas jurisdictions consistently impose positive disclosure obligations, provide for liability in damages and give due diligence defences. An analysis of the statutory position in these jurisdictions is set out in Appendix D.

Impact on business

The possibility that section 52 of the Trade Practices Act might apply to fundraising and takeovers matters regulated under the Corporations Law and previous companies and securities legislation, has existed since

---

1 Silence may be misleading and deceptive conduct in limited circumstances. See Appendix C, p 33.

2 *Hornsby Building Information Centre Pty Ltd v Sydney Building Information Centre* (1978) 140 CLR 216, *Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd* (1982) 149 CLR 191 and *Yorke v Lucas* (1985) 158 CLR 661.

section 52 was enacted in 1974. In 1992, the Prospectus Law Reform Subcommittee of the Companies and Securities Advisory Committee reported that this overlap created uncertainty and that this was detrimental to the efficient operation of the capital markets.[3] The Subcommittee report recommended that the Corporations Law rules on prospectuses should prevail over section 52 where there was an overlap.

The decision of the Federal Court of Australia in *Fraser v NRMA Holdings Ltd* [4] has led to renewed calls from the business community and professional advisers for the overlap to be removed. The principal concern is that the defences given by the Law in relation to fundraising and takeover liability are illusory, if the claim is brought under the Trade Practices Act, because defences are not available. In addition, it is unsatisfactory for 2 regulatory agencies to have responsibility for the same conduct. As the NRMA decision was an action for an injunction rather than an action for damages, the removal of the overlap would not affect the outcome in a similar case because there are no defences to an injunction under the Corporations Law, although it would change the source of the applicable law.

Options

The 2 options to resolve the issue are:

- regulate conduct connected with fundraising, takeovers and other dealings in securities under the Corporations Law to the exclusion of Part V (including section 52) of the Trade Practices Act; or

- repeal the specific Corporations Law provisions establishing civil liability regimes for fundraising, takeovers and other dealings in securities and leave conduct in relation to these matters to be regulated under 1 or both of Part V of the Trade Practices Act (including section 52) or section 995 of the Corporations Law (which is in similar terms to section 52).

---

[3] The Companies and Securities Advisory Committee (CASAC), established under the *Australian Securities Commission Act 1989*, advises the responsible Minister on companies, the securities markets and industry and the futures market and industry. The Prospectus Law Reform Subcommittee was appointed by CASAC in July 1991 to review the prospectus provisions of the Corporations Law to identify problems in the Corporations Law system and recommend possible solutions. The Subcommittee reported in March 1992.

[4] (1994) 52 FCR 1, (1995) 55 FCR 452.

4. Analysis

Investor protection

The Corporations Law sets up a comprehensive regime of investor protection measures in connection with fundraising, takeovers and other dealings in securities. These measures provide investors with more complete and relevant protection than that available under section 52 of the Trade Practices Act. The difference between the coverage of the Corporations Law and the Trade Practices Act is illustrated by the following table.

	s 52	**s 995**	**Prospectus** **s 996** **s 1022**	**Takeover** **s 704** **s 705** **s 750**
DISCLOSURE				
All material information			✓	✓
BASIS FOR LIABILITY				
Misleading or deceptive conduct	✓	✓		
False or misleading statements or omissions			✓	✓
REMEDIES				
Damages	✓	✓	✓	✓
Injunctions	✓	✓	✓	✓
Criminal			✓	✓
DEFENCES				
to actions for damages		See Note	✓	✓
to actions for injunctions				
to criminal actions			✓	✓

Note: Where the misleading or deceptive conduct is constituted by a false or misleading statement in or an omission from a prospectus, arguably the defences in Part 7.11 of the Corporations Law will apply.

Full disclosure of information to enable investors to make informed decisions is an important aspect of the Corporations Law regime.

Investors in securities take up interests in a corporate business or a pool of income-producing assets. In so doing, they value those securities by assessing the rate of return they expect to receive against the expected risk of the investment. This valuation process is primarily forward-looking and involves an assessment of the prospects of the corporation. Investment in securities involves the voluntary assumption of the risk inherent in the corporate business, with a view to receiving a return that is higher than the risk-free rate of return.

Similar considerations apply in relation to decisions about whether or not to accept takeover bids. These decisions essentially involve making a judgment about the value of bid securities, compared with the value of the consideration offered (which often will be or include other securities).

The best and often only sources of information about value and prospects are the corporations seeking capital, those making takeover bids and the targets of such bids.

To promote informed markets, the Corporations Law requires comprehensive disclosure of information in prospectuses and takeover documents. Although the terms of the disclosure obligations vary, they are aimed at meeting the reasonable information needs of investors. To avoid problems with stale information, there is a requirement to issue supplementary prospectuses in certain circumstances and to refresh certain takeover documents. These disclosure obligations go well beyond anything required by the common law.[5] The Trade Practices Act does not of itself generally require the disclosure of any information in relation to offers of securities or takeover offers.

A wide range of measures under the Corporations Law deal with situations where the disclosure obligations have not been fully complied with. Although many of these are comparable to those available under the Trade Practices Act, in some significant aspects the Corporations Law regime goes much further in protecting investors.

---

[5] At common law and in equity, non-disclosure of a material fact by a person offering securities for subscription will not generally be actionable unless it turns on a positive statement which has been made into a misrepresentation (*New Brunswick and Canada Railway and Land Company v Muggeridge* (1860) 1 Dr & Sm 363; 63 ER 418, *Central Railway Co of Venezuela v Kish* (1867) LR 2 HL 99, *Henderson v Lacon* (1867) Lr 5 Eq 249, *Peek v Gurney* (1873) LR 6 HL 377, *McKeown v Boudard Peveril Gear Co* (1896) 74 LT 310, *Aaron's Reefs Ltd v Twiss* [1896] AC 273). In limited cases a fiduciary relationship between those offering securities for subscription and those taking them up may give rise to obligations of disclosure (*Erlanger v New Sombrero Phospate Company* (1878) 3 AC 1218, *United Dominions Corporation Ltd v Brian Pty Ltd* (1985) 157 CLR 1, *Hill v Rose* (1990) VR 129).

The Corporations Law requires prospectuses and major documents associated with takeover bids to be lodged with the ASC before they are issued to potential investors or to the shareholders of the target company. Although the ASC does not engage in detailed pre-vetting, its examination often results in non-complying documents being identified and rectified before investors are exposed to any risks. The Trade Practices Act regime does not require the regulatory agency to become involved before conduct occurs which may expose investors to risk.

The ASC has an administrative power to issue 'stop orders' against prospectuses which do not comply with the Law. The effect of such an order is to prohibit the further issue of securities on the basis of the prospectus. The 'stop order' power enables the ASC to act quickly to prevent loss to investors from prospectuses which do not comply with the Law. There is no equivalent power in the Trade Practices Act. If the ACCC wished to intervene, it would have to seek an injunction through the courts to restrain any breaches of section 52.

