6.3.2 Securities Act 1978

Civil liability for Misstatements

Changes to this area of law came into effect on 25 October 2006. The position now is that Part II of the 78 Act contains a heading entitled, “Liability of Issuers, etc., and Offences”. The first section here is section 55 which deals with the interpretation of the subsequent provisions relating to advertisements and prospectuses. Thus, a statement is deemed to be untrue it is misleading on the form and context in which it is included.

Immediately after section 55, a new heading and new sections 55A to 55G appear. These sections were inserted by the Securities Amendment Act 2006 and are now in force. The new heading is “Civil liability”. Section 55A says that certain civil remedies are available if there is a “civil liability event”. The civil remedies are a pecuniary penalty order (a maximum of $500, 000 for an individual and $5 million for a corporation) and declaration of civil liability (on application by the NZSC only) under section 55C and compensation under section 55G.

Section 55B defines civil liability events as distribution of an advertisement or registered prospectus that includes an untrue statement or a breach of regulations made under the 78 Act relating to the offer, sale or management of interests in contributory mortgages.

Section 55C states when a court (on application by the NZSC) may make pecuniary penalty orders and declarations of civil liability. Section 55D then goes on to spell out the purpose and effect of declarations of civil liability. Section 55D (1) states that the purpose of a declaration of civil liability is to enable a person who brings proceedings under section 55G (compensation orders) to rely on the declaration and not be required to prove the civil liability event. Section 55E then says what declarations of civil liability must state.

Section 55G deals with compensation orders. Section 55G (1) gives the court power to order a liable person to pay compensation to all or any persons who subscribed for securities on the faith of an advertisement or registered prospectus that contains an untrue statement. A “liable person” is a person liable for a civil liability event under ss. 56-7 of the 78 Act.

Issuers, directors and promoters may be liable to pay compensation to persons who subscribe for securities on the faith of an advertisement (“advertisement” includes an investment statement by reason of section 2A (2) (b) of the Act) or registered prospectus which contains
any untrue statement and who sustain loss or damage by reason of the untrue statement: s 56. Where the issuer is an individual, the issuer of the securities is liable for the misstatement: s 56(1) (a).

In the case of an advertisement, every person is liable who (1) is a director of the issuer at the time that the advertisement is distributed; or (2) has authorised being named and is named in the advertisement as a director of the issuer; or (3) has agreed to become a director either immediately or after a period of time: s 56 (1) (b).

In the case of a registered prospectus, every person is liable who (1) has signed the prospectus as a director of the issuer; or (2) has authorised being named and is named in the prospectus as a director of the issuer; or (3) has agreed to become a director after an interval of time: s 56(1)(c).

Every promoter of the securities is also liable for any untrue statements: s 56(1) (d).

A statement included in an advertisement or registered prospectus is deemed untrue if it is misleading. A statement is misleading either in the form and context in which it is included or by reason of the omission of a material particular: s 55. As to falsehood by omission, note that the non-disclosure must have the effect of amounting to deception or the creation of a false impression.

Exceptions to liability under sections 55 and 56 fall into two categories. First, in respect of a registered prospectus no person is liable if he or she proves that (1) having consented to becoming a director of the issuer, consent was withdrawn before distribution; and (2) written notice of the withdrawal and the reason for it was given to the NZSC, and, (3) the registered prospectus was distributed without his consent or authority: s. 56(2). Second, in respect of an advertisement or registered prospectus, liability may be avoided where (in general), there is proof of lack of knowledge or consent, consent was withdrawn and notification made or there were reasonable grounds to believe the statement was true: s. 56(3).

For an analysis of these provisions before the 2006 amendments, see P Fitzsimons, “If the Truth be Known: The Securities Act 1978 and Directors’ Liability for Misstatements in a Prospectus” (1999) 5 NZBLQ 164. Note that the majority of the New Zealand case law has involved criminal liability for misstatements. Readers are directed to section 12.2 herein for
discussion of this case law. There are substantial overlaps with civil liability, which go to the ingredients of the civil and criminal offences.

Section 57 deals with civil liability for misstatements by experts and section 57A deals with civil liability for breach of the contributory mortgage regulations.

Under the heading, “General provisions on civil liability remedies”, sections 57B to 57E appear. These comprise machinery provisions dealing with matters such as standard of proof.

6.3.3 Companies Act 1993

Various provisions of the Companies Act 1993 could be regarded as providing relief for forms of fraud or manipulative conduct. An example is the statutory remedy for oppression.

6.3.4 Insider Trading

As stated elsewhere, a major overhaul of insider trading legislation in the SMA came into force in February 2008. The reforms are based on the Australian model.1

In New Zealand, there exist three principal avenues to the control of insider trading. At common law, a shareholder could recover from a director of a company where the director purchased shares off the shareholder.2 However, to succeed with such an action the courts held that it is necessary to establish a fiduciary relationship between the parties,3 which would normally be only available in private companies.4

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3 Woodhouse J stated that some of these factors included a “dependence upon information and advice, the existence of a relationship of confidence, the significance of some particular transaction for the parties, and of course the extent of any positive action taken by or on behalf of the directors to promote it.” Id., 325.

4 In Cotton v. GUS Properties Ltd (1995) 7 NZCLC 260,821 the Court of Appeal confirmed the applicability of the Coleman v. Myers decision and discussed that decision in context of a non-listed company which had 200 shareholders. The Court was prepared to find that directors “intending to participate as purchasers in the share exchange, owed a duty to shareholders to ensure they were fully
The Companies Act 1993 has provisions dealing with insider trading. Section 145 prohibits a director from disclosing company information to any person, or using the information without the consent of the board. Similarly, section 148 requires a director to disclose share dealings in the company shares to the board. Section 149 goes further and restricts a director who possesses company information “which is information material to an assessment of the value of shares” from acquiring or disposing of these shares unless the consideration given or received “is not less than the fair value of these shares or security”. 5 Under section 149 (4), the director is liable to the person from whom the shares were purchased or to whom they were sold for the difference between the sale price and the fair value of the shares. However, section 149 does not apply in relation to a company to which Part 1 of the SMA applies. 6

The third and principal means of dealing with insider trading in listed companies has been - since 1998 - the provisions of the SMA. In broad overview, the insider trading regime in effect between December 1998 and 29 February 2008 was ineffective. And while it may be that case law under the 1998-2008 will be of assistance in interpreting the new post-February 2008 regime, the better view is that scrutiny of the Australian law - upon which the New Zealand post-February 2008 insider trading regime is modelled - will be of more utility. Accordingly, all of the previous discussion and analysis of insider trading in New Zealand under the 1998-2008 SMA regime appearing in this Booklet has been jettisoned.

6.3.5 The New Insider Trading Regime

We begin by noting that the NZSC has published a guide (available for download on its website) to the new regime. The guide is entitled, NZSC, New Securities Law for Investment Advisers and Market Participants 2008: A guide to new requirements under the Securities Markets act 1988 (2008).

Part 1 of the SMA creates three criminal offences in relation to insider conduct in relation to securities: These are:

5 Section 149 (1). Section 149 (2) provides that “the fair value of shares or securities is to be determined on the basis of all information known to the director or publicly available at the time”.

6 Section 149 (6).
the trading offence appearing in section 8C;

the disclosing (“tipping”) offence contained in section 8D, and

the advising or encouraging offence contained in section 8E.

In addition, pursuant to section 11E, the same three offences apply to insider conduct in relation to futures contract(s). As we shall see, civil liability also attaches such that a person (called an “aggrieved person” in the SMA) make seek to recover loss or damage.

The ingredients of the insider trading offences:

(1) **Territorial connection:** The relevant insider conduct must occur within New Zealand. There is no provision in the SMA that captures conduct outside New Zealand as is the case in relation to the general dealing misconduct prohibition: see section 18.

(2) **Securities of a public issuer:** The relevant insider conduct must be in relation to securities. Section 2 of the SMA defines the term, “security”. Note here the particular definitions contained in paragraphs (b) and (c) of the definition which apply to Part 1, Subpart 1 of the SMA. The key part of the definition of a security appearing in paragraph (b) is that the security must have been allotted and listed on a registered exchange’s market. Paragraph (d) extends the meaning of a security further to catch that which we might describe as relevant interests in securities. The term, “public issuer” is also defined in section 2 of the SMA. It means a person who is a party to a listing agreement with a registered exchange or a person who was previously a party to a listing agreement with a registered exchange, in respect of any action or event or circumstance to which the SMA applied while the person was a party to a listing agreement with a registered exchange.

(3) **Information insider:** There must be an “information insider”. This term is defined in section 8A. A person is an information insider of a public issuer if that person (a) has material information relating to the public issuer that is not generally available to the market; and (b) knows or ought reasonably to know that the information is material information; and (c) knows or ought reasonably to know that the information is not generally available to the market. A public issuer may be an information insider of itself: see section 8A (2). Further, the relevant “inside information” means the
information in respect of which a person is an information insider of the public issuer in question: section 8B.

(4) **Material information relating to a public issuer:** An information insider must have material information. Although the term, “information” is not specifically defined in the SMA, note that section 4 of the SMA (definition of information generally available to the market) provides some guidance. Section 3 of the SMA defines material information in relation to a public issuer as information that (a) a reasonable person would expect, if it were generally available to the market, to have a material effect on the price of listed securities of the public issuer; and (b) relates to particular securities, a particular public issuer, or particular public issuers, rather than to securities generally or public issuers generally.

(5) **Information not generally available:** Pursuant to section 4, information is generally available to the market: (a) (i) if it is information that has been made known in a manner that would, or would be likely to, bring it to the attention of persons who commonly invest in relevant securities; and (a) (ii) since it was made known, a reasonable period for it to be disseminated among those persons has expired or (b) if it is likely that persons who commonly invest in relevant securities can readily obtain the information - whether by observation, use of expertise, purchased from other persons, or any other means – or (c) if it is information that consists of deductions, conclusions, or inferences made or drawn from either or both of the kinds of information referred to in paragraphs (a) and (b).

(6) **Materiality:** The prohibition against insider conduct applies only where a reasonable person would expect that the material information, if it were generally available to the market, would have a material effect on the price of listed securities of the public issuer. This is an objective test.

(7) **Knowledge:** Pursuant to section 8A, it must be proved that the information insider knows or ought reasonably to know that the information is material information and on knows or ought reasonably to know that the information is not generally available to the market.

**The Three Offences:**
(1) The Trading Offence: Where the ingredients described above are present, an information insider of a public issuer must not trade securities of the public issuer: section 8B.

