

THE SHAREHOLDER



A BIANNUAL NEWSLETTER PRODUCED BY IMF

March 2009
Issue 7

IMF's SHAREHOLDER NEWSLETTER IS BACK

After a brief absence IMF's Shareholder Newsletter is back. The newsletter will now be published biannually and will provide an update on recent developments relevant to shareholders' rights .

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COMPETING CLASS ACTIONS AND LITIGATION COMMITTEES

Finkelstein J, before he ruled himself out of play, sought to develop class action procedures where two competing class actions are filed *and to develop greater involvement in the control of proceedings*. On 9 May 2008 proceedings were commenced by Kirby against companies in the Centro group ("Centro") (the "Kirby proceedings"). These proceedings were filed by Maurice Blackburn lawyers and are funded by IMF. Shortly thereafter proceedings were commenced by Slater & Gordon on behalf of Centro shareholders funded by a different litigation funder (the "Vlachos proceedings").

The Kirby and Vlachos proceedings are substantially similar in that they both allege that Centro breached its continuous disclosure obligations and engaged in misleading and deceptive conduct. The key difference between the proceedings is that the Kirby proceedings are brought on behalf of a closed class (investors who had purchased shares within a prescribed period and who had entered into a funding agreement with IMF) and the Vlachos proceedings are brought on behalf of an open class (being all investors who had purchased shares within a prescribed period). Centro applied to the Court to stay the Vlachos proceedings until the Kirby proceedings had been concluded. Kirby supported this application.

When faced with multiple actions dealing with the same facts and issues, Finkelstein J could have either stayed one set of proceedings,

ordered joint trials or for the matters to be consolidated. In October 2008, he indicated that before deciding how to proceed he would like to know the views of class members of both actions. His view was that the guiding principle behind any decision should be what is in the best interests of the group members. He proposed that a litigation committee for each action be established to ascertain the views of class members and requested submissions from the parties regarding this suggestion.

Finkelstein J, also suggested that where multiple class actions concerning common facts and legal issues had been commenced, it might be appropriate to conduct a sealed bid auction process to determine which law firm should run the case. His preference was that the firm should be selected by the Court, having received the opinion of the litigation committees.

In response to the Judge's invitation for submissions regarding these proposals, both Kirby and Vlachos objected to the proposals. However, as Justice Finkelstein has directed that the case be allocated to another Judge (see article below – 'Judges and their Shareholdings') it remains to be seen whether these suggestions will be adopted by another Judge.

RECOVERY IN AN INSOLVENCY CONTEXT - SONS OF GWALIA

In the landmark 2007 *Sons of Gwalia* decision, the High Court held that a shareholder who had been misled at the time of purchasing shares was entitled to rank equally with other unsecured creditors' in the company's administration.

"The decision has had significant implications for the conduct of external administrations, as well as for the provision of corporate debt finance. In September 2007 the Corporate and Markets Advisory Committee (CAMAC) released a discussion paper responding to the High Court's decision. 20 submissions were received. On 29 January 2009 CAMAC released its report recommending that no action be taken to overturn the effect of the High Court's decision. The Committee noted that legislation to provide aggrieved shareholders with direct rights of action in respect of corporate misconduct should not be undermined as shareholder actions complement the role of regulators in relation to corporate disclosure.

The Committee acknowledged concerns that shareholder claims may add complexity, expense and delay to the conduct of external administrations but did not feel that this was a compelling reason to interfere with the High Court's decision. The Committee has made some suggestions regarding the efficient conduct of external administrations involving claims by shareholders and recommended that the position be monitored and, if necessary, there be legislative intervention in due course.

In any event, it seems that some external controllers have already come to grips with the ramifications of the High Court's decision and adopted pragmatic and novel approaches to deal with the claims of aggrieved shareholders alongside those of traditional unsecured creditors. The Sons of Gwalia administration is a good example.