Under the Corporations Law, issuing a prospectus that omits material information or which contains a material statement that is false or misleading is a serious offence carrying a penalty of a $20,000 fine or 5 years imprisonment or both.[6] There are criminal sanctions for issuing defective statements in connection with takeover bids.[7] In contrast, a breach of section 52 of the Trade Practices Act gives rise only to civil remedies. Criminal sanctions are available in relation to some of the more specific provisions in Part V, but the application of these to dealings in securities is more limited.

The Corporations Law also includes stringent civil liability regimes in connection with prospectuses and takeover documents that do not comply with the Law. These regimes serve the dual function of encouraging persons who prepare disclosure documents to do so in a proper manner and providing for compensation for investors in appropriate circumstances. Provisions in the Trade Practices Act enable persons who suffer loss as a consequence of misleading or deceptive conduct to recover that loss from the offender. However, the Corporations Law and Trade Practices Act civil liability regimes differ in 3 significant respects.

- Investors will often have an easier burden of proof to discharge in proceedings under the Corporations Law than under the Trade Practices Act. In order to establish liability for damages under the Trade Practices Act, the plaintiff must show either that the defendant engaged in misleading or deceptive conduct or was involved in that conduct. Proving the latter is particularly

---

[6] Corporations Law, s 996 and Sch 3. For a body corporate, the fine could be up to $100,000 (s 1312).

[7] Corporations Law, ss 704, 705 and 1312 and Sch 3.

problematic.[8] The prospectus liability provisions in the Corporations Law overcome the problems of proof by treating various classes of persons associated with the preparation of prospectuses as being involved in any contravention. Substantially the same result is achieved under the Law in connection with takeover documents, although the range of persons with 'automatic' liability is smaller.

- The Corporations Law provides most persons who are potentially liable in relation to prospectuses and takeover documents with defences. Although the form of the defences varies depending on the category of person in question, their main thrust is based on having exercised due care. In the prospectus context, this means that the person must have made reasonable inquiries or exercised due diligence. The level of inquiry and verification required by the Law is high, particularly in relation to central participants.[9] No defences are available in relation to actions for damages under the Trade Practices Act.

- Investors have twice as long to commence an action under the Corporations Law. The limitation period under the Law is 6 years, but only 3 under the Trade Practices Act.[10]

The availability of defences under the Corporations Law and the absence of defences under the Trade Practices Act is central to the issue of how the overlap between them should be resolved. Removing the application of section 52 from dealings in securities necessarily has the effect of removing potential liability in damages which currently exists. Arguably, this amounts to a diminution of investor protection.

However, the impact of removal of the application of the Trade Practices Act on the overall level of investor protection would be slight. Damages against the corporation will usually not be an appropriate remedy for investors in shares who suffer loss or damage as a result of investing on the basis of a false or misleading prospectus or a prospectus which omits

---

[8] Under section 75B of the Trade Practices Act, a person is involved in a contravention if they have aided, abetted, counselled or procured the contravention; induced, whether by threats or promises or otherwise, the contravention; have been in any way, directly or indirectly, knowingly concerned in, or party to, the contravention; or have conspired with others to effect the contravention. These elements are derived from the criminal law. A person must act with the intention to bring the conduct about based on knowledge of the essential facts constituting the contravention: *Yorke v Lucas* (1985) 158 CLR 661.

[9] *JP Coats v Crossland* (1904) 20 TLR 800, *Shepheard v Broome* (1904) AC 342, *Adams v Thrift* (1915) 1 Ch 557, *Escott v BarChris Construction Corporation* 283 F Supp 643 (SDNY) 1968, and *Feit v Leasco Data Processing Equipment Corporation* 332 F Supp 544 (EDNY) 1971.

[10] In 1994, the Australian Law Reform Commission recommended in Report No 68 *Compliance with the Trade Practices Act 1974* that s 82(2) of the Trade Practices Act be amended to allow the court to extend the period in which a claim for damage can be commenced if the court considers it appropriate to do so.

material information. This is because an award of damages against the corporation necessarily causes detriment to the corporation and in turn reduces the value of the investor's shares. It is generally not regarded as economic for corporations to attempt to insure against prospectus related suits by their shareholders.

In any event, investors will still be able to seek remedies at common law which could not be defeated by the Corporations Law defences. The most significant of these is the contractual remedy of rescission which is available where there has been a material misrepresentation leading to the formation of the contract. Rescission of the contract enables the investor to be restored to their initial position by returning the shares and obtaining a refund of their original investment.[11]

In addition, the court could make orders under subsection 1325(5) of the Corporations Law which are in the nature of rescission. As with the rescission remedy, the availability of a defence to an action for damages would not be a barrier to making the order. However, remedies under subsection 1325(5) are discretionary (as is rescission) and the court may therefore have regard to the conduct of the defendant in deciding whether to make an order.

There are relatively few instances where a different result would be achieved in an action under the Corporations Law compared to one under the Trade Practices Act. This would only happen in a damages action where loss has been suffered as a result of misleading or deceptive conduct of a kind which could not be discovered by making reasonable inquiries or at all. In that case an action would succeed under section 52 but not under the Corporations Law.

This different result would also depend on the aggrieved investor having established in those circumstances that:

- the corporation or other defendant engaged in misleading or deceptive conduct or was involved in that conduct; and

- the investor relied on that conduct resulting in loss.

Removal of the application of the Trade Practices Act from dealings in securities would have no effect on the capacity of investors and regulatory agencies to seek injunctions in relation to prospectuses and takeovers. These will continue to be available irrespective of whether the conduct necessary to establish a defence to an action for damages has been carried out.

---

[11] Rescission is a discretionary remedy which will ordinarily only be given where it is possible to restore the parties to their original position. It may not be available if the securities have been transferred to a third party.

Most importantly, the level of investor protection applicable in relation to dealings in securities other than prospectuses and takeovers will remain unchanged. All the remedies which may be available in an action under section 52 of the Trade Practices Act will be available in an action for a breach of section 995.[12] The Task Force has proposed in the context of the Third Corporate Law Simplification Bill that the existing uncertainty about whether defences are available in relation to actions for damages should be removed by making it clear that there are no defences available for a breach of section 995. As at present, no defences would be available in relation to actions for injunctions.

Economic efficiency

The market for securities in Australia is obviously important to the Australian economy. Active and fully informed markets in securities are essential to attract and allocate capital for productive investment. Productive corporate activity essentially involves taking risks for gain. Similarly, the maintenance of an efficient market for corporate control is in Australia's long term economic interest. Proper disclosure is necessary to facilitate decisions about the re-allocation of productive resources.

Imposing liability for damages, irrespective of the degree of care which has been exercised, is out of line with international regulatory practice. That practice consistently involves imposing positive disclosure obligations, coupled with liability for damages for breaches and defences based on the exercise of due care. Strict liability has probably raised the cost of fundraising for Australian businesses by inducing fundraisers to take precautions beyond what is reasonable.

The justification for a strict liability regime is that, by imposing the cost of damage on the person who bears the least cost of preventing or minimising that loss, the possibility of damage is minimised at the least cost to society. Whatever the merits of this approach in relation to other aspects of human behaviour, the analysis is not compelling in relation to prospectuses and takeover documents.