(2) The Disclosing Offence: Where the ingredients described above are present, an information insider (A) of a public issuer must not directly or indirectly disclose inside information to another person (B) if A knows or ought reasonably to know or believe that B will, or is likely to trade securities of the public issuer or if B is already a holder of those securities, continue to hold them or advise or encourage another person (C) to trade or hold them.

(3) The Advising or Encouraging Offence: Where the ingredients described above are present, an information insider (A) of a public issuer must not (a) advise or encourage another person (B) to trade or hold securities of the public issuer or (b) advise or encourage (B) to advise or encourage another person (C) to trade or hold those securities.

Contravention of sections 8C to 8E is a criminal offence: see section 8F.

Exceptions to the prohibition: There are eight exceptions to the prohibition on the insider conduct. These are described in sections 9-9G.

Affirmative Defences: There are five affirmative defences. They are:

- absence of knowledge of trading: section 10;
- inside information obtained by independent research and analysis: section 10A;
- equal information: section 10B;
- options and trading plans: section 10C and
- Chinese wall defence: section 10D.

Criminal penalties: Section 43 provides for a criminal penalty for the criminal liability established in section 8F. For an individual, the maximum penalty is imprisonment for a term
not exceeding five years or a fine not exceeding $300,000 or both. For a company, the maximum penalty is a fine not exceeding $1,000,000.

**Civil Remedies:** Civil remedies are also available for breach of the insider conduct prohibition: see section 42W. First, the NZSC may seek a pecuniary penalty and declaration of contravention: section 42R. The maximum amount of a pecuniary penalty for a contravention of an insider conduct prohibition is the greater of (a) the consideration for the transaction that constituted the contravention (if any) or (b) three times the amount of the gain made, or the loss avoided, by the person in carrying out the conduct or (c) $1,000,000. Second, under section 42ZA, an “aggrieved person” who has suffered loss or who is likely to suffer loss, may apply for a compensatory order.
7. Tender Offers, Takeovers and other Corporate Combinations

7.1 General

A takeover involves someone acquiring enough shares in a company to give them “control” of the company. Often a takeover is a full takeover, where 100 per cent of the shares are acquired. A full takeover is sometimes called a “merger”. But a partial takeover is also possible. Here, the takeover bidder acquires a shareholding of less than 100 per cent but large enough to give control. The principal legislation is the Takeovers Act 1993.

The Takeovers Code

The Takeovers Code made pursuant to the Takeovers Act 1993 came into force on 1 July 2001. The Takeovers Code effectively deems a shareholding of 20 per cent or larger to be a controlling shareholding. This reflects the fact that, in many companies, that are listed on the NZX:

- There is a very large number of shareholders, many of whom hold only a small parcel of shares (that is, many companies are “widely held”); and

- Many shareholders do not exercise their voting rights.

In a “widely held” company, a 20 per cent or larger shareholding will commonly provide “effective” or “practical” control of the general meeting. That is, motions put to the shareholders in general meeting – in relation to matters like election of directors – will normally be passed or rejected according to how the 20 per cent plus shareholder votes.

Data on takeover activity in New Zealand up until 1993 may be found in John Farrar, ed., Takeovers (Auckland: OUP, 1993). Today, data on takeover activity may be found in Code Word, the newsletter of the Takeovers Panel or on the website of the Takeovers Panel <www.takeovers.govt.nz>.

The purposes of the takeover provisions appearing in the Takeovers Code are set out in the Takeovers Act 1993. The Takeovers Act 1993 created a Takeovers Panel. The Takeovers Panel has two main functions. The first was to prepare a takeovers code that complied with
the objectives set out in the Act. The second function was to enforce the resultant code. Thus, the principal purposes of the Takeovers Code appear in sections 20, 21 and 24 of the Takeovers Act 1993. These sections were not amended by the Takeovers Amendment Act 2006.

Section 20 states that, in formulating a takeovers code, the Panel shall consider the following objectives:

- Encouraging the efficient allocation of resources;
- Encouraging competition for the control of specified companies;
- Assisting in ensuring that holders of securities in a takeover are treated fairly;
- Promoting the international competitiveness of New Zealand’s capital markets;
- Recognising that the holders of securities must ultimately decide for themselves the merits of a takeover offer;
- Maintaining a proper relation between the costs of compliance with the code and the benefits resulting from it.

Section 21 specifies certain matters to be considered by the Panel in formulating a code such as whether advance notice and publicity should be given.

Section 24 states that when formulating a code, the Panel should have regard, to any principles applying to the co-ordination of business law between Australia and New Zealand set out in any agreement or memorandum of understanding between the Governments of Australia and New Zealand. The latest version of such agreement is contained in the Memorandum of Understanding between the Governments of Australia and New Zealand on the Harmonisation of Business Law signed on 22 February 2006.

### 7.2 Overview of the Takeovers Code
There is a general prohibition (the “fundamental rule”) contained in Rule 6 of the Takeovers Code on acquiring control of more than 20 per cent of the voting rights in a code company except as set out in the code.

Exceptions to the “fundamental rule” contained in Rule 6 are contained in Rule 7. Rule 7 states that a person may increase a holding of voting rights beyond the 20 per cent threshold in one of the following ways:

- Acquisition under a full offer;
- Acquisition under a partial offer;
- Acquisition approved by resolution of shareholders of the target company;
- Acquisitions of less than 5 per cent per year by a holder of between 50 and 90 per cent of the voting rights; or
- Acquisitions by a person holding at least 90 per cent of voting rights in a code company.

Section 45 of the Takeovers Act 1993 also permits the Takeovers Panel to grant exemptions from the requirements of the code.

The general prohibition or “fundamental rule” is contained in Rule 6 of the Takeovers Code. This rule prohibits a person holding or controlling more than 20 per cent of the voting rights in a code company except as prescribed in the code.

The general prohibition contained in Rule 6 applies to companies that are:

- Party to a listing agreement with a registered exchange and have securities that confer voting rights quoted on the registered exchange’s market;
- Were a party to a listing agreement with a registered exchange in the 12 months before or after the event referred to in the code; or
- Have 50 or more shareholders

These companies are code companies and cannot contract out of the code.
The term “control” is defined in Rule 3 (1) of the Takeovers Code to mean, in relation to a voting right, as “having, directly or indirectly, effective control of the voting right” and the term “controller” has a corresponding meaning. Rule 6 (2) provides that a person will have control if that person acted jointly or in concert with other persons or if a person joins another person or group of persons controlling voting rights as an “associate”, or if a person controls voting rights together with “associates”.

The term “associate” is defined in Rule 4. A person is an associate of another person if:

- The persons are acting jointly or in concert; or
- The first person acts, or is accustomed to act, in accordance with the wishes of the other person; or
- The persons are related companies; or
- The persons have a business relationship, personal relationship, or an ownership relationship such that they should, under the circumstances, be regarded as associates; or
- The first person is an associate of an associate.

However, directors are not associates of companies merely by reason of their status as director.

The provisions of the Takeovers Code could be easily avoided if they did not include the concepts of associate and control. Consider the following example:

Five people each own 10 per cent of the shares of company A. They each agree to vote the same way to make sure they control who will be directors of Company A. The five shareholders therefore have control of Company A. They are each associates of each other. This means that each of the five shareholders has “voting rights” of 50 per cent. Assume that they agree that one of them can buy the shares of the other four. The agreement means there is a breach of the general prohibition or fundamental rule in Rule 6.

The Takeovers Code does not contain any provisions regarding breach of Rule 6. However, Part III of the Takeovers Act 1993 empowers the Panel to act in relation to compliance with
the code. Under sections 32 and 33 of the Takeovers Act 1933, the Panel may issue a “temporary restraining order” to prevent a takeover from proceeding.

The High Court also has powers under Part III, Subpart 2 of the Takeovers Act 1993. For example, it can order disposal or forfeiture of shares and payment of compensation.

As mentioned, the main exemptions to the fundamental rule contained in Rule 6 are acquisitions resulting from an offer to shareholders under a formal “takeover bid”. Offers may be full or partial and may be made on-market or off-market.

A full offer is an offer for all the voting and non-voting securities of the target company. If the target company has different classes of securities, the full offer must be fair and reasonable as between different classes.

A partial offer (for less than 100 percent) is permitted but must be extended to all holders of voting securities. The partial offer must be for a specified percentage of each holder’s voting securities. If there is more than one class of voting security, the partial offer must extend to each class. If the offeror’s existing holding is 50 per cent or less, the offer must be for securities which will result in the offeror holding or controlling more than 50 per cent of the voting rights. A partial offer can be made for a lesser percentage if approval is obtained from the target company.

An off-market bid may be made for shares in listed and unlisted companies. A market bid can only be made for shares in listed companies because the offers under a market bid are made through the NZX’s trading system.

An off-market bid will normally be successful only if the bidder offers to buy the shares for a price significantly above the market price of the shares just before the bid is announced. That is, the target company’s shareholders must normally be offered a “premium”.

There are detailed requirements for a takeover bid, including:

**Offer procedure.** Part 6 of the Takeovers Code (Rules 41-49) sets out a procedure for full and partial takeover offers. A takeover notice must be sent to the target together with the information specified in Schedule 1. If listed, the target company has to notify the NZX. If
unlisted, the target company must inform offeree shareholders. The target company is then required to provide the offeror a copy of its securities register (a document on which the names of its shareholders appear). A written offer is then sent to all offerees. The offer must be open for between 30 and 90 days although a full offer can be extended by up to 60 days.

**Equal treatment of shareholders.** With both full and partial offers, the same terms (including price) must be offered to all security holders within a class of securities. Where there are different classes of securities, an independent adviser must certify that the price is fair and reasonable as between classes.

**Price.** There is no restriction on the price that can be offered except that the price must be fair and reasonable between different classes of securities.

**Minimum acceptance condition.** Where the bidder does not hold or control more than 50 per cent, the offer must be conditional on receiving acceptances which will bring the offeror’s total holding above the 50 per cent threshold, unless it is a partial offer and shareholder approval for a lesser percentage is obtained.

The Takeovers Code restricts defensive tactics by the target company’s directors that might “frustrate an offer” except in limited circumstances.

A shareholder who receives an offer under a takeover bid has the choice of accepting the offer (and selling their shares to the bidder) or rejecting the offer (and keeping their shares). In limited circumstances, a shareholder who has rejected the offer can later be forced to sell their shares to the bidder.

Under Part 7 of the Takeovers Code, a takeover bidder has the power to compulsorily acquire shares where, some time up to the end of the offer period the bidder controls 90 per cent or more of the voting rights in the target company. Such a person is called a “dominant owner” and has the right to acquire all the remaining securities of the company.