In December 2007, following negotiations between IMF and Ferrier Hodgson, the administrators of the Sons of Gwalia group ("SOG"), creditors voted overwhelmingly to support a proposed amendment to the Deed of Company

Arrangement to allow for the payment of an interim dividend to creditors, including shareholders with a claim against the Company.

The basis for the proposal was an agreement that the shareholder claims' validity was due to the wrongdoing by SOG's directors and auditors. The dilemma faced by the Administrators was that if the shareholder claims were accepted and subsequent proceedings to recover against the directors and auditors were unsuccessful, the Administrators may have paid out the shareholders' claims in circumstances where they should not have done so.

The compromise position involved the Administrator agreeing in mid 2008 to pay out from "the first pool" (being approximately \$130 million held by the Administrators) to all creditors, including eligible shareholders (whose claims totalled approximately \$260 million) who could prove they purchased shares within the period that they had been misled. Shareholders funded by IMF received approximately \$10 million from the "first pool" payout. A second distribution of a similar amount is expected during the course of 2009.

This first pool payment was made on the basis that shareholders agreed to the negotiated arrangement and that the claims of the shareholders against the directors and auditors would be joined with the existing claims of SOG against SOG's directors and the auditors. If the litigation is ultimately successful, the shareholders will receive their pro rata share via a third payment (being funds arising from the litigation).

The compromise solution has ensured an early payment to all creditors (including eligible shareholders) and that the maximum recovery possible against the directors and auditors will be achieved for all creditors.

IMF is funding a number of other matters where the defendant company is under external control (for example ION Ltd and ABC Learning Centres Ltd). It is hoped that the pragmatic approach adopted by the Administrators in SOG will serve as a useful example of how external controllers can efficiently resolve shareholder proofs of debt and maximise creditor returns.

PRODUCTION OF INSURANCE POLICIES PRIOR TO AND IN LITIGATION

One of the biggest difficulties faced by shareholders seeking to bring an action against a company is establishing the extent of the potential defendant's financial resources to satisfy a judgment. The existence of an insurance policy which will respond to the claim is an important consideration.

Defendants can be compelled to produce insurance policies to an 'eligible applicant' (including ASIC, a liquidator or administrator) pursuant to the examination provisions of the Corporations Act. However, there is no general right for shareholders to access a company's insurance policies. A potential claimant may be able to invoke the procedural rules relating to pre-action discovery to gain access to insurance policies. However, it remains to be seen how the courts will deal with these applications.

Even once litigation has been commenced, documents relevant to a defendant's insurance cover can only be discovered in limited circumstances. The general rule is that documents which relate to a 'matter in dispute' in the proceedings are discoverable. Although there is limited authority, it seems that the courts have narrowly construed 'matter in dispute' to deny discovery of insurance documents.

However, in a 2007 English case, *Josh Harcourt v FEF Griffin [2007] EWHC 1500 (QB)*, the High Court considered that the aim of the rules was to "to avoid waste of time and cost and to ensure swift and, as far as possible, proportionate and economical litigation". As the existence of an insurance policy (and its terms) was central to the plaintiff's decision whether to proceed with the case or not, the court held that the policy was discoverable.

Arguably, this English case is limited to its facts. However, in recent years there has been increasing focus on managing the rising cost of litigation and to limit well-resourced litigants, particularly assisted by insurance funding, causing unnecessary delay and cost in the resolution of claims

IMF awaits future developments in this area with interest.

ARISTOCRAT SETTLEMENT

In August 2008 Justice Stone approved the settlement of the Aristocrat class action. The settlement of \$135 million plus \$8.5 million for costs is the largest shareholder class action settlement to date.

The Aristocrat proceedings were commenced in 2004 and heard by Justice Stone in the Federal Court of Australia during the course of 2007. During the trial Aristocrat did not deny that it had overstated its profit forecasts and had failed to provide timely information to the market. The main issues remaining for determination by the Court were causation and quantification of loss. The settlement of the action means that there is still no clear guidance as to which of a number of competing loss theories will be accepted by the courts. On 21 January 2009 Justice Stone J handed down her reasons for approving the settlement in August 2008.