The Corporations Law imposes positive disclosure obligations based upon reasonable inquiries and care, backed by criminal, civil and administrative penalties. Only in limited circumstances will a different result occur depending on whether the action is brought under section 52 of the Trade Practices Act or the Corporations Law. A difference will only arise in relation to an action for damages for a misleading or deceptive document if the defect could not have been discovered by taking the reasonable steps necessary to make out the Corporations Law defences. It follows that liability for damages under the Trade Practices Act will only be broader where the steps to avoid the loss were unreasonable or impossible.

---

[12] Sections 1324 and 1325 of the Corporations Law, which deal with court remedies for breaches of the fundraising provisions, mirror ss 80 and 87 of the Trade Practices Act.

Even in the very limited circumstances where a different result will depend on whether an action is taken under the Corporations Law or the Trade Practices Act, a strict liability provision will not necessarily have the effect of shifting any loss from the investor to the corporation. An investor who successfully sues a corporation of which they are a member in relation to loss suffered from a deficient prospectus or target statement will in turn suffer loss from the reduction in the value of the corporation. While different groups of investors may ultimately bear different proportions of the loss, the asset backing of the shares necessarily falls as a result of an award of damages against the corporation.

The risks inherent in investing in a productive enterprise include the risk that information exists which is material to an investment decision, but which no degree of care or inquiry can uncover. Investment by its nature involves the voluntary assumption of these risks for reward. Because the risk cannot be excluded, the imposition of strict liability will do nothing to reduce it.

It will only be in limited circumstances, if at all, that misleading disclosure could have been avoided by the exercise of care and making inquiries beyond that which is reasonable. Any efficiency gain in the resource allocation process arising from imposing strict liability in these circumstances must be weighed against the detriment arising from the increased transaction costs flowing from it. In the case of an investment in a corporation issuing securities under a prospectus or takeover document, those additional costs inevitably flow to investors in the corporation, irrespective of whether they lead to any benefit in the form of better disclosure. In the context of risk-taking activity, investors may readily assume that risk rather than incur the costs of efforts to remove it. Imposition of strict liability would prevent this. Although the additional costs imposed by strict liability under the Trade Practices Act are not easily quantifiable, it is not apparent what practical economic purpose is achieved by, in effect, requiring business to take steps beyond what are reasonable to ensure proper disclosure.

Imposition of strict liability may, in the absence of the strict disclosure obligations under the Corporations Law, also lead to documents which are less useful to investors. The documents may omit relevant information rather than risk strict liability for making statements which are misleading. Thorough due diligence processes, with a healthy tension between the expanded range of parties with potential liability (which apply under the Corporations Law) may not be adopted because liability under the Trade Practices Act may arise despite the most exhaustive processes. Advisers may distance themselves from the preparation process in order to minimise the possibility of incurring liability.

Strict liability may also discourage the entry of new enterprises into the securities markets. Those who are likely to be discouraged will tend to be those involved in riskier ventures. These are potentially the most rewarding ventures.

Unintended consequences

Although it was recognised that the Trade Practices Act may apply to dealings in securities, it seems clear that the overlap between the 2 regimes has had unintended consequences.

The retention of the overlap may itself be a source of inefficiency. It potentially requires those involved in capital raising and other dealings in securities to deal with more than 1 regulatory agency in respect of substantially the same conduct. At its worst, different regulators may adopt different stances on the same issue, leaving market participants to satisfy the requirements for both. Potential inefficiencies exist for Government as resources may need to be duplicated. Even with a fully co-ordinated approach between the 2 regulatory agencies, the overlap is a possible source of confusion. This confusion could be exacerbated by the involvement of the various State and Territory agencies which administer the Fair Trading Acts.

Floodgates

Because section 52 is a provision of general application, it has been argued that the Task Force proposal would result in the 'opening of floodgates' for other exclusions from section 52.

This argument does not go directly to the merits of the proposal in relation to the Corporations Law. The Task Force has not considered whether carve outs from the Trade Practices Act are appropriate in other areas as this is beyond the scope of its brief. However, it notes that defamation matters are already effectively carved out by section 65A of that Act.

The case for different treatment in relation to the Corporations Law is based on the special features of the Corporations Law regime for fundraising and takeovers. The regulatory regime involves positive disclosure obligations in relation to matters which are inherently uncertain. Although positive disclosure regimes are provided for certain specific industries, those regimes deal with disclosure to arm's length parties. On the whole, the disclosures required under these other regimes are of a different character to that required under the Corporations Law. In particular, these other regimes generally do not focus on dealing with forward-looking matters which involve as many complexities as the prospects of a trading enterprise. Nor do these other regimes generally require inquiries to be made. This results in some of the information disclosed being second-hand. Irrespective of whether it is appropriate to overlay these other regimes with section 52, the overlap is not appropriate in relation to fundraising and takeovers.

Alternative means of removing the conflict

It would not be logical to retain the present operation of section 52 and have defences in the Corporations Law in relation to fundraising and

takeovers. One way of removing this overlap would be to remove the specific Corporations Law defences applicable to liability for fundraising and takeovers, leaving the liability to be regulated under 1 or both of the Trade Practices Act and the equivalent prohibition in section 995 of the Corporations Law.

This would involve accepting that due diligence defences should not be available in relation to liability connected with regulated offers and purchases of securities. Other consequences of this would be:

- Liability under the Trade Practices Act would only apply to 'corporations' (as defined in the Act) and persons knowingly involved in a contravention by that corporation. Liability imposed under section 1006 of the Corporations Law by virtue of a person's status or connection to the offer, would be lost, thereby:

  (i) narrowing the range of persons who are engaged in the due diligence process;

  (ii) leaving a more limited number of persons against whom proceedings may be brought; and

  (iii) making cases against those involved harder to prove under the Trade Practices Act than under section 1006.

- The ASC would administer the disclosure obligations under the Corporations Law, register prospectuses and stop issues under deficient prospectuses. However, it would need to refer actions for injunctions, damages or other court remedies to the ACCC or the various agencies which administer the State and Territory Fair Trading Acts. An arrangement of this kind would be inefficient, requiring the various regulatory agencies to duplicate expertise. Furthermore, persons involved in securities markets transactions would be required to deal with more than 1 regulatory agency, potentially giving rise to confusion, even if a high degree of coordination and cooperation existed between the regulatory agencies. A regulatory approach of this kind, with the specialist agency not having effective enforcement powers, is undesirable in principle and inconsistent with international practice.

If this were done, it would be consistent to remove the disclosure provisions in the Corporations Law for fundraising and takeovers. This would avoid the inappropriate combination of mandatory disclosure and strict liability provisions. However, it is difficult to justify removal of these disclosure obligations in circumstances where market efficiency depends on the availability of accurate information. It would also involve the removal of other specific investor protection measures which go beyond section 52. Furthermore, such an approach would be out of line with international practice.