Part 8 of the Takeovers Code was introduced by the Takeovers Amendment Act 2006. It includes a new Rule 64 which contains a prohibition on misleading or deceptive conduct.
Substantial shareholder disclosure

In most major markets around the world, there is a regulatory obligation on large shareholders in listed companies to disclose their identity and details of their holding. This is regarded as an important element of a liquid securities market. The disclosure threshold varies from country to country – for example, it is 3 per cent in the United Kingdom and 5 per cent in the United States and Australia.

This area of law was amended by the Securities Markets Amendment Act 2006. A new Part 2, Subpart 3 was introduced and came into force on 29 February 2008. The purpose of this subpart is stated in section 20. It states that the purpose of the subpart is, “to promote an informed market, and to deter insider conduct, market manipulation, and secret dealings in potential takeover bids, by ensuring that participants in New Zealand's securities market have access to information concerning the identity and trading activities of persons who are or may at any time be, entitled to control or influence the exercise of significant voting rights in a public issuer”.

Under Part 2, Subpart 3 of the Securities Markets Act 1988, a person who is a “substantial security holder” (generally speaking a 5 per cent or greater shareholding) in a listed New Zealand company must disclose certain information to the company and to the NZX. The main features of the New Zealand regime are:

- A “substantial security holder” is defined in section 21 in relation to a public issuer as a person who has a “substantial holding” in a public issuer. A person has a substantial holding in a public issuer for the purposes of the Act if the person has a relevant interest in listed securities that comprise five per cent or more of a class of listed voting securities of the public issuer. The term “relevant interest” is very widely defined in section 5, 5A and 5B so as to catch any type of legal or beneficial ownership as well as, for example, the power to control the exercise of any voting right. A person who has power over voting rights attached to shares, or over disposal of the shares, has a relevant interest in the shares regardless of whether or not the person is the registered owner of the shares. Once a person has a substantial holding in a public issuer, disclosure must be made to the public issuer and the registered exchange: see sections 22, 26 and 27.
• Once a person is above the 5 per cent threshold, the person must disclose again if their holding goes up or down by a whole percentage point or more: section 23.

• The information that must be disclosed to the company and the stock exchange is described in section 26 and includes details of the nature of the relevant interest.

• Disclosure must be made as soon as the person knows or ought to know that the person is a substantial security holder in the public issuer: section 22 (2).

Sections 34 and 35 of the SMA give the NZSC and listed companies the power to send out notices (called “tracing notices”) requiring a member of a listed company to provide details about their own relevant interest in the company’s shares and the relevant interest of other persons in those shares. This enables a listed company to discover who controls the voting rights attached to shares registered in the name of nominees. It also assists in the proper functioning of the takeover provisions. For example, somebody may be secretly assembling a stake of just below 5 per cent in a listed company, through several nominees, before making a takeover bid. As their stake is below 5 per cent, the substantial security holder provisions do not apply.

The other main features of the tracing regime are:

• Where the public issuer requires a person who has a relevant interest to disclose information, that person must supply that information immediately and in writing: section 35 (2).

• Failure to comply with the substantial holding disclosure obligation is an offence: section 35BA.

• The NZSC may make a disclosure order if it is satisfied that the person has contravened a substantial holding disclosure obligation: section 42B. Failure to comply with such an order is an offence: section 42J.

• The civil remedy provisions of the SMA are available for breach of the substantial holding disclosure obligation: section 42S.
7.3 **Companies Act 1993**

This Act is not directed at takeovers but some provisions may be relevant in a takeover context. These include:

- directors’ duties to act in good faith and in the best interests of the company.
- directors’ duty to disclose personal interests in transactions.
- directors’ duty not to disclose confidential information.
- directors’ duty to disclose dealings in company’s securities and to ensure that the other party to the dealing receives fair value.
- safeguards in the Act to protect shareholders against misuse of the power to have a company acquire its own shares or financially assist in the purchase of its own shares.
- requirement that disposal or acquisition of assets worth more than 50 per cent of the company’s value demands approval by special resolution of shareholders.
- minority shareholder buy-out rights.
- general protection against oppression, unfair prejudice and unfair discrimination.

There is a good discussion of these duties in J. Farrar, *Corporate Governance in Australia and New Zealand, 2nd ed.* (2005) and in Austin, Ford and Ramsay, *Company Directors* (2005).

7.5 **NZX Listing Rules**

The latest version of the NZX Listing Rules is downloadable from the NZX website. The NZX made amendments to the NZSX Listing Rules effective 1 July 2006. Section 4 of the NZX Listing Rules governs takeovers. Where a company is a code company as defined, then LR 4.3.1 states that the issuer’s constitution must contain Notice and Pause provisions, Enforcement provisions and Compulsory Acquisition provisions.

**Notice and Pause Provisions**

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The fundamental rule contained in Section 4 is that “notice and pause” provisions will apply to all “restricted transfers”. These are changes of ownership or control of securities of a class carrying more than 20 per cent of the votes in that class, or more than 5 per cent per annum once that 20 per cent threshold has been reached. Every issuer must have notice and pause provisions in its constitution: LR 4.3.1. These provisions may be modified so that they apply only where the bidder or purchaser is an insider: LR 4.4.2. This will provide a more liberal takeover regime than the standard Notice and Pause provisions. The provisions require offerors to give periods of public notice before the transfer can take place. The notice periods are:

- one business day where the transfer is effected solely through the NZX
- three business days for off-market transactions
- fifteen business days where any offeree is an insider.

**Minority Veto Provisions**

These provisions are optional and are an alternative to the standard notice and pause provisions. A listed company may amend its constitution by adopting the restrictive “minority veto” provisions pursuant to LR 4.4.1 through LR 4.6. These require that restricted transfers be made only by offers to all holders of securities of the class in question or only by on-market transactions except where approved by a resolution passed by a simple majority of each “relevant group”. These provisions also require directors to obtain an independent report on the proposal. Very few companies listed on the NZX have chosen the restrictive minority veto provision.

**Enforcement Provisions**

NZX LR 4.7 makes provision for enforcement procedures where a default has occurred as defined in LR 4.1.1.

**Compulsory Acquisition Provisions**

LR 4.8 contains provisions dealing with compulsory acquisitions in takeover situations. These are intended to take the place of s. 208 of the Companies Act 1955 (which section was not re-enacted in the Companies Act, 1993). The provisions come into effect when a majority holder
acquires 90 per cent or more of a class of securities of the issuer. In that event, within 20 business days, the majority holder must notify the remaining security holders of the acquisition and either express an intention to acquire all remaining securities in the affected class or inform the remaining holders that they may require the majority holder to purchase their securities.

**Restrictions and Defensive Measures**

LR 4.2 prohibits certain provisions which might be used as takeover defences.

### 7.7 Fair Trading Act 1986

Section 44E of Takeovers Act 1993 states that the Fair Trading Act 1986 does not apply to conduct in relation to any transaction or event regulated by the Takeovers Code. This section of the Takeovers Act 1993 came into effect on 29 February 2008.

### 7.8 Commerce Act 1986

Section 47 of the Commerce Act 1986 prohibits the assets of the business or shares if the acquisition would have, or would be likely to have, the effect of substantially lessening competition in the market.

### 7.9 Overseas Investment Act 2005

Where a takeover offer is made by an overseas person involving “significant business assets” with a consideration in excess of NZD100 million, the Overseas Investment Act 2005 requires that the offeror obtain the consent of the Treasurer: section 13 (1) (c ). The criteria for consent are contained in section 14 and 18 of the Overseas Investment Act 2005.

### 7.10 Securities Act 1978

The review function of the NZSC under s. 10 of the Act is very wide. In *City Realities Ltd v. The NZSC* [1982] 1 NZLR 74 (CA), it was said that the NZSC has the power to investigate in depth a particular company takeover or attempted takeover and that such power may be exercised while the attempt is in progress. The NZSC also has the power to compel persons to give evidence and produce documents. Whilst the NZSC has no power to make binding decisions, an investigation by the NZSC could provide a serious impediment to a takeover proposal.
7.11 Amalgamations

The procedure for amalgamations is contained in Part XIII of the Companies Act 1993. The procedure allows two or more companies to amalgamate without having to seek Court approval. An amalgamation is now made effective by the issue of a certificate of amalgamation by the Registrar of Companies. The amalgamation procedure under the Companies Act 1993 was reviewed by the Court of Appeal in *Carter Holt Harvey v McKernan* [1998] 3 NZLR 403. See also *Elders New Zealand Limited v PGG Wrightson* [2007 1 NZLR 710 (High Court).

8. Accounting and Auditing

8.1 Companies Act 1993

The statutory obligation to keep accounting records is found in s. 194 of the Companies Act 1993. Section 194 requires that the board of a company must cause accounting records to be kept that:

- correctly record and explain the transactions of the company
- enable the financial position of the company too be determined at any time with reasonable accuracy
- enable the directors to ensure that the financial statements of the company comply with section 10 of the FRA
- are capable of being readily and properly audited.

The responsibility for ensuring that proper accounting records are kept rests with the board of directors and failure to comply with this provision renders the directors personally liable to a pecuniary penalty.

8.2 Financial Reporting Act 1993
The statutory obligations with regard to financial statements are contained in the Financial Reporting Act 1993. All companies must prepare financial statements. The FRA distinguishes three basic types of companies: issuers; exempt companies and other companies. An “issuer” is defined in s. 4 of the FRA as including those companies which are party to a listing agreement with a stock exchange in New Zealand and who have issued securities which are quoted on such an exchange.

The main accounting requirements imposed by the FRA are as follows:

**Balance date:** Every company is required to have a balance date which is the financial year end. This is either 31 March or any other date adopted by the directors.

**Financial statements:** The main financial statements required by the FRA are:

- a balance sheet as at the balance date
- a profit and loss statement relating to the accounting period ending at the balance date
- a statement of cash flows for the period ending at the balance date where required by an applicable financial reporting standard.

**Group financial statements:** These consist of consolidated balance sheets, profit and loss statements and a cash flow statement for an entire group of companies.

The financial statements of every company must be completed within 5 months after the balance date. Financial statements must comply with generally accepted accounting standards as defined in s. 3 FRA. Issuers must deliver copies of financial statements to the Registrar of Companies for registration.

