CHAPTER 16

OTHER MATTERS

16.1 In the course of the inquiry by the PJSC some suggestions were made to the PJSC that other additional matters arising from the *Company Law Review Act 1998* ought to be dealt with in subsequent legislation. These additional matters are discussed below.

Redeemable preference shares

16.2 A number of submissions drew attention to the operation of redeemable preference shares under the new section 254K of the Corporations Law, inserted by the *Company Law Review Act 1998*.[1] Ernst & Young told the PJSC that the section will prevent redeemable preference shares (RPFs) from being used in the manner originally intended as withdrawable/returnable capital. The problem is caused by the extension of 'capital maintenance' requirements to RPFs under section 254K. Previously, only the par value of RPFs was required to be included under the 'maintenance of capital' requirements. The par value, which was very small relative to the premium, was redeemable from profits or from the proceeds of new issues of shares. The share premium was recorded when the shares were issued and eliminated when the shares were redeemed. The share premium reserve was used to pay the premium on RPFs. Accordingly, RPFs were structured with a low par value and a high share premium.

16.3 Ernst & Young advised the PJSC that the Law requires the whole of the value of the share (par value and share premium) to be maintained by the proceeds of a new share issue or out of profits. This is inconsistent with the removal of the 'capital maintenance' concept in Chapter 2J of the Law. At its hearing on 16 June 1999, Mrs Ruth Picker, a Partner with Ernst & Young, told the PJSC that the redeemable preference share provisions should be repealed:

> It seems to me that dealing with one particular type of financial instrument, being a redeemable preference share in the law, and singling it out, has no purpose anymore. There does not seem to be any need for it, particularly now that par value has gone, particularly now that we have an accounting standard on how to account for these. In fact, in many cases a redeemable preference share would be classified as debt under the accounting standards, not as equity; not as capital in the first place. So there would be no need to have any kind of capital maintenance provision for it under the law. Our

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1 See for example Caltex Australia Ltd, Submission 30, pp 4-5 and Ernst & Young, Submissions 31 and 38a, pp 4-5 and pp 1-5.

> submission in relation to redeemable preference shares is to remove section 254KB, but, even further, to consider removing all provisions specifically relating to redeemable preference shares.[2]

Selective capital reductions

16.4 Section 256B of the Law relates to capital reductions and section 256C specifies the requirements for shareholder approval for what are called "equal reductions" and "selective reductions". Under 256B(2) a reduction in share capital is an "equal reduction" if it relates only to ordinary shares, it applies to each holder of ordinary shares in proportion to the number of ordinary shares they hold, and the terms of the reduction are the same for each holder of ordinary shares. For an "equal reduction" the Law requires an ordinary resolution by shareholders. If unequal amounts are paid in a reduction of share capital, proportionate to the amount paid up on the shares, then it is a "selective reduction". In this case, the Law requires either (a) a special resolution where no votes are cast in favour of the resolution by shareholders who will receive consideration as part of the reduction or (b) a unanimous resolution at a general meeting.

16.5 Dr Elizabeth Boros of the Law Institute of Victoria told the PJSC that under the procedures for shareholder approval of "selective reductions" a unanimous resolution was not likely to happen for any listed company. To reduce the capital under these circumstances the company would need to pay an equal amount for each share, whether fully paid up or not. Dr Boros noted that in some cases under the current provision the selective reduction approval requirement has the unintended effect of delivering "disproportionate power to one dissenting shareholder".[3] Dr Boros recommended that the Law should provide for a class protection mechanism in place of the current approval requirements. Dr Boros referred to the judgment of Santow J in the case of Re ETRADE Australia Limited (1999) NSWSC 254:

> The effect of that definition in the present circumstances would have been to give rise to the absurdity that in practical terms the necessary resolution could not have been passed unless there were total unanimity, inviting corporate blackmail. This is because no shareholder could vote under paragraph (a) – as all shareholders receive consideration as part of the resolution. That renders paragraph (b) applicable, requiring unanimity of all ordinary shareholders at the meeting. Even one dissenting shareholder could thus scuttle the proposal.[4]

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2 Mrs Ruth Picker, Committee Hansard, 16 June 1999, p 83.

3 Dr Elizabeth Boros, Committee Hansard, 16 June 1999, p 102.

4 Dr Elizabeth Boros, Committee Hansard, 16 June 1999, p 102.

Table of replaceable rules - section 141

16.6 Freehill Hollingdale and Page advised the PJSC that some confusion has resulted from amendments to section 141 which sets out the provisions of the Law that apply as replaceable rules. The purpose of the Table of replaceable rules is to assist users in particular small business for which the replaceable rules are principally designed. However, as a result of the amendments and the renumbering of the table items, the table is incomplete and inaccurate. To contain a complete and accurate list of the replaceable rules, Freehill Hollingdale and Page recommended that a reference to section 224D should be inserted in Table item 2.[5]

Drafting of section 112(4)

16.7 Section 112 of the Law deals with the two types of proprietary companies and four types of public companies that can be registered. Section 112(4) which deals with restrictions on tribute arrangements for a no liability company replaces former section 398 of the Law. Mr Stephen Stockwell, a Senior Associate with Mallesons Stephen Jacques, submitted that in duplicating the restriction in the former section, new section 112(4) has omitted an important requirement thereby creating an anomaly under that section.[6] Specifically, section 112(4) makes no reference to a 3 month time limit on the duration of a tribute arrangement effected without shareholder approval which was in the former section. Mr Stockwell advised that there did not appear to be any basis for a change in the Law.

Anomalies in the Company Law Review Act

16.8 In addition to its written submission to the PJSC, the Law Institute of Victoria provided the PJSC with a summary of drafting anomalies contained in the *Company Law Review Act 1998*. [7] Some of these drafting issues have been considered by the PJSC elsewhere in this Report. The remaining anomalies are of a technical kind.

Conclusion

16.9 The PJSC has not undertaken an inquiry into the additional matters raised and is therefore unable to offer a definitive judgment on the merits of the drafting issues and the particular anomalies arising from the Company Law Review Act. However, the PJSC has made available all of those comments and suggested amendments to the Government for further consideration.

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5 Freehill Hollingdale and Page, Submission 3, p 1.

6 Mr Stephen Stockwell, Submission 86, p 2.

7 Law Institute of Victoria, Submission 55a, pp 1-5.

Senator Grant Chapman

Chairman