Implementation of Task Force recommendations

As the State and Territory Fair Trading legislation contains provisions corresponding to Division 1 of Part V of the Trade Practices Act, the overlap also needs to be removed from this legislation. If it is to be effective, the overlap in relation to the Trade Practices Act and the Fair Trading Acts should be removed at the same time. It would be desirable to introduce these changes along with the changes to the takeover and prospectus liability provisions in the Third Corporate Law Simplification Bill.

Given that the regulation of securities markets is ultimately the responsibility of the Federal Government, it would be appropriate for the Corporations Law provisions applicable to dealings in securities to be amended so that they exclude liability under the State and Territory Fair Trading legislation. This would, in effect, involve a partial reversal of subsection 1005(3) of the Corporations Law which preserves liability under other laws.

5. *Recommendations*

The Corporations Law Simplification Task Force recommends that:

(a) the *Trade Practices Act 1974* be amended so that Division 1 of Part V (including section 52) does not apply to conduct in relation to fundraising, takeovers and other dealings in securities to which the Corporations Law applies;

(b) the Corporations Law be amended so that it applies to fundraising, takeovers and other dealings in securities to the exclusion of provisions in the State and Territory Fair Trading Acts corresponding to Part V of the Trade Practices Act; and

(c) the necessary amendments of the Trade Practices Act and the Corporations Law be included in the Third Corporate Law Simplification Bill.

6. Appendixes

A. List of submissions

B. Analysis of current and proposed Corporations Law provisions

C. Analysis of Trade Practices Act provisions

D. Overseas regulation of securities dealings

Appendix A — List of submissions

ACT Consumer Affairs Bureau

AMP Society

Australian Accounting Research Foundation

Australian Bankers' Association

Australian Competition & Consumer Commission

Australian Consumers' Association

Australian Finance Conference

Australian Institute of Company Directors

Australian Securities Commission

Australian Stock Exchange Limited

Bain & Company

Commercial Law Association

Commissioner for Consumer Affairs, Queensland

Companies and Securities Advisory Committee and its Legal Committee

Department of Fair Trading, NSW Consumer Protection Agency

Greg Golding, Malleson Stephen Jaques

Tony Greenwood, Blake Dawson Waldron

Group of 100 Inc.

International Banks and Securities Association of Australia

Investment Funds Association of Australia Limited

Law Council of Australia, Corporations Committee and Trade Practices Committee

Law Institute of Victoria (Commercial Law Section)

Law Society of New South Wales

Ministry of Fair Trading (Western Australia)

National Mutual Holdings

Brian Salter, Clayton Utz

Securities Institute of Australia

Telstra Corporation Ltd

Trustee Corporations Association of Australia

Victorian Employers' Chamber of Commerce and Industry

Appendix B — Analysis of current and proposed Corporations Law provisions

Fundraising

Generally, the Corporations Law regulates offers of securities for subscription by requiring a prospectus for the offer. Section 1022 of the Law requires that the prospectus contain information which investors and their professional advisers would reasonably require, and reasonably expect to find in the prospectus, to make an informed assessment of:

(a) the assets and liabilities, financial position, profits and losses, and prospects of the corporation; and

(b) the rights attaching to the securities.

The information required is that which any person liable for the content of the prospectus knows or ought reasonably to have obtained by making inquiries.

A different regime applies to offers of securities which have been quoted on the Australian Stock Exchange for 12 months (section 1022AA), in recognition of the existence of a market price based on continuous disclosure of information and market scrutiny.[13]

Section 996 of the Law prohibits the issue of a prospectus which contains a material statement that is false or misleading, or which omits material information. A breach of section 996 is an offence.[14]

Under section 1005 a person who suffers loss or damage because of the conduct of another person which is in contravention of certain provisions, including section 996, may recover the amount of that loss or damage from that person. Where an action is brought under section 1005 in relation to a prospectus which contains a material statement that is false or misleading or which omits material information, section 1006 extends liability to:

(a) the corporation;

(b) a director or proposed director of the corporation;

(c) a promoter of the corporation;

---

[13] Essentially this involves the disclosure of transaction specific information, but not other information about the entity itself.

[14] The defendant may establish a defence to prosecution by showing:

(a) that they had reasonable grounds to believe the statement was not misleading or that the omission was not material, in each case after reasonable inquiries; or

(b) that an omission was inadvertent (s 996(2)).

(d) an expert who consents to the inclusion of their statement in the prospectus;

(e) a stockbroker or underwriter of the issue named with their consent;

(f) an auditor, banker or solicitor of the corporation or in relation to the issue named with their consent; and

(g) a person named with consent as having performed a professional, advisory or other function for the corporation or in relation to the issue.

Sections 1007 to 1011 describe the extent of liability of these persons, and provide a range of defences which relate to withdrawal of involvement, making reasonable inquiries or exercising due diligence.

Subsection 1011(1) provides the corporation, an issuer of the prospectus, a stockbroker, an underwriter, and a promoter with a defence, where they show that the false or misleading statement or omission:

(a) was due to a reasonable mistake; or

(b) was due to reasonable reliance on information supplied by another person (other than their director, servant or agent); or

(c) was due to the act or default of another person (other than their director, servant or agent), and they took reasonable precautions and exercised due diligence to ensure that all statements to be included in the prospectus were true and not misleading and that there were no material omissions.[15]

Further due care defences are available for directors, proposed directors and experts where they show that, after making such inquiries (if any) as were reasonable, they had reasonable grounds to believe that the statement was true and not misleading, or that there were no material omissions from the statement (subsections 1008A(4) and 1009(3)).[16]

A breach of section 996 may also lead to injunctive or other relief under sections 1324 and 1325 of the Law (similar to sections 80 and 87 of the Trade Practices Act). No defences are available in relation to actions for injunctions under these provisions, although the fact that a person has exercised due care may be relevant to the exercise of the court's discretion whether to grant an injunction.

---

[15] These defences are based on s 85 of the Trade Practices Act. The defences in s 85 apply to criminal prosecutions but not to civil actions.

[16] These defences were taken from the former Companies Codes, and are similar to those in the *Directors' Liability Act 1890* (UK).

This regime does not exclude liability under any other law (subsection 1005(3)). Accordingly, the legislation expressly envisages that other liability regimes may apply to prospectuses. The possibilities include actions at common law in contract or tort (especially negligent misstatement), as well as liability under the Trade Practices Act and State and Territory Fair Trading Acts.

Takeovers

The takeover provisions in Chapter 6 of the Corporations Law involve a regime of disclosure obligations, civil liability for non-compliance and defences based on taking due care in preparing documents.

A person making offers under an off-market takeover bid must prepare a Part A statement and an offer document. The Part A statement must comply with the specific disclosure requirements in Part A of section 750 of the Law, many of which involve inquiries of others. If the consideration for the offer is securities, the Part A statement must contain the matters which would be required by section 1022 or 1022AA to be contained in a prospectus in relation to those securities.

Part A statements must also contain all other information known to the bidder, which is material to a shareholder's decision whether or not to accept an offer and which has not previously been disclosed to the shareholders. The offer document must set out the terms of the offer and, in effect, update information about the bidder's holding of shares in the target company.