### 8.3 Audit

The directors of an issuer are required to ensure that the financial statements and group financial statements are audited by a qualified auditor: s. 15 FRA. After auditing the financial statements of every company, the directors must provide a written report containing the following:

1. A statement that, so far as they are aware, the financial statements comply with the requirements of the FRA.
2. A statement that, so far as they are aware, the consolidated financial statements of the group comply with the requirements of the FRA.

statements, the auditor is required to prepare a report which must contain the following information:

- the work done by the auditor
- the scope and limitations of the audit
- any relationship or interest in the company which the auditor has
- whether or information and explanations required have been provided
- whether, in the auditor’s opinion, proper accounting records have been kept
- whether the financial statements comply with the FRA
- whether the financial statements give a true and fair view of the company’s affairs and, if not, the respects in which they fail to do so.

If the auditor’s report shows that the FRA has not been complied with, the auditor must send a copy of the report (together with a copy of the relevant financial statements), to the Registrar of Companies. In turn, the Registrar is required to send copies to the NZSC and the Accounting Standards Review Board.

The auditor’s report must be distributed as part of the annual report by the directors.

9. International Securities Transactions

Recognition of foreign issuers is a matter which the NZSC has generally dealt with on a case-by-case basis. The NZSC may give an exemption from the requirements of the New Zealand legislation where prospectuses have been issued overseas which generally conform to the requirements of New Zealand law and are made available to investors in New Zealand. Thus, an exemption might be granted in a specific case and an exemption notice gazetted pursuant to s. 5(5) of the Act in respect of an offshore issuer. By way of example, in 1999 the NZSC promulgated The Securities Act (Great Britain Collective Investment Schemes) Exemption Notice that enabled British fund managers to market their investment products in New Zealand.9

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9 See G. Sheeran, “Tax relief in sight for funds” Sunday Star-Times, August 13 2000, E1 (British based funds do not pay tax on capital gains but New Zealand fund managers pay tax on earnings in the form of...
There are four exemption notices, however, which have a more immediate application. Two of these relate to Australian issuers; two relate to overseas companies and overseas listed issuers.

In the case of Australia, New Zealand and Australia are party to a regional Free Trade Agreement (RFTA) the Closer Economic Relations Treaty (CER) which took effect on 1 January 1983. The CER Treaty is simultaneously the central enabling document for the RFTA between New Zealand and Australia and the umbrella agreement for a range of downstream agreements and other documents that better implement the CER Treaty. Collectively, these agreements and documents are known as the CER Agreement. One of the downstream agreements is the MOU on Coordination of Business Law signed on 31 August 2000 (this MOU was updated on 22 February 2006).\(^\text{10}\) As a consequence of this MOU, the Australian Treasury and the Ministry of Economic Development in New Zealand issued a discussion document entitled, *Trans-Tasman Mutual Recognition of Offers of Securities and Managed Investment Scheme Interests* (May 2004). This document proposed a formal mutual recognition scheme between Australia and New Zealand whereby offers of securities and managed investment schemes will be subject to a mutual recognition regime.\(^\text{11}\) On 22 February 2006, a Treaty between the Government of Australia and the Government of New Zealand in Relation to Mutual Recognition of Securities Offerings was signed.\(^\text{12}\) In June 2008, implementing regulations were made: see Securities (Mutual Recognition of Securities Offerings – Australia) Regulations 2008 and NZSC, *Offering securities in New Zealand and Australia under mutual recognition* (2008) available at the NZSC website.

### 9.1 The Securities Act (Australian Issuers) Exemption Notice 2002

In this notice, the term “Australian issuer” means a company incorporated in Australia, or a company incorporated in a country other than Australia and admitted to (or having made application to be admitted to), the official list of the Australian Stock Exchange (“ASX”). The term “Australian prospectus” means a document, *inter alia*, that contains an offer of securities by an Australian issuer, is identical to a prospectus registered in Australia, contains a dividends and interest, as well as capital gains when shares are sold. British-based funds are hence enjoying an advantage over local funds).

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statement that any documents required to be inspected in Australia can be inspected at the office of the Registrar of Companies (ROC) in Wellington and which has been deposited with the Registrar together with supporting documentation. (In practice, the initial lodgement is made in to the ROC in Auckland.) Subject to certain conditions, such an Australian prospectus is exempt from compliance with the provisions of ss. 33(2), 37, 37A (2), 38A and 51-54 of the Act. Note that this Exemption Notice appears to have been overtaken by the mutual recognition regime described above.

9.2 The Securities Act (Australian Registered Managed Investment Schemes) Exemption Notice 2003

This notice operates in a similar fashion to the Australian Issuers Notice discussed above.

9.3 The Securities Act (Overseas Companies) Exemption Notice 2002

This notice is designed to cover rights issues and takeovers of other overseas companies by an overseas company. The term “overseas company” means a company incorporated outside of New Zealand. The term “specified exchange” means a stock exchange in the United Kingdom, Australia, Canada, USA or Hong Kong. In general, such companies are exempt from parts of Part II of the Act and Regulations in respect of certain offers and allotments of securities where (a) the securities are quoted on a specified exchange and the issuer has complied with the requisite requirements of the specified exchange, and, (b) the only members of the public to whom the securities are offered in New Zealand are persons who already hold securities of which the overseas company is the issuer.

9.4 The Securities Act (Overseas Listed Issuers) Exemption Notice 2002

This notice came into force in 2002. It does not apply in relation to offers to which the exemption notices discussed at sections 9.1 and 9.3 above apply. The notice allows companies listed on the London Stock Exchange (LSE), the NASDAQ National Market and the New York Stock Exchange (NYSE) to use their overseas prospectuses to make offers of securities in New Zealand subject to the deposit of the requisite documentation with the Registrar of Companies in Wellington.

In a Media Release dated 9 October, 1995, the NZSC stated that the general purpose of the 1995 version of this exemption was to provide increased opportunity for New Zealand investors to participate in overseas issues while substantially lowering the compliance costs and transaction costs for overseas issuers. The notice was viewed as a base from which the NZSC might seek to negotiate the cooperation of overseas jurisdictions to reciprocal arrangements for New Zealand issuers.

9.5 NZX Listing Rules

LR 5.1.1(b) states that any person may apply to the NZX for listing with a “Recognised Stock Exchange” as the “Home Exchange” if that person is domiciled or incorporated outside New Zealand and listed on a “Recognised Stock Exchange” (an “Overseas Listed Issuer”). LR 5.1.1(c) makes provision for application for listing as a “Dual Listed Issuer”. The terms “Dual Listed Issuer”, “Home Exchange” and “Recognised Stock Exchange” are defined in Section 1 of the Listing Rules. A “Dual Listed Issuer” means an issuer listed on the ASX and the NZX. The key term is “Recognised Stock Exchange” which is defined as a stock exchange approved by the NZX from time to time as enforcing rules sufficiently similar to those of the NZX as to justify classification as a Recognised Stock Exchange for the purposes of the Listing Rules. Full members of the World Federation of Exchanges (WFE) are recognised for this purpose. LR 5.1.2 specifies the information required to be submitted for listing generally. An “Overseas Listed Issuer” is deemed to have complied with the LR 5.1.2 so long as it remains listed on its “Home Exchange”: LR 5.1.6. The intention of Rules 5.1.6 and 5.1.7 (Rules applicable to Overseas Listed Issuers), is that a company or other entity which is listed on a recognised overseas stock exchange (and accepted by the NZX for listing on the NZX as well), is not required to comply with the Listing Rules so long as that company or other entity complies with the rules of the overseas stock exchange. The NZX may however in its discretion at any time require compliance with any provision of the Listing Rules. As a general rule, the NZX will cancel the listing of an Overseas Listed Issuer if the listing of that issuer is cancelled on its Home Exchange. Overseas Listed Issuers must appoint a natural person resident in New Zealand with whom the NZX may communicate and such person must be authorised on behalf of the issuer to accept service of notices or legal proceedings from the NZX.

9.6 International Organization of Securities Commissions (IOSCO)
The NZSC is a member of IOSCO and one of the subscribers to the Rio Declaration of 1986 which calls on signatories to provide assistance on a reciprocal basis in the gathering of information related to market oversight and protection of investors against fraudulent securities transactions. In 2004, the NZSC was accepted as a signatory to the IOSCO multilateral MOU which enables cooperation between signatories to combat international fraud and to effectively enforce securities law. In May 2004, NZSC Chairman, Jane Diplock, was elected to chair the Executive Committee of IOSCO.

The NZSC has signed bilateral MOUs with the China Securities Regulatory Commission, the Indonesian Capital Markets Supervisory Agency, and, the Malaysian Securities Commission. It also has MOUs with ASIC, the USA CFTC, the Hong Kong SFC, the PNG Securities Commission and the SEC of Sri Lanka. The NZSC has an exchange of letters with the USA SEC.

A recent statement of the NZSC’s position as regards IOSCO and other international involvement can be found in the NZSC’s *Annual Report* for 2008.13

### 10. Investment Companies and Investment Advisers

Company legislation in New Zealand does not recognise a distinct category of “investment company”. The provisions of the Unit Trusts Act 1960 cover any scheme or arrangement that has the effect of providing facilities for the participation, as beneficiaries under a trust, by members of the public in income and gains arising from money, investments and other property subject to the trust. From 1 October 1997, offers of interests in New Zealand unit trusts were subject to the provisions of the 78 Act as to the disclosure of information.

#### 10.1 Investment Advisers and Brokers

The Investment Adviser (Disclosure) Act 1996 has been repealed and the activities of investment advisers and brokers are now governed by Part 4 of the SMA. Section 2 of the SMA defines the various terms. An investment adviser is a person who, in the course of the

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person’s business or employment gives investment advice. An investment broker is a person who, in the course of the personal and business or employment, receives investment money or investment property. A person can be an investment adviser and an investment broker.

The SMA requires an “investment adviser” to disclose information in accordance with sections 41B to 41F before giving investment advice to a member of the public. The types of information that must be disclosed are as follows:

- experience, qualifications and professional standing;
- criminal convictions;
- fees;
- other interests and relationships;
- details of the securities about which advice is given;

The SMA requires an “investment broker” to disclose information in accordance with sections 41H and 41I before receiving investment money or investment property from a member of the public. The information that must be disclosed is as follows:

- criminal convictions, bankruptcy, banning orders etc., and,
- procedures for dealing with investment money or investment property.

Disclosure must be made by means of a written disclosure statement: section 41J. Failure to comply with the disclosure obligation is an offence: section 41P. Sections 41Q and 41R create offences relating to deceptive, misleading, or confusing disclosure or advertisements.

The various disclosure obligations have extraterritorial effect: section 41U. There is no contracting out: section 41V.