Section 33V of the Federal Court Act provides that a representative proceeding may not be settled without the approval of the Court.

In considering whether to give approval to a proposed settlement the court will consider whether it is fair, reasonable and adequate in the circumstances of all group members.

In making her determination, Justice Stone considered three aspects of the proposed settlement - the amount of the

settlement, the mechanics of the settlement process and costs. She found all three to be fair, reasonable and adequate.

In considering the first of these factors, Justice Stone made some interesting comments regarding the (confidential) "Loss Assessment Formula" that had been developed to calculate each participating group member's entitlement under the settlement.

Pursuant to the settlement, it was agreed that Aristocrat would pay:

1. \$109 million in respect of the claims of funded group members, with Aristocrat retaining no right or interest to any part of that money after distribution to group members; and
2. \$27 million in respect of the claims of non-funded group members, with any balance outstanding after distribution to be refunded to Aristocrat.

The Loss Assessment Formula was designed to ensure that group members funded by IMF and non-funded group members would ultimately recover similar proportions of their estimated losses. The effect of Justice Stone's approval is that non-funded group members were not able to "free ride" and obtain a greater recovery than funded group members who had, in effect, paid for the proceedings to be brought.

DOWNER SETTLEMENT BEFORE LITIGATION

In May 2007 IMF announced that it intended to fund an action against Downer EDI Limited ("Downer") on behalf of shareholders who had purchased shares in the company between 23 February 2006 and 7 August 2006 and who had entered into a funding agreement with IMF ("the group members").

The proposed action was based on allegations that Downer had engaged in misleading and deceptive conduct when issuing a profit guidance in February 2006 and that Downer had acted in breach of its continuous disclosure obligations in failing to inform the market about losses in connection with a project concerning Iluka Resources Limited.

In October 2007 Slater & Gordon, the lawyers instructed by IMF to conduct the proceedings, provided Downer with a draft application and statement of claim and invited Downer to enter into settlement discussions before the claim was filed in the Federal Court. An expert was appointed to perform a preliminary assessment of the group members' loss.

At a mediation in September 2008 the parties agreed to settle the claim (for a confidential sum) conditional upon the group members voting to accept the settlement sum.

The group members subsequently voted to agree to the settlement.

The resolution of this matter within 18 months of IMF's decision to fund the class action is a first for IMF. Until now, class actions funded by IMF have taken some years to resolve with numerous and costly disputes over pleadings and other interlocutory skirmishes.

IMF believes that a pragmatic and open approach to litigation is required to minimise legal costs and ensure a speedy return to aggrieved shareholders. The Downer case is a good example of how it is possible, with cooperation, to facilitate the early resolution of a claim, saving both sides millions of dollars in legal fees. IMF encourages the opportunity to explore settlement at an early stage in all of the matters it funds.

ABC LEARNING CENTRES CREDITORS' COMMITTEE

On 6 November 2008 Ferrier Hodgson was appointed administrators and McGrathNicol was appointed receivers and managers to the ABC Learning Centres group ("ABC").

At the first creditors' meeting on 18 November 2008, one of IMF's clients was appointed to the creditors' committee.

Committees of creditors, which comprise a number of creditors, may be appointed by the general body of creditors to assist the Administrator with matters relevant to the administration and to receive and consider reports by the administrator. The committee's role is consultative only. The committee is appointed at the first meeting of creditors and the committee continues in existence while the administration continues.

The appointment of one of IMF's clients to the committee is a new and welcome development and recognises (in line with the *Sons of Gwalia* decision) that shareholders with claims against a company in administration are a relevant interest group who can offer assistance to the external controllers and are entitled to have their views considered and to receive adequate and timely information concerning the administration process.