Where an offer under an off-market bid is varied, a notice of variation must be sent to each person to whom an offer was made. The notice of variation must set out the terms of the variation and particulars of modifications of the Part A statement made necessary by the variation (section 657). These particulars may involve significant additional disclosure.

The target is required to send a Part B statement to each shareholder to whom an offer was made. The Part B statement is subject to specific disclosure requirements and a general test (Part B of section 750). Where the bidder is entitled to at least 30% of a class of voting shares in the target, or the bidder and target have common directors, the Part B statement must be accompanied by an expert's report as to whether the takeover bid is fair and reasonable (section 648).

A person making an on-market bid must prepare a Part C statement which is subject to similar disclosure requirements for a Part A statement involving cash consideration. No offer document is required for an on-market bid. The target of an on-market bid is required to send a Part D statement to the Australian Stock Exchange. The content of a Part D statement is similar to a Part B statement.

A successful bidder has a right in some circumstances to compulsorily acquire the outstanding shares (subsection 701(2)). A bidder who has the right to compulsorily acquire shares, but chooses not to, must give dissenting offerees an opportunity to dispose of their holding (subsections 703(1)-(3)). The holders have a right to sell those securities to the bidder on terms which are agreed or which are determined by the courts (subsection 703(8)). A notice to holders of non-voting shares, renounceable options or convertible notes under subsection 703(4) must not propose terms unless it is accompanied by an expert's report as to whether the proposed terms are fair and reasonable (subsections 703(5)-(7)).

Where the various takeover documents contain matter which is false in a material particular or materially misleading, or omit material information, liability for prosecution or to compensate a person who suffers loss or damage on the faith of the misstatement, is imposed under section 704. In general, directors of the entity issuing the document and any experts are liable for the damages.[17] Defences are available where the defendants can show that they believed on reasonable grounds at all relevant times that there was no misstatement or material omission (subsections 704(6) and (8)).

Securities dealings

In addition to the specific provisions dealing with liability for the contents of prospectuses and takeover documents, section 995 of the Corporations Law provides that a person must not engage in conduct which is misleading or deceptive or likely to mislead or deceive in connection with any dealing in securities, prospectus or takeover bid. As with a breach of section 52, a contravention of section 995 is not an offence, but may give rise to civil sanctions including damages and injunctions.

Section 995 came into effect with the Corporations Law on 1 January 1991. According to the Explanatory Memorandum:[18]

> The provision is considered to be important in maintaining the integrity in the securities market. While supporting deregulatory moves in general, the Government is concerned that investors be protected from unscrupulous activities in the securities market. This clause emphasises that persons, in their dealings in the securities industry, should not engage in misleading or deceptive conduct (cl.762 gives a guide to what constitutes the relevant conduct).

---

[17] Directors who vote against the Part B statement or who are not present for the vote are not liable for its content (s 704(4)(b)).

[18] *Corporations Bill 1988 Explanatory Memorandum* Vol 3 pp 723 — 724.

> A guide to what type of conduct is misleading or deceptive can be gained from the many cases decided under TPA s.52. The Courts have tended to give a broad meaning to the terms. It can also be noted that TPA s.52 may itself apply in some cases of securities dealing. In order to stress the undesirability of the conduct in question it was considered important to include a similar provision to s.52 in the Bill. Persons who engage in misleading and deceptive conduct thus run, at the least, the risk of civil liability.

With the benefit of experience, it is not clear that the overlapping application of section 995 is necessary or desirable.[19]

It is unclear whether defences are available in relation to actions for damages for a contravention of section 995, where the misleading or deceptive conduct is constituted by a false or misleading statement in or an omission from a prospectus. In such cases it is arguable that the defences in Part 7.11 Division 4 are available. This view is at its strongest in connection with prospectuses required by the Corporations Law to be lodged with the ASC.

It is unclear whether defences are available for actions for damages for defective takeover documents if the action is pursued under section 995, rather than under the specific liability provisions in section 704. If the interpretation that no defences are available is correct, the enactment of section 995 of itself renders the specific regime in section 704 redundant. Much of the recent litigation in relation to takeover documents has been brought under section 995, either instead of or as well as for breaches of the specific takeover provisions. None of those cases involved an action for damages.[20]

The Task Force's fundraising and takeovers proposals

In the context of the Third Corporate Law Simplification Bill, the Task Force has proposed a number of amendments to the regimes for disclosure and liability in relation to fundraising and takeovers to improve their operation. These proposals would bring the approach for takeovers into line in certain respects with that applying to the fundraising provisions.

It is proposed to retain the general disclosure test for prospectuses in section 1022, subject to minor amendments. The Task Force has proposed that the check list approach to disclosure in relation to takeover documents

---

[19] See generally analysis at p 15.

[20] *Re BNQ Sugar Pty Ltd* (1994) 12 ACSR 695, *Pancontinental Mining Ltd v Goldfields Ltd* (1995) 16 ACSR 463; *Solomon Pacific Resources NL v Acacia Resources Ltd* (1996) 19 ACSR 238; 14 ACLC 505; 19 ACSR 677; 14 ACLC 637, *Ampolex Ltd v Mobil Exploration & Producing Australia Pty Ltd* (1996) 19 ACSR 354; 19 ACSR 394; 14 ACLC 743.

be replaced with a general disclosure test designed to elicit all the information necessary to make an informed decision about whether or not to accept a bid.

The requirement to issue a supplementary or replacement prospectus would continue where a material adverse change occurs or where matters which should have been included in the prospectus are uncovered subsequent to its issue. Consideration is being given to an express obligation to supplement disclosures already made in connection with a takeover bid.

The Task Force has proposed some rationalisation of the existing civil liability and defence provisions in relation to fundraising and takeovers. A person who suffers loss as a result of a misleading or deceptive statement in a prospectus or an omission from the prospectus will be able to recover that loss from those involved in its preparation.

The body issuing the securities, its directors, promoters, underwriters and stockbrokers to the issue would continue to be liable in relation to the whole of the prospectus. Experts and other persons performing professional or advisory functions would be liable only for statements and omissions that relate to the performance of those functions.

The existing defences would be rationalised by replacing the current medley of defences, which differ in form and which are drawn from different sources, with a single set of defences applicable to all those who are potentially liable. It is proposed that defences be available where:

(a) after taking reasonable precautions and exercising due diligence, the person believed that a statement was true and not misleading, and that there was no material omission from the prospectus;

(b) the person placed reasonable reliance on a statement or a report supplied by another person; or

(c) the person withdrew their consent to being named in the prospectus.

A similar approach to defences and liability is proposed in relation to takeover documents. This would involve some tightening of the provisions when compared with the regime in existing section 704. In particular, direct liability to shareholders would be extended to experts and other professional advisers involved in the preparation of the documents. The defences proposed in relation to prospectus liability would also be available in relation to takeovers.