Matters of enforcement and civil remedies are dealt with in Part Five of the SMA.
11. Broker-Dealers or Entities Authorized to Trade in Securities

Sharebroking activities in New Zealand are governed by the Sharebrokers Act 1908 as amended. Section 2 of the Act defines a “sharebroker” as any person, firm, or company who, for remuneration, sells or purchases shares for or on behalf of or as agent for any other person but excludes banks selling or purchasing shares for their customers in the ordinary course of their business and members of an authorised futures exchange where such member sells or purchases share options. Pursuant to s. 3 of the Act, sharebrokers must hold a sharebroker’s licence. Licences are issued by District Courts.

Only members of authorised futures exchanges may carry on the business of a futures dealer: see section 38 of the SMA.

12. Civil and Criminal Liability

12.1 Civil Liability

12.1.1 Liability for Misstatements

Civil liability is imposed for misstatements in advertisements or registered prospectuses by s. 56 of the Act. This section was discussed above. Civil liability is also imposed for misstatements by experts: s. 57.

12.1.2 General Prohibition on Indemnities or Insurance

Except as provided for in section 61B, an issuer must not indemnify, or directly or indirectly effect insurance for a director, employee or auditor in respect of liability or costs incurred for any negligence, default, breach of duty, or breach of trust: section 61. An indemnity given in breach of this section is void: section 61 (2) of the 78 Act.

There are permitted exceptions to the general rule and these can be found in sections 61A (permitted indemnities) and 61B (permitted insurance) of the 78 Act.

12.1.3 Power of Court to Grant Relief
Under s. 63 of the Act, a court may grant relief from liability for negligence, default, breach of duty, or breach of trust in connection with the following:

- an offer to the public or allotment of securities;
- distribution of a registered prospectus or advertisement;
- the management of securities offered to the public, or
- any matter related thereto.

Relief may be granted if it appears that the person acted honestly and reasonably and ought fairly be excused.

12.1.4 Civil Liability for Insider Trading

Civil liability for insider trading is discussed above.

12.1.5 Civil Liability for Breach of Continuous Disclosure Provisions

Part 5, Subpart 3 of the SMA provides a civil remedy for breach of the continuous disclosure provisions: see section 42S (d). An “aggrieved person” may seek a compensatory order: section 42ZA.

12.1.6 Civil Liability of Substantial Security Holder for Failure to Notify Relevant Interest

This area of law was amended by the Securities Markets Amendment Act 2006. To briefly reiterate: a new Part 2, Subpart 3 was introduced and came into force on 29 February 2008. The purpose of this subpart is stated in section 20. It states that the purpose of the subpart is, “to promote an informed market, and to deter insider conduct, market manipulation, and secret dealings in potential takeover bids, by ensuring that participants in New Zealand's securities market have access to information concerning the identity and trading activities of persons who are or may at any time be, entitled to control or influence the exercise of significant voting rights in a public issuer”.

Under Part 2, Subpart 3 of the Securities Markets Act 1988, a person who is a “substantial security holder” (generally speaking a 5 per cent or greater shareholding) in a listed New
Zealand company must disclose certain information to the company and to the NZX. The main features of the New Zealand regime are:

- A “substantial security holder” is defined in section 21 in relation to a public issuer as a person who has a “substantial holding” in a public issuer. A person has a substantial holding in a public issuer for the purposes of the Act if the person has a relevant interest in listed securities that comprise five per cent or more of a class of listed voting securities of the public issuer. The term “relevant interest” is very widely defined in section 5, 5A and 5B so as to catch any type of legal or beneficial ownership as well as, for example, the power to control the exercise of any voting right. A person who has power over voting rights attached to shares, or over disposal of the shares, has a relevant interest in the shares regardless of whether or not the person is the registered owner of the shares. Once a person has a substantial holding in a public issuer, disclosure must be made to the public issuer and the registered exchange: see sections 22, 26 and 27.

- Once a person is above the 5 per cent threshold, the person must disclose again if their holding goes up or down by a whole percentage point or more: section 23.

- The information that must be disclosed to the company and the stock exchange is described in section 26 and includes details of the nature of the relevant interest.

- Disclosure must be made as soon as the person knows or ought to know that the person is a substantial security holder in the public issuer: section 22 (2).

Sections 34 and 35 of the SMA give the NZSC and listed companies the power to send out notices (called “tracing notices”) requiring a member of a listed company to provide details about their own relevant interest in the company’s shares and the relevant interest of other persons in those shares. This enables a listed company to discover who controls the voting rights attached to shares registered in the name of nominees. It also assists in the proper functioning of the takeover provisions. For example, somebody may be secretly assembling a stake of just below 5 per cent in a listed company, through several nominees, before making a takeover bid. As their stake is below 5 per cent, the substantial security holder provisions do not apply.

The other main features of the tracing regime are:
• Where the public issuer requires a person who has a relevant interest to disclose information, that person must supply that information immediately and in writing: section 35 (2).

• Failure to comply with the substantial holding disclosure obligation is an offence: section 35BA.

• The NZSC may make a disclosure order if it is satisfied that the person has contravened a substantial holding disclosure obligation: section 42B. Failure to comply with such an order is an offence: section 42J.

• The civil remedy provisions of the SMA are available for breach of the substantial holding disclosure obligation: section 42S.

The dominant purpose of the law on substantial security holder disclosure is to further a key goal of securities regulation - timely and fair information disclosure to all investors in order to ensure market integrity and address the problem of “information asymmetry”: see section 20 for a statement of the purpose of the subpart. Information asymmetry in securities markets refers to the situation where select market participants – usually by virtue of their relationship to a company - possess significant information that is not available to the market at large. The presence of information asymmetries has significant implications for market efficiency. A central tenet of the Efficient Capital Market Hypothesis (ECMH) is that an efficient market will accurately reflect all publicly available information about securities in the price of those securities. Where information asymmetries exist, a privileged few may exploit significant information (not yet available to the market as a whole) for personal gain. Ideally, however, all participants in a public securities market should have equal access to information relevant to market decisions: the so-called “fairness” rationale. In order to achieve fair disclosure of significant information such information must be in the public domain. The NZSC has stated:

A marketplace is full of rumours, and nothing will change it. It is the testing of judgment against events that provides much of the interest in share market operations. Yet the market must operate upon the basis of information, and there is no doubt that there is a core of information about any security that ought to be public knowledge.14
The identity of substantial security holders may be a significant factor in the price and value of listed securities. Substantial security holders are in a position to exercise voting or other control rights and their presence or absence on a share register will affect the investment decisions of investors. The activities of controlling shareholders can precipitate major market activity. If substantial security holder transactions take place without the disclosure of that information to the market, market efficiency is impaired. Disclosure enables the market to respond rapidly to new information thereby ameliorating the price effect of significant information.

Substantial security holder disclosure is regarded as an important element of a liquid securities market and is a requirement in most major international markets. The disclosure threshold varies from country to country – for example, it is 3 per cent in the United Kingdom and 5 per cent in the United States and Australia. The Australian provisions are very similar to the New Zealand regime. Since New Zealand and Australia seek business law co-ordination and because New Zealand is actively following Australian law in the area of securities regulation it is useful to outline the cognate Australian provisions.

12.1.6.1 The Cognate Australian Provisions

In Australia, substantial security holder disclosure is regulated by Chapter 6C of Corporations Act 2001 entitled “Information about Ownership of Listed Companies and Managed Investment Schemes” which incorporates amendments from the latest round of CLERP reforms. The recently revised Australian Securities and Investment Commission (ASIC) policy statement on substantial holdings, Policy Statement 159: Takeovers, Compulsory Acquisitions and Substantial Holding Notices, discusses these changes and provides additional explanation of the key prohibition contained in section 671B using recent case law. The general purpose of substantial security holder disclosure in Australia is stated as

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15 Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004 (CLERP 9). The CLERP 9 changes bolstered tracing procedures under Part 6C.2 of the Corporations Act, 2001 by introducing a register of information about relevant interest in a listed company or listed management scheme to be kept by that entity: s 672DA. The details to be included in the register, its location, availability and duplication procedures are dealt with in s 672A.
17 The revised policy was released on 18 November 2004, and now incorporates the substantial holdings policy. The policy replaces Policy Statement 110: Substantial Shareholding Notices; Interim Policy Statement
being “to maintain an informed market in quoted securities”. Australian courts have affirmed this rationale as the primary purpose of the law: Re North Broken Hill Holdings Ltd (1986) 10 ACLR 270 at 282, 283; Australian Securities Commission v. Bank Leumi Le-Israel (Switzerland) (1996) 69 FCR 531; New Ashwick Pty Ltd v Westfarmers Ltd (2000) 35 ACSR 263. The following passage from the judgment in Brunswick NL v Blossomtree Pty Ltd states the rationale for substantial security holder disclosure in Australian law:

It is in the interests of shareholders, current as well as past, to have information as to the real owners of shares which may influence the future of the company and their future as shareholders and which indeed might impact upon the management and control of the company. It is also in the market interest to know those matters and whether or not any such shares were acquired illegally.

More specifically, the disclosure requirements aim to facilitate access to information regarding:

(a) who the controllers of substantial blocks are;
(b) who the associates of substantial holders are;
(c) details of any consideration or special benefits a person received for disposing of their relevant interest; and
(d) details of any agreements or special condition or restrictions that may affect the disposal of shares or the way in which they are voted.

Pursuant to section 671B(1) of the Corporations Act, a person must provide a substantial holding notice if they:

(a) begin to have or cease to have a substantial holding in the body; or
(b) have a substantial holding in the body and there is a movement of at least 1 per cent in their holding; or
(c) make a takeover bid for securities of the company or scheme.

18 Policy Statement 159.271.
20 Policy Statement 159.269.
A person is deemed to have a “substantial holding” if they or their associates have a relevant interest in 5 per cent or more of the voting shares of the body: s 9. A person has a relevant interest in securities if they:

(a) are the holder of the securities; or

(b) have power to exercise, or control the exercise of, a right to vote attached to the securities; or

(c) have power to dispose of, or control the exercise of a power to dispose of, the securities: s 608.

Note here that the terms “power” or “control” catch the use of a trust, an agreement or a practice: s 608 (2). For our purposes, the relevance of the term “practice” in the Australian law is that the first version of the Securities Legislation Bill 2004 in New Zealand proposed the introduction of the new section 5A which contained the same term - presumably to negate the effect of the decision of the Court of Appeal in the *Ithaca* case. However, the version of the Bill reported back from the Commerce Committee recommended that proposed section 5A be deleted and the term, “practice” does not appear in the new section 5A.