To apply for funding please contact:

SYDNEY	BRISBANE	MELBOURNE	PERTH
John Walker or Clive Bowman	Andrew Charles	Simon Dluzniak	Hugh McLernon or Charlie Gollow
Level 5, 32 Martin Place Sydney NSW 2000	Level 5 232 Adelaide Street Brisbane QLD 4001	Level 3 480 Collins Street, Melbourne VIC 3000	Level 6, Citibank House 37 St George's Terrace Perth WA 6000
Tel: +61 2 8223 3567 Fax: +61 2 8223 3555	Tel: +61 7 3221 7651 Fax: +61 2 8223 3555	Tel: +61 3 9629 1211 Fax: +61 2 8223 3555	Tel: +61 8 9225 2300 Fax: +61 8 9225 2399

IMF (Australia) Ltd**CENTRO
MEDIATION**

In December 2007, Justice Ryan made orders that the Centro class actions be mediated by 17 April 2009.

This is a welcome development which IMF hopes will also facilitate the early resolution of the proceedings before substantial legal costs are incurred.

**JUDGES
AND THEIR
SHARE-
HOLDINGS**

In November 2008, Finkelstein J ordered that the Centro case be reallocated to another Federal Court Judge. The basis of this decision was that as he had an interest in Centro Property Group through a self-managed superannuation fund there may be a reasonable apprehension of bias by "fair minded lay observers". Lawyers for Centro argued that the fact that the Judge's fund had sold the Centro shares, rather than relieving the Judge of any reasonable apprehension of bias, strengthened their argument as a loss (of approximately \$19,000) had been crystallised by the sale.

NEWS IN BRIEF**IMF's MELBOURNE OFFICE**

IMF's Melbourne office opened in May 2008 and is conveniently located at Level 3, 480 Collins Street Melbourne. Please contact Simon Dluzniak on (03) 9629 1211 or sdluzniak@imf.com.au for any enquiries.

"LESSONS FROM ARISTOCRAT" CONFERENCE

In September 2008 IMF hosted conferences in Sydney and Melbourne for its clients and other key stakeholders. Given the settlement of the Aristocrat claim, the aim of the conference was to share the wealth of information that IMF obtained in the course of running the case. The aim of the conference was to provide an opportunity to discuss issues facing our clients when participating in shareholder actions. Speakers and panel members included counsel, representatives of our clients, ASIC and Maurice Blackburn. The papers can be found on IMF's website.

www.imf.com.au/presentations/LessonsFromAristocrat.pdf

IMF's ANNUAL GENERAL MEETING

IMF's Annual General Meeting was held on Friday, 7 November 2008 at the Westin Hotel, 1 Martin Place, Sydney. The meeting was broadcast on Boardroom Radio and a recording is available via IMF's website. IMF's annual report and the presentation given at the AGM may be accessed via the following link: www.imf.com.au/info.asp?content=announcements

VICTORIAN LAW REFORM COMMISSION CIVIL JUSTICE REVIEW

The Victorian Law Reform Commission's Civil Justice Review Report was published in May 2008 following a lengthy consultation with stakeholders commencing in September 2006. The proposals are currently being considered by the Victorian Government and, if accepted, will have a significant impact on the civil justice system and aims to reduce the cost, complexity and length of civil trials.

The chapter "*Achieving Greater Access to Justice*" makes eight recommendations regarding litigation funding. The report further recommends that the court should have discretion to order disclosure of a party's insurance policy or funding arrangement. The report does not address the need for regulation of existing litigation funders, an issue currently being considered by the Standing Committee of Attorneys-General. The Report can be viewed at www.lawreform.vic.gov.au

IMF Submissions are at: www.imf.com.au/pub.asp?content=legalci

A LIST OF FUNDED MULTI-PARTY SHAREHOLDER ACTIONS AND PROPOSED ACTIONS CAN BE VIEWED AT:

<http://www.imf.com.au/cases.asp?content=casemain&showlist=1>

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