Court injunctions and other remedies would also be available in relation to the issue of a prospectus or a takeover document which is misleading or deceptive or which omits required matters. As at present, no defences would be available if an injunction is sought. As a result, while defences would be appropriate in relation to actions for damages, if a document is

actually misleading or deceptive or omits required information, a court should be able to restrain its circulation, irrespective of whether due care was taken in relation to its preparation. Mechanisms would continue to be available for documents to be corrected.

The Task Force also proposed a new interface between the specific prospectus and takeover liability provisions and the general misleading and deceptive conduct prohibition in section 995. This involves the specific regimes based around sections 996 and 704 applying in relation to the content of prospectuses and takeover statements to the exclusion of section 995. As a consequence, the operation of section 995 would not undermine the specific prospectus or takeover liability provisions.

Section 995 would continue to apply in relation to any dealing in securities not covered by these specific regimes. In such cases, no defences would be available in relation to an action for damages as a result of a contravention. Thus, where no specific disclosure and liability regime is provided in relation to dealings in securities, the extent of liability under section 995 would be the same as that in relation to an action under section 52 of the Trade Practices Act. Similarly, injunctive relief would continue to be available in relation to contraventions of section 995 without any defences being available.

Appendix C — Analysis of Trade Practices Act provisions

The Trade Practices Act has 2 main purposes: to strengthen the regulation of restrictive trade practices and monopolisation, and to protect consumers from unfair commercial practices. State and Territory laws, as well as the common law, operate concurrently with the Act.[21] Following encouragement from consumer bodies, the States and Territories passed Fair Trading legislation between 1985 and 1992 with provisions corresponding with the consumer parts of the Trade Practices Act. Earlier State and Territory legislation had dealt with particular areas of business activity on an ad hoc basis.

Subsection 52(1) of the Trade Practices Act provides that 'a corporation shall not, in trade or commerce, engage in conduct that is misleading or deceptive or is likely to mislead or deceive'. The Fair Trading legislation of each of the States and Territories contains a similar prohibition which is applicable to persons.[22] The test of what is misleading or deceptive is objective, and liability can exist even where a person acts honestly and with reasonable care.[23]

A contravention of section 52 is not an offence, but gives rise to a number of civil sanctions. Under section 80 of the Trade Practices Act, a statutory injunction lies against conduct in breach. Section 82 provides for the recovery of loss or damage caused by the conduct, while section 87 gives the court wide discretionary powers to make other orders.

These orders may be sought against the person who contravened section 52 (necessarily a person within the extended meaning of 'corporation' in the Trade Practices Act) or a person who was involved in that contravention (under section 75B this includes persons who aid or abet a contravention or are knowingly concerned in a contravention).[24] Damages are assessed in the same manner as for damages in tort for breach of a statutory duty. Actions for contravening the equivalent provisions in the State or Territory Fair Trading legislation may be brought against a natural person.

---

[21] Subsection 75(1) provides that Part V is not intended to exclude or limit the concurrent operation of any law of a State or Territory. Part V was held to evince an intention not to cover the field and thus exclude the operation of the State Fair Trading Acts (*Re Credit Tribunal (SA) Ex parte GMAC* (1977) 137 CLR 545).

[22] *Fair Trading Act 1992* (ACT) s 12, *Fair Trading Act 1987* (NSW) s 42, *Consumer Affairs and Fair Trading Act 1990* (NT) s 42, *Fair Trading Act 1989* (Qld) s 38, *Fair Trading Act 1987* (SA) s 56, *Fair Trading Act 1990* (Tas) s 14, *Fair Trading Act 1985* (Vic) s 11, *Fair Trading Act 1987* (WA) s 10.

[23] See *Hornsby Building Information Centre Pty Ltd v Sydney Building Information Centre* (1978) 140 CLR 216, *Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd* (1982) 149 CLR 191 and *Yorke v Lucas* (1985) 158 CLR 661.

[24] In *Yorke v Lucas* (1985) 158 CLR 661, the High Court held that to be involved in a contravention, a person must act with the intention to bring the conduct about based on knowledge of the essential matters which make up the contravention.

Although section 85 of the Trade Practices Act provides a defence in relation to prosecutions for offences under Part V, no defences exist in relation to actions for damages flowing from a breach of section 52. Nor are defences available in relation to actions for injunctions.

In *Fraser v NRMA*[25] the Full Court of the Federal Court of Australia upheld an injunction issued in relation to a document which was in part a prospectus based upon breach of section 52. Section 52 has also been held to apply to conduct connected with a takeover bid. In a case before a single judge of the Federal Court of Australia, the target of a takeover successfully argued for the grant of an injunction against the offeror for a contravention of section 52.[26] Other provisions of Part V of the Trade Practices Act may also apply to prospectuses and takeover documents.

There is no basis for suggesting that the defences in Part 7.11 Division 4 of the Corporations Law are available in an action under section 52 of the Trade Practices Act. This is incongruous if they are available under section 995. Although the court in *Fraser v NRMA* stated that an unfavourable interpretation of section 995 could not be avoided by reliance on section 52,[27] it is not clear whether the action would have failed if it had been for damages rather than for an injunction.

Although some decisions have suggested that, in some instances, section 52 should not be seen as displacing established legal regimes, there has been no judicial decision on whether section 52 is impliedly excluded by the prospectus provisions or by section 995.[28]

---

[25] (1995) 55 FCR 452.

[26] *Australian National Industries Ltd v Consolidated Press Securities Ltd* (6/6/1989, Beaumont J (unrep)). Arguments alleging contraventions of section 52 in takeover documents were considered but failed on the facts in *Industrial Equity Ltd v North Broken Hill Holdings Ltd* (1986) 9 FCR 385 and *Bell Resources Ltd v The Broken Hill Proprietary Company Ltd* (1986) ATPR 47, 658. In *Concrete Constructions (NSW) Pty Ltd v Nelson* (1990) 169 CLR 594, a majority of the High Court took a restrictive view of the words 'in trade and commerce' (in section 52) holding that the phrase 'refer[s] only to conduct which is itself an aspect or element of activities or transactions which, of their nature bear a trading or commercial character' (at 603). IA Renard and JG Santamaria in their work *Takeovers and Reconstructions in Australia*, Butterworths 1990 (p 9076) suggest that, although communications between offeror and the target or target shareholders would be viewed as bearing a 'commercial character', notices sent by target directors to their own shareholders would probably not be so characterised.

[27] *Fraser v NRMA Holdings Ltd* (1995) 55 FCR 452, at 464 per Black CJ, von Doussa and Cooper JJ.

[28] *Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd* (1982) 149 CLR 191, at 225 per Brennan J, *Concrete Constructions (NSW) Pty Ltd v Nelson* (1990) 169 CLR 594 at 603-604 per Mason CJ, Deane, Dawson and Gaudron JJ, *Webb Distributors (Aust) Pty Ltd v State of Victoria* (1993) 179 CLR 15, at 37 per Mason CJ, Deane, Dawson and Toohey JJ. See also Gillooly, M. 'Limiting Section 52 of the Trade Practices Act: The Side-Wind Argument' (1994) 24 *Western Australian Law Review* 278.