The substantial shareholder must disclose details of their relevant interest and any relevant agreement and the nature of any association and the associate’s interest: s 671B (3). This requirement is predicated on full disclosure rather than minimum or technical disclosure. For example, a party must disclose movements in each direction and not merely net movements in substantial holdings.21 The relevant transaction should be described in clear commercial and legal terms22 such that the nature of the substantial holding or the change in the holding is apparent to other investors.23

Disclosure must be made within two business days (or by 9.30 a.m. next trading day during a takeover bid) after the party has become aware of the information; s 671B (6). This deadline is designed “to compel, in fast-moving markets, the immediate disclosure of the identity of the persons who become substantial security holders”.24 Disclosure must be made “whether or not they have completed a larger investment move or unwound their investment position

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21 Policy Statement 159.263.
22 Policy Statement 159.262.
within that time”, notwithstanding that the situation may have changed by the time disclosure is due.25

The substantial security holder disclosure requirements have not been extensively litigated in Australia. This is noteworthy given the number of cases which the cognate New Zealand provisions have spawned. A possible explanation is the Australian Investment and Securities Commission’s (ASIC) propensity for pursuing actions under s 606 appearing in Chapter 6 (entitled “Takeovers”) of the Corporations Act, 2001 (acquisitions contravening the 20 per cent threshold), thus prioritizing contraventions that result in a change of control in a company. (As with the substantial shareholding disclosure provisions, s 606 is concerned with the acquisition of relevant interests, but only if share acquisition leads to an accumulation of voting power beyond permitted levels.) One of few relevant cases to go before an Australian court, ASIC v. Terra Industries Inc, involved a failure on the part of the defendant to lodge substantial shareholder notices within two business days of acquiring a relevant interest in more than 5 per cent of the company’s shares.26 Merkel J held that Terra Industries’ contraventions were “wilful, contumelious and … led to a seriously uninformed and misinformed market”.27 Terra Industries was deprived of its disposal rights and its shares vested in ASIC for the purpose of sale.

12.1.6.2 History of the New Zealand provisions

Prior to the introduction of the Securities Amendment Act 1988 in New Zealand, there was no means of ascertaining the identity and interests of substantial security holders (or their nominees) in public companies. As early as 1981, the New Zealand Securities Commission highlighted the need for reform in a report entitled Nominee Shareholdings in Public Companies: A Review of the Law and Practice with a Proposal for Reform (hereafter NZSC report). The NZSC report focussed on takeover activity in New Zealand and overseas. Such activity had been referred to as “takeover by stealth”, “takeover by inches” and “acquisition

23 Policy Statement 159.274.
25 policy Statement 159.264 & 159.279.
27 Id., 208.
by ambush”. The NZSC report foreshadowed the development of an “informal and off the record market in substantial shareholdings” as well as practices designed to “conceal transactions and interests which the principals do not wish to expose.” As a remedy, the NZSC report proposed that a substantial security holder disclosure regime be introduced. Though ultimately providing the policy basis for the substantial security holder disclosure regime, these recommendations languished for many years before being incorporated into the Securities Amendment Act 1988 (SAA).

The impetus for the introduction of a substantial security holder disclosure regime next arose out of “concern at so-called nefarious activities through nominees in the share market prior to the crash in October 1987”. However, substantial security holder disclosure quickly assumed a secondary importance. When the SAA was first introduced into Parliament in July 1988, nearly all attention was focused upon the insider trading provisions under Part I. There was little comment on the provisions in Part II which dealt with the disclosure of interests of substantial security holders. In 2000, the New Zealand Government embarked on a broad programme of reforms aimed at strengthening the regulatory framework of the securities market. Despite anecdotal evidence of concerns about the effectiveness of the disclosure regime, the law directly relating to substantial security disclosure remained unchanged.

The issue of substantial shareholder disclosure assumed greater prominence in 2003 when two significant cases reached the Court of Appeal. These cases arose in the context of takeovers and highlighted a number of difficulties in the legislation. The first case, Ithaca (Custodians) Ltd v. Perry Corporation (hereafter, Ithaca), examined the meaning of ‘arrangement or understanding’ and the standard of proof for determining whether relevant interests exist. The second case, Richmond Ltd v. PPCS Ltd (hereafter, Richmond), concerned the nature and purpose of orders that can be made against a party in default. These cases are reviewed later in this section.

28 New Zealand Securities Commission Report, above at para. 3.7
29 Id., 10.12 & 3.2
30 Brook Investment Ltd (in vol liq) v. Paladin Ltd (21 October 1989) High Court Auckland M1581/89, per Sinclair J.
32 [2004] 1 NZLR 731.
33 [2004] 1 NZLR 256.
12.1.6.3 Meaning of “substantial security holder”

The term “substantial security holder” is now defined in section 21 as a person (including a company) who has a “relevant interest” in 5 per cent or more of the voting securities of the public issuer. Section 2 describes “voting security” in general terms as a security which confers a right to vote at members meetings (with or without restrictions or limitations). Voting securities do not encompass rights to vote that, under conditions attached to the security, are exercisable only in exceptional circumstances, for example, on a proposal to put the public issuer into liquidation. A “public issuer” is defined as a person who is, or was at the relevant time, a company listed on a stock exchange.

The key question in determining whether or not a person is a substantial security holder is whether that person holds a “relevant interest” in a threshold stake. The substantial security holder regime will apply to any person whose interest exceeds this threshold.

12.1.6.4 Meaning of “relevant interest”

The term “relevant interest” is broadly defined and may arise in a variety of situations. The new definitions are contained in section 5-6. Section 5 provides the basic definition which is expanded or qualified in sections 5A-6.

Describing the former section 5, Fisher J noted in *Mercury Energy Ltd v. Utilicorp N.Z. Ltd & Power New Zealand Ltd. (Mercury Energy)*, that s. 5 broadly encompassed three categories of relevant interest: beneficial ownership, presently existing powers, and arrangements which may give rise to powers in the future”.

The need for such an extensive provision results from the nature of voting securities and the ingenuity of the legal mind. Shares confer a bundle of rights including the right to vote, the right to dividends, and the right to share in any available surplus upon the winding up of a company. These rights can be dealt with individually and assigned outright to other persons as can other property right. Alternatively, the benefit of the exercise of these rights (particularly the right to vote) can be transferred (for example, for a particular occasion such as a general
meeting or for a period of time) while the legal title and other rights are retained. In the context of voting rights, this can be achieved by granting a proxy to a person which is open-ended and allows that person to vote as they think fit at a general meeting. Alternately, it can be achieved by a shareholder entering into an agreement with another party to attend and vote at a meeting as directed to by that party. The ability to obtain control of shares and particularly the right to vote (without the need to obtain a beneficial interest in the shares) requires that the provisions be widely drafted.

In most cases, whether a person has acquired a “relevant interest” is easily established. For example, in Securities Commission v. Re Jones, Sir Robert Jones sold shares in Robert Jones Investments Ltd (RJI) but failed to give the appropriate notice. It was clear that Sir Robert was beneficial owner of the shares. Brook Investments Ltd v. Paladin Ltd and Securities Commission v. Honor Friend Investment Ltd involved overseas parties acquiring shares in New Zealand listed companies. In each case, it was clear that beneficial ownership had been transferred. The relevant issue was the failure of the new owners to disclose their acquisition.

The expansive reach of the former Part II was confirmed by the inclusion in section 5(1) (f) of the terms “arrangement” or “understanding”. These terms now reappear in new section 5A of the SMA. These terms were and are not defined in the SMA, however, they will be familiar to those involved in competition law, and arise in a number of sections of the Commerce Act 1986, particularly section 27. As a result of their inclusion, it is possible that dealings between parties which result in a meeting of minds, but which are not a contract, could create a relevant interest if they confer on one party “power” or “power to control” voting securities.

12.1.6.5 The Ithaca Litigation

As noted earlier, the meaning of the terms “arrangement” and “understanding” in the context of former section 5(1) (f) of the SMA was discussed in Ithaca (Custodians) Ltd v. Perry

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36 High Court, Auckland, 21 October 1989, M 1581/89, Sinclair J.
Corporation (Ithaca). Involving allegations of a failure to give notice of a relevant interest by Perry Corporation, a United States-based fund-manager. In April 2001, Perry Corporation held shares (amounting to 10.81 per cent) in the listed company Rubicon Ltd. In May 2001, Perry Corporation sold 14 million of these shares to Deutsche Bank and 17 million shares to UBS Warburg. These sales were matched by sophisticated equity swap transactions (governed by master agreements) with the two institutions. While the terms of the agreement provided for a termination date, the nature of the situation was such that the shares would be available for repurchase on demand. Perry Corporation subsequently made further purchases of Rubicon shares which were on-sold to Deutsche Bank on similar terms to those above. In September 2001, the equity swaps transactions were partially unwound. This enabled Perry Corporation to participate in a Rubicon buy-back, after which time it set about re-establishing its shareholding.

In June 2002, Guinness Peat Group plc (GPG) began purchasing shares in Rubicon with a view to assembling a holding of just under 20 per cent (to avoid the takeover threshold). GPG acquired a 19.87 per cent stake in the company and filed notice accordingly. It soon became apparent that GPG and Perry Corporation were strategically (if not philosophically) incompatible. In particular, the two were at odds over the future of Rubicon Forest Holdings Ltd, a Rubicon subsidiary. In July 2002, all the equity swaps were unwound and cash settled. Perry Corporation was consequently entitled to vote on those securities at Rubicon’s first annual meeting. In all, Perry Corporation filed substantial shareholder notices on three occasions. Disclosure was not made in respect of the shares held by Deutsche Bank and UBS Warburg as a hedge for the equity swaps. On this basis GPG instituted proceedings against Perry Corporation.

The High Court held that entry into the equity swaps did not give rise to a disclosure obligation per se. Under the circumstances, however, Potter J found that there was an arrangement or understanding pursuant to which Perry Corporation could repurchase the

38 [2004] 1 NZLR 731.
39 For an expert description of the type of transaction involved, see Gooch and Klein, Documentation for Derivatives, 4th ed., Vol. 1 (Euromoney Books). Use of equity swaps in this context is not confined to New Zealand. There have been recent instances in the UK and Australia. For the UK, see The Panel on Takeovers and Mergers, Consultation Papers on Dealings in Derivatives and Options (January 2005 and May 2005). For Australia, see Guidance Note 1: Unacceptable Circumstances and In the Matter of Austral Coal 02 [2005] ATP 13; In the Matter of Austral Coal 02(R) [2005] ATP 16.
shares which gave rise to an ongoing interest in the shares. On this basis, Potter J concluded
that Perry Corporation had breached its disclosure obligations by not disclosing the equity
swaps. The following factors were determinative in this regard:

(a) Perry Corporation was confident that the shares would be available for repurchase as
required, as were Rubicon and the Deutsche bank.

(b) at all relevant times, Rubicon treated Perry Corporation as being a substantial
shareholder;

(c) Both Rubicon and Perry Corporation were concerned about GPG’s intentions and
wished Perry Corporation to be able to exercise its voting rights as a major
shareholder at the annual general meeting.

(d) On both occasions when Perry Corporation needed large parcels of shares, the equity
swaps were promptly terminated and the shares repurchased.41

Taking into account the deliberate nature of the non-disclosure (perpetrated by a sophisticated
investor); that it lasted over 12 months; related to 36 million shares and the need for
deterrence, Potter J ordered the forfeiture of 12 million Rubicon shares and the on-market sale
of the remaining 24 million shares.42

The New Zealand Court of Appeal set aside the orders made by the High Court. The Court of
Appeal ruled that the terms “arrangement” and “understanding” describe something less than
a formal contract but more than mutual expectations based on commercial reality. In this case,
market reality (in a practical business sense) diminished the necessity for an arrangement or
understanding in relation to the reacquisition of the hedge shares. Hence, it was regarded as
inherently unlikely that one was entered into. Moreover, the power to control securities must
arise by virtue of the arrangement or understanding and not merely as a result of its
performance. The Court was satisfied that the pattern of dealings and transactions by Perry
Corporation merely reflected market reality and did not give rise to an arrangement or
understanding. With respect to section 5(2), the Court ruled there was insufficient evidence to
draw the inference that Perry Corporation’s equity swap partners were accustomed to act in
accordance with its wishes.

40 GPG was in fact the second respondent in this case. Ithaca (Custodians) Ltd (the first respondent) is a GPG
subsidiary holding GPG’s share investments in New Zealand. Rubicon Ltd was the third respondent.
41 [2004] 1 NZLR 731.
42 The orders targeted the 36 million voting securities that the equity swaps related to. Perry Corporation was
prohibited from exercising voting rights or receiving any payments in relation to the shares pending their
sale.
Ithaca demonstrates that sophisticated financial instruments can be used to avoid the substantial shareholder regime. It is submitted that the decision of the Court of Appeal was wrong and that the decision of Potter J in the High Court is to be preferred. The proposed amendments contained in the first version Securities Legislation Bill 2004 (noted above) were aimed at negating the effect of the Court of Appeal decision. However, in the version of the Bill reported back from the Commerce Committee these amendments were removed.

12.1.6.6 Meaning of “Power” and “Power to Control” pre-February 2008.

The former section 5(1) was considered in relation to claims involving “relevant interests” (other than beneficial ownership) by both the High Court and in a report by the NZSC into the voting securities of Air New Zealand Ltd in 1991. Although the NZSC report has no precedent value, it is one of few times that section 5 has been considered in New Zealand.

Gulf Resources

In *NZSC v. Gulf Resources and Chemical Corporation*, the NZSC alleged that Gulf Resources (Gulf) had acquired a relevant interest in the voting securities of City Realties Ltd (CRL) yet had failed to disclose this interest as required. In this case, certain persons made representations to Tower Corporation for the purpose of acquiring its shares in CRL allegedly on behalf of other persons. The NZSC alleged that the shares were acquired by a company, Zelas Enterprises Ltd (Zelas), as trustee for Gulf. As a result, Gulf was the beneficial owner of the shares and therefore had a relevant interest in the shares (under section 5(1) (a)).

43 For a review of Perry Corp’s activities in other jurisdictions, see Henry Hu and Bernard Black, “Hedge Funds, Insiders, and Decoupling of Economic and Voting Ownership in Public Companies” (January 2006). University of Texas School of Law Working Paper No. 53).

44 The difficulty that disclosure laws have with complex transactions (such as the equity swaps in *Ithaca*) was examined by Professor Steven Schwarz in “Rethinking the Disclosure Paradigm in a World of Complexity” (2004) 1 *U of Illinois LR* 1-37. The conduct described in the *Ithaca Case* might give rise to “unacceptable circumstances” in a takeover context in Australia. See *In the Matter of Austral Coal* [2005] ATP 16.

45 In the Commentary to the Bill as reported back, it was stated that (at page 8): “Extension of the relevant interest definition to include a power or control exercised through a practice was intended to cover a potential gap in the law exposed by recent litigation. However, we consider that the deficiency is factspecific to that case, and that the proposed solution would create undue uncertainty as to when the substantial security holder disclosure obligation arises.”

46 (1990) 5 NZCLC 66,324.
McGechan J determined that the initial moneys advanced to Zelas for the purchase came from one of the persons who had made the original representations to Tower Corporation, not from Gulf.\(^{47}\) He also found that a subsequent advance by Gulf to Zelas of $16.7m was in fact a loan. Accordingly he was satisfied “that no beneficial ownership by Gulf of either Zelas or of Zelas’ CRL holding was thereby created”.\(^{48}\)

This was not the end of the matter, however, since four documents were signed in relation to the loan and shares in Zelas and were later issued to Gulf. The four documents comprised a loan agreement between Zelas and Gulf; a debenture over Zelas to Gulf; a mortgage over the Zelas’ shares by the shareholders to Gulf; and, “a Deed of Covenant between Mr McGoldrick and Mr Whitaker and Gulf under which to speak very roughly the latter gentlemen were not to act prejudicially to Gulf”.\(^{49}\) Gulf only disclosed the loan agreement. The NZSC attacked the omission of the Deed of Covenant as a breach of the Act. McGechan J then found:

\[\text{I think the omission of the Deed of Covenant from the notice was technically a failure to notify a relevant interest under sec 5(1) (f) and so under sec 5(2). The Deed’s restraint upon prejudicial action carried with it a restraint and hence control on voting from at least the time of the Gulf loan to Zelas and contract as represented by the Deed.}\(^{50}\)

While McGechan J did not specify which subparagraph of section 5(1) (f) he was relying upon, it would appear to be subparagraph (ii) which deals with the “power to control the exercise of any right to vote attached to the voting security”. Ordinarily this would cover a situation where the substantial security holder indicates that a shareholder has to vote for or against a particular resolution. The terms of the Deed of Covenant are not set out in the judgment but it seems that there was no requirement for the covenantees to consult with Gulf prior to voting. McGechan J’s view extended the concept of “power to control” to a situation where a shareholder can vote as they wish provided they do not prejudice the other party’s interests - in a sense a negative constraint or “control” on the power to vote. This raises the question of whether or not a positive obligation that a shareholder take into account the interests of another when considering how to exercise one’s power to vote, without the other

\(^{47}\) Id., 66,333.
\(^{48}\) Id., 66,334.
\(^{49}\) Id., 66,334. Emphasis added.
\(^{50}\) Id., 66,335. Emphasis added.
party specifying how to vote or actually influencing how a vote is cast, would also constitute a “control” or a “power to control”.

In any event, the concept of “power to control” under section 5 (on McGechan J’s interpretation) appears to have a very wide ambit. It could be found to arise from something less than an agreement (“an arrangement or understanding”), which may be express or implied (section 5(4)(a)), whether or not it is legally enforceable (section 5(4)(c)).

The Air New Zealand Report

The NZSC report pertains to the privatisation of Air New Zealand Ltd (Air NZ) in 1989 and 1990.51 Qantas and Brierley Investments Ltd (BIL) formed part of a consortium that made a bid for a stake in Air NZ. Part of the arrangements for the consortium included an agreement between Qantas and BIL.

Qantas and BIL’s agreement provided for consultation when either party decided to sell its shares.52 Essentially, notice was given in order that the other party might find a possible purchaser. If the other party found a purchaser at a better price that party was to share in the price obtained that exceeded the original price notified by the offering shareholder. Clause 4(b) provided for the payment of 25 per cent of the sale price of any shares sold in the event that either party sold their shares without first advising the other. Clause 4(c) provided for a 5 per cent penalty in the event that the shares were sold to a purchaser, who had not been located by the other party, at the same price or on better terms for the purchaser. The agreement did not require that the shares be offered to the other party first, although the other party could obviously have bid for the shares, so that it did not constitute a pre-emptive requirement. In fact, clause 4(d) expressly provided that neither party had “any power to control the disposition of any of the seller’s shares” in Air NZ, and that the sole remedy was in damages as measured by the amounts specified in clauses 4(c) or 4(d).

One of the issues that concerned the NZSC was whether or not some of the provisions of these agreements constituted a constraint “on either party’s freedom to dispose of the securities of such as to give rise to a relevant interest in the voting securities of Air New

52 Id., Appendix D.
Zealand”. The NZSC considered what was meant by “power to control”. It accepted the submission of one counsel that “control” should be taken as having its ordinary (dictionary) meaning:

… the fact of controlling, or of checking and directing action; domination, command, sway.

Taking into account this definition the NZSC stated:

Having regard to this ordinary meaning given to the word “control”, the statutory expression would cover the circumstances where a person is in a position to direct or to exercise a dominating influence over the acquisition or disposition of a share by another person.

The NZSC then considered decisions pertaining to parallel Australian provisions. In particular, it noted a decision of Beach J in Re Kornblums Furnishings Ltd “that where the practical effect of an agreement to dispose of shares is that any shareholder who was a party to the agreement could restrain any other shareholder from selling his shares on the open market, a relevant interest had been created”. In the light of this decision, and taking into account section 5(6) (which provides that a “power” can include a power that arises from breaching a trust, agreement or understanding, whether or not it is legally enforceable) the NZSC formed the view that:

When proper weight is given to s.5 (6), it follows that a negative constraint, although not capable of enforcement by way of injunction, may still constitute the exercise of a power of control. The existence of an economic power which would effectively constrain a shareholder’s freedom of action in the disposition of his shares may constitute a relevant interest for the purposes of the Act.

The NZSC later appeared to qualify this statement, stating that counsel for the parties had accepted that “where a shareholder was in a position to place a significant economic constraint on the freedom which another shareholder would otherwise have to dispose of its shares, this could amount to the exercise of a power to control the disposition of the shares,

53 Id., 22.
54 Id., 23.
55 Ibid., Emphasis added.
56 [1982] VR 123.
58 Ibid. Emphasis added.
and so create a relevant interest”.\(^{59}\) Having determined that a (significant) economic power is sufficient, the issue then became whether or not on the facts of this case such a power existed.