While section 52 has a wide ranging reach, it does not contain positive disclosure obligations. A failure to disclose a matter will normally only be misleading or deceptive if there is a relevant requirement for the matter to be disclosed or an expectation that it will be disclosed.[29]

[29] *Rhone Poulenc Agrochimie SA v UIM Chemical Services Pty Ltd* (1986) 12 FCR 477, *Demagogue v Ramensky* (1992) 39 FCR 31, *Warner v Elders Rural Finance Ltd* (1993) 41 FCR 399, *Beach Petroleum NL v Johnson* (1993) 43 FCR 1, *Fraser v NRMA Holdings Ltd* (1994) 52 FCR 1, (1995) 55 FCR 452.

Appendix D — Overseas regulation of securities dealings

The regulatory regimes applicable to fundraising in comparable overseas countries generally include:

(a) obligations to issue a prospectus complying with rigorous content rules;

(b) persons involved in the preparation of the prospectus being liable to compensate persons suffering loss as a result of investing on the basis of prospectuses which contain materially false or misleading statements or which omit material matters; and

(c) those persons having 'due care' defences against that liability.

This regulatory pattern is long established, having its origins in nineteenth century English companies legislation.

A similar regulatory pattern operates in relation to takeovers, although few countries have regimes which are directly comparable to that in Australia.

A survey of the history and content of the legislation in comparable overseas countries on fundraising and takeovers is set out below.

United Kingdom

The regulation of fundraising in the United Kingdom has a lengthy history. In the *Companies Act 1867*, section 38 treated a failure to disclose a material contract in a prospectus as fraudulent, but did not impose any other liability. Common law actions for damages such as the tort of deceit, were available for untrue statements upon which a plaintiff had acted to their detriment.

The House of Lords held in *Derry v Peek*[30] that fraud needed to be shown for a common law action in deceit. This decision meant that there was no legal obligation to take reasonable care to check that statements made in a prospectus were true, and led to the enactment of the *Directors' Liability Act 1890*. The Act imposed liability for misleading statements in the prospectus where a person was induced to subscribe by those statements. The plaintiff did not have to prove that the statement was fraudulent or negligent. Liability did not arise if the person had 'reasonable grounds' for believing the statement to be true.

Stringent liability for misleading prospectuses remained an important statutory safeguard ensuring adequate disclosure of information in dealings

[30] (1889) 14 AC 337.

in securities. The Directors' Liability Act was incorporated into subsequent Companies Acts of the United Kingdom. Although offerings of listed and unlisted securities in the United Kingdom are now subject to different statutory regimes,[31] both are subject to similar civil liability provisions with associated due care defences and to the *Misrepresentation Act 1967*.[32] In addition, common law remedies are available.[33]

Despite the minimal statutory regulation of takeovers in the United Kingdom, the Code on Takeovers and Mergers encourages full disclosure of material information in the making of takeover offers. Inadequate disclosure may lead to disciplinary proceedings or a referral to the Takeovers Panel which has responsibility for supervising compliance with the Code.

No general prohibition against misleading or deceptive conduct in the course of trade exists in United Kingdom law. Remedies for an investor suffering loss from a misleading or deceptive representation are provided in the statutes indicated above or at common law.

New Zealand

The New Zealand *Securities Act 1978* and *Securities Regulations 1983* impose civil liability for misstatements in a prospectus coupled with due diligence defences.

Takeovers in New Zealand are primarily regulated by the *Companies Amendment Act 1963*. The Listing Rules of the New Zealand Stock Exchange provide limited regulation of takeover offers for listed companies.[34] The 1963 Act is based on provisions in the Australian Uniform Companies legislation enacted in the early 1960s. Its purpose is to protect shareholders by ensuring they have sufficient time and information

---

[31] The contents of a prospectus for offerings of listed securities are regulated by the *Financial Services Act 1986* and the London Stock Exchange Listing Rules, and for unlisted securities by the *Public Offers of Securities Regulations 1995* and the *Companies Act 1985*. Liability with associated due care defences for false and misleading statements in a prospectus lies in ss 150 and 151 of the *Financial Services Act 1986* for listed securities and in Regulations 14 and 15 of the *Public Offers of Securities Regulations 1995* for unlisted securities. The *Public Offers of Securities Regulations 1995*, made under the *European Communities Act 1972*, implement the requirements of the EC Prospectus Directive 89/298/EEC.

[32] The *Misrepresentation Act 1967* would allow a claim for damages against the company for a misrepresentation made by or on behalf of the company which has induced subscribers to enter into a contract of allotment. The misrepresentation may arise in documents other than a prospectus. However, the remedy is only against the contracting party. The party will be entitled to damages unless the party making the representation proves they had reasonable grounds of belief, and actual belief, that up to the time the contract was made, the facts represented were true.

[33] Common law remedies available include rescission, action for damages for the tort of deceit, damages for negligent representation, and damages for breach of contract.

[34] The *Companies Amendment Act 1963* applies to companies registered under the *Companies Act 1955* as well as to those coming within the *Companies Act 1993*, by virtue of the *Company Law Reform (Miscellaneous Provisions) Act 1994*.

to make an appropriate decision.[35] Disclosure requirements are coupled with civil liability provisions for false and misleading takeover offer documents and due diligence defences.[36] Enactment of a proposed Takeovers Code was deferred indefinitely by the New Zealand Government in August 1995.

New Zealand enacted a Fair Trading Act in 1986, modelled on Part V of the Trade Practices Act, which has its genesis in requirements for harmonisation between New Zealand and Australia under the Closer Economic Relations Treaty. Section 9 of the Fair Trading Act is identical to section 52 of the Trade Practices Act and no defence is provided. Principles drawn from section 52 cases are considered relevant to the interpretation of section 9 of the Fair Trading Act.

United States

Civil liability and associated defences in relation to fundraising are governed in the United States of America by the *Securities Act 1933* (known as the 'truth in securities Act') passed by Congress following the collapse of the Wall Street stock market in 1929.[37] The Act was adopted 'to bring back public confidence in the securities market'.[38] The Act was to achieve this through a system of mandatory disclosure of material information coupled with due diligence defences, based on the *Companies Act 1929* (UK).[39] A plaintiff may also have a claim under section 10(b) of the *Securities Exchange Act 1934* and Securities Exchange Commission Rule 10b-5. Actions under these heads of liability require proof of intent. The civil liability provisions are designed to secure adherence to high standards of conduct through the 'in terrorem' nature of the liabilities[40] and the defences were intended to improve the standards of conduct in the distribution of securities by imposing standards of honesty, care and competence.[41]

---

[35] *Carr v New Zealand Refrigerating Co. Ltd.* [1976] 2 NZLR 135.

[36] Under s 10 of the *Companies Amendment Act 1963*, the civil liability provisions in the *Securities Act 1978* for misstatements in a prospectus extend to misstatements in takeover offer documents.

[37] In 1911, Kansas passed the first state investor protection legislation (known as 'blue sky law') which was subsequently used as a model for securities laws in other states. However, the state laws were generally regarded as ineffective in eliminating securities fraud.

[38] President F D Roosevelt, H.R. Rep No. 85, 73rd Cong. 1st Sess. 2 (1933).

[39] Section 11 of the *Securities Act 1933* provides a remedy, subject to due diligence defences, to a person acquiring a security where a prospectus has been filed in a registration statement and it contains an untrue statement of a material fact or a material omission. The issuer is strictly liable. Under s 12(2), liability is imposed on a director who is responsible for disseminating misleading information in relation to an offer or a sale of securities. A due diligence defence is also provided.

[40] In *Globus v Law Research Service Inc* 418 F 2d 1276, at 1288 (CA2, 1969), the Court noted that 'civil liability under section 11 and similar provisions was designed not so much to compensate the defrauded purchaser as to promote enforcement of the Act and to deter negligence by providing a penalty for those who fail in their duties'.

[41] H.R. No. 85, 73 Cong. 1st Sess. (1933) 5.

The Federal law in the USA regulating 'tender offers' (takeover offers) is the Securities Exchange Act, as amended by the *Williams Act 1968*.[42] Before the adoption of the Williams Act, little Federal or State law regulated takeovers.[43] In the 1960s, there was an increase in takeover activity as corporations sought to avoid Federal statutory provisions regulating mergers.[44] The Williams Act, and subsequent state legislation, was enacted to fill this gap. In contrast with the State laws which generally aim at deterring takeovers to protect incumbent management and employees in the target company, the Williams Act is designed to protect investors through mandatory disclosure. Material misstatements or omissions in the disclosure documents give rise to an action for damages for loss suffered where the plaintiff proves reliance on the misstatement or omission. A defence of good faith and absence of knowledge that the statement was false or misleading is provided.

Consumer protection in the USA is governed by Federal and State laws. Section 5(1)(a) of the *Federal Trade Commission Act 1914*, comparable to section 52 of the Trade Practices Act, provides that 'unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce, are hereby declared unlawful'.[45] The Federal Trade Commission imposes 'cease and desist orders' following a contravention where proceedings would be in the public interest. The Act does not enable personal actions to be brought. Rather, State consumer laws provide liability damages for unfair and deceptive practices. Most of the States have provisions mirroring section 5(1)(a) of the Federal Trade Commission Act.[46] The general rule is that state consumer legislation does not cover securities fraud.[47] Securities actions are normally exempt from the ambit of State consumer protection statutes because either securities transactions are outside the scope of a 'consumer' transaction[48] or because securities are regulated under another act or agency.[49]

---

[42] The Williams Act covers securities registered under the Securities Exchange Act and sets out the rules for open market acquisitions, privately negotiated acquisitions and tender offers.

[43] Booth, RA, 'The Problem with Federal Tender Offer Law' Vol 77 *California Law Review* 707 at 713.

[44] Hazen, TL, *Securities Regulation,* West Publishing Co., 1991 at p 687.

[45] In its original form, the Federal Trade Commission Act merely prohibited 'unfair methods of competition'. In 1938, the *Wheeler-Lea Amendment* inserted the additional phrase: 'unfair or deceptive acts or practices in commerce' thus introducing consumer protection legislation.

[46] The State legislation coexists with and complements existing federal trade laws as long as the state laws do not conflict with the Federal law and operate in furtherance of Federal policy: *Corpus Juris Secundum*, Volume 21, West Publishing 1995, p 370.

[47] For example, *Robertson v White* 633 F.Supp. 954 (1986).

[48] For example, securities fraud was held not to be within the scope of coverage of the Texas *Deceptive Trade Practices and Consumer Protection Act* when the defendant argued before the US District Court that shares did not fall within the definition of goods: *Allais v Donaldson, Lufkin & Jenrette* 532 F.Supp. 749 (1982).

[49] For example, in *Allais v Donaldson, Lufkin & Jenrette* 532 F.Supp. 749 at 752 (1982), the US District Court held that the Texas *Deceptive Trade Practices and Consumer Protection Act* did not apply to a broker's advice as to the value of purchasing a security because the Texas Blue Sky Law had due diligence defences which would be 'emasculated' if the consumer statute, which had no such defences, applied to the case.

Canada

Fundraising is largely regulated under provincial legislation. Most provinces of Canada have legislation based on the USA legislation. In Ontario, which is generally regarded as the leading province in securities regulation, civil liability provisions of the Ontario Securities Act are based on section 11 of the *Securities Act 1933* (USA).

Takeover bids are regulated by Provincial Securities Acts and the Federal Canada Business Corporations Act (the CBCA). Civil liability under the Ontario Securities Act for misrepresentation in takeover disclosure documents is coupled with due care defences. Part XVII of the CBCA, regulating takeover bids, is modelled on the takeover provisions of the Ontario Securities Act.

Consumer protection in Canada is governed by Federal and State laws. At present, under section 52(1)(a) of the Federal *Competition Act*, it is an offence to make a representation to the public that is false or misleading in a material respect for the purpose of promoting the supply or use of a product or for the purpose of promoting any business interest. Civil liability in damages is imposed for contravention of this provision. Criminal and civil liability are subject to a defence of reasonable precautions and the exercise of due diligence. This provision is currently under review by the Canadian government.

The *Business Practices Act* of Ontario contains a prohibition against engaging in unfair practices, including the making of false, misleading or deceptive representations in connection with the supply of ‘goods’. Securities are expressly excluded from the definition of ‘goods’.

Publications of the Simplification Program

Stage 1

December 1993	Plan of action
March 1994	Share buy-backs - Proposal for simplification
March 1994	Small business - Proposal to simplify proprietary companies
April 1994	Company registers - Proposal for simplification
July 1994	First Corporate Law Simplification Bill - Exposure draft
December 1994	First Corporate Law Simplification Bill - (introduced into Parliament)

Stage 2

May 1994	Annual returns and Financial Reporting to shareholders - Proposals for simplification
August 1994	Plan of action - Stage 2
August 1994	Defunct companies - Deregistration and reinstatement Proposal for simplification
October 1994	Accounts and audit - Proposal for simplification
November 1994	Share capital rules - Proposal for simplification
November 1994	Company names - Proposal for simplification
December 1994	Forming a company - Proposal for simplification
December 1994	Company meetings - Proposal for simplification
June 1995	Second Corporate Law Simplification Bill - Exposure Draft and Commentary
August 1996	Second Corporate Law Simplification Bill and Explanatory Memorandum (referred to Parliamentary Joint Committee on Corporations and Securities)

Stage 3

April 1995	Plan of action - Stage 3
June 1995	Organising the Law Drafting issues
June 1995	Designing the Law Drafting issues
September 1995	A singular use of THEY Drafting issues
October 1995	Officers and related party transactions - Proposal for simplification
November 1995	Fundraising Trade Practices Act, s 52 and securities dealings
January 1996	Takeovers - Proposal for simplification
September 1996	Section 52 Trade Practices Act and dealings in securities