Counsel for BIL and Qantas both argued that clauses 4(b) and (c) of the agreement were designed to encourage compliance and that “the requirement to consult and the financial mechanisms in the agreements [did] not create or permit the exercise the of a degree of control sufficient to oblige or coerce a party to act in a certain manner”, rather they were incentives or inducements.\(^ {60}\) Counsel relied upon Australian High Court dicta that “a power on a person to provide shareholders with an incentive or inducement to exercise their voting power as that person may wish is not aptly described as making the company capable of being controlled by that person”.\(^ {61}\) The NZSC was unwilling to accept these dicta outright, saying that “it is a matter of degree, and it may be necessary to determine at what point a mere inducement or incentive becomes sufficiently powerful to constitute an effective constraint which directs a party towards a desired course of action”.\(^ {62}\) After analysing the clauses the NZSC held that they were not an effective economic constraint on either party. The NZSC also stated that it gave little weight to clause 4(d) as it took the view that it was necessary to look at the agreement as a whole, and that such a declaration would not have any effect if there were provisions that did confer control over the disposition of shares.

The NZSC clearly viewed the expression “power to control” as having a wide ambit. Economic incentives have the potential to come within this term and hence create a relevant interest. If clauses 4(b) or 4(c) had provided for a 100 per cent penalty for the failure to comply or had provided that the seller had to give six to twelve months notice then it is possible that the NZSC would have viewed these provisions as conferring a “significant economic constraint”. However, it should be remembered that “economic power” does not need to refer directly to the disposition of shares as happened in this case. It is possible to imagine two parties which have a commercial relationship (such as supplier and purchaser of manufactured goods or financial services) where the supplier is able to use its economic power, arising from the commercial relationship, to “oblige or coerce” the purchaser into dealing with the shares in a way that is desired by the supplier. The provision of goods or services at a favourable rate or the threat to remove supply or only to supply at unfavourable

\(^{59}\) Id., 25. Emphasis added.
\(^{60}\) Id., 26.
\(^{61}\) WP Keighery Pty Ltd v. FCT (1956) 100 CLR 66, 86.
rates may be sufficient. As only an “arrangement or understanding” is needed and the arrangement can be indirect or even unenforceable it is possible that a “relevant interest” could arise in such a situation.

The Mercury Energy Case

This case arose out of a long running takeover battle for the control of Power NZ Ltd between Mercury Energy Ltd (Mercury) and Power NZ Ltd (Power NZ) and Utilicorp NZ Ltd (Utilicorp). The takeover battle spawned a significant amount of litigation as each side attempted to use various actions to slow down or gain an advantage over the other side. Previous actions included an unsuccessful claim by Power NZ alleging the takeover offer by Mercury was in breach of the Fair Trading Act 1986 and the Companies Amendment Act 1963, and a further unsuccessful claim that the proposed merger would breach the Commerce Act 1986. Mercury too pursued its share of unsuccessful claims, including an injunction to restrain Power NZ acquiring shares in Waikato Energy Ltd. The most recent litigation between the parties, Mercury Energy Ltd v. Utilicorp N.Z. Ltd & Power New Zealand Ltd, involved an allegation that Utilicorp failed to give the appropriate notice under Part II of the SMA. Like the Air NZ case referred to above, this case involved analysis of a written agreement. The critical issue was whether or not a put option or pre-emptive agreement came within the terms of section 5, so as to confer a relevant interest on Utilicorp.

In December 1995, in the midst of the takeover battle between Mercury and Utilicorp, Utilicorp entered into an oral agreement with three local councils who held shares in Power NZ. The local councils granted a put option to Utilicorp and a right of first refusal in the event that the councils wished to sell their shares. At the time Utilicorp failed to notify this agreement under Part II of the SMA. In early July 1996 Mercury became aware of the agreement (when a fax was sent to the home of one of Mercury’s officers containing some of the local councils’ confidential documents). In late July, under threat of litigation by Mercury, Utilicorp gave notice of its interests pursuant to the agreement. The notice made it

clear that the effect of the agreement was to raise Utilicorp’s relevant interests (taking into account its interest in WEL Energy Group Ltd which was a shareholder of Power NZ) from 35 to 42.76 per cent.

Mercury then commenced an action claiming that Utilicorp had breached Part II. Though conceding it was engaging in the proceedings to “assist in its take-over battle”, Mercury argued that the orders it was seeking (including suspension of Utilicorp’s voting rights; forfeiture or disposal of its shares; forfeiture of its dividends and/or restraints upon share transactions to which it might be a party the forfeiture of Utilicorp’s shares) were in the “wider public interest”.67

Fisher J considered whether the put option or the right of first refusal conferred a relevant interest on Utilicorp. He noted that the option did not impose an obligation on the local councils to sell, nor to sell at a particular price, or even to sell to Utilicorp. Utilicorp did gain a potential right to insist upon a sale but this was subject to the fundamental condition that the local council’s wished to sell their shares. Fisher J found that neither provision conferred beneficial ownership nor did it give Utilicorp any existing powers. The issue then became whether it created a power which arose in the future.

Fisher J held that the relevant provision to examine was section 5(1) (f) (iii) (which deals with a person who may have the power to dispose or acquire shares at any time). He thought that section 5(1) (d) (which deals with a person having the power to acquire or dispose of the voting security) could be of potential relevance when combined with section 5(4). The latter provides, among other things, that the power can exercisable presently or in the future (s 5(4) (f)) and only on fulfilment of a condition (s 5(4) (g)). Fisher J was inclined to think that the reference to condition in section 5(4) (g) “was intended to refer to an event beyond the control of the contracting parties, thereby excluding put options and rights of first refusal”. Why Fisher J came to this conclusion is not clear as there is nothing in the subparagraph that would appear to support this view.

The elements of section 5(1)(f)(iii) that Fisher J considered in greater depth were the meaning of the term “power”, and the significance of the phrase “may at any time”. In considering the term “power” Fisher J found:

67 Ibid.
I agree with Mr Craddock that in this context “power” is concerned with the ability to do something, that the ability to bring about the effect required must lie within one’s own hands and not those of another, and that a notion of domination or command is involved. None of those facilities necessarily exists at the time that a right of first refusal is conferred but of course s 5(1) (f) (iii) does not demand the existence of the power from the beginning. Nor is it necessary to postulate that the power will necessarily ever arise in the future. It is sufficient if at the time of the agreement one can say that the grantee “may at any time” have such power. And of course the possibility that the power may only arise in the future, and be exercisable only on fulfilment of conditions, is expressly provided in s 5(4) (f) and (g).68

Fisher J’s view that “power” involves the notion of domination or command is similar to that of the NZSC in the _Air NZ_ report. This position places a relatively high threshold on what constitutes “power”, although this is tempered by the requirement that it “may arise any time” in the future.

Fisher J went on to consider the phrase “may at any time”. He rejected an argument put forward by counsel for Utilicorp that attempted to equate this term with the term “will”. In his view:

The phrase “may at any time” is not to be equated with the word “will”. Section 5(1) (d) (“has the power to acquire”) in combination with section 5(4) (f) (“is exercisable...in the future”) already caters for the case in which it is known that the power to acquire will arise in the future. The significant element introduced by s5(1)(f)(iii) is that in place of certainty it becomes sufficient if by virtue of the agreement the power “may at any time” accrue. The role of the word in s5 (1) (f) (iii) is thus to indicate uncertainty: there is a possibility that the grantee will “have the power to acquire” the shares but equally there is the possibility that that power will never accrue. That is precisely the situation with a right of first refusal.69

Fisher J considered the “absurd consequences” that could flow from holding that the mere possibility that an interest may be acquired was sufficient to constitute a relevant interest. He accepted that there were “many situations in which a trust, agreement, arrangement or understanding creates the mere possibility that a person may acquire shares or may control their acquisition or disposition”. After considering the policy behind the legislation (particularly that of promoting the prompt provision of adequate information to the market), the Act’s legislative history, and the approach to this issue in Australia, Fisher J was of the view that the result was not so absurd “that one would be justified in departing from the literal  

68 Id., 501.
69 Ibid.
language of s 5". He preferred to deal with “anomalous situations” by exercising the discretion under section 32 for the imposition of any penalty. As a result, Fisher J determined that Utilicorp should have disclosed the December agreement and the put option and right of first refusal.

12.2 Criminal Liability

12.2.1 Criminal Liability for Misstatements

Advertisements: Section 58(1) of the Act states that where an advertisement which contains an untrue statement is distributed then the issuer of the securities referred to in it, if an individual, commits an offence. If the issuer is a body, an offence is committed by every director of it at the time of distribution.

Registered Prospectus: Section 58(3) of the Act states that, where a registered prospectus that includes an untrue statement is distributed, every person who signed the prospectus commits an offence. Section 55 defines untrue statements by way of a deeming provision. A statement in a registered prospectus is deemed to be untrue if it is misleading in the form and context in which it is included or it is misleading by reason of the omission of a material particular. Decisions on s. 58 are R v Reid (1990) 5 NZCLC 66, 483 (HC); R. v Rada Corporation Ltd (No. 2) [1990] 3 NZLR 453 (HC); District Registrar of Companies v Heenan (1996) 1 BCSLR 264, 279 (DC) and R v Baxter [1998] 3 NZLR 144 (CA). Section 58 (3) – which concerns an untrue statement in a registered prospectus - is a strict liability offence subject to a statutory defence of immateriality or reasonable grounds to believe that the statement was true. The term, “distribute” is defined in the 78 Act in section 2 (1). The onus is on the defendant to avoid a conviction, assuming a prima facie case is made out by the prosecution. The prosecution need not show that an investor suffered loss as a result of the untrue statement. The defendant must prove one of the two statutory defences on the balance

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70 Id., 505.
71 Ibid.
72 See Arnison v Smith (1889) 1 Dr. & Sm 363; R. v Kylsant [1932] 1 KB 442; Flavel v Giorgio (1990) 8 ACLC 608; R v Rada Corporation (No 2) [1990] 3 NZLR 453.
of probabilities. Whether a statement is immaterial is to be looked at not only from an actual investor’s standpoint but also from the reasonable investor’s standpoint.

**Penalty:** An offence against s. 58 carries a penalty of imprisonment for up to 5 years or a fine not exceeding $300,000 on conviction on indictment. On summary conviction, the penalty is imprisonment for up to 3 months or a fine not exceeding $300,000.

**Defences:** Liability is avoided where it is proven either that the statement was immaterial or that there were reasonable grounds to believe (and the requisite person did so believe up to the time of distribution of the advertisement or prospectus), that the statement was true.

**Materiality:** The leading case in New Zealand on the meaning of “material” is *Coleman v. Myers*.74 Directors of what was essentially a family company offered to purchase shares from shareholders without disclosing that the accounts, which were based on the book value of the company’s assets, significantly understated the market value of those assets. Cooke J (as he then was) discussed the obligations of directors to disclose material information to shareholders when they are advising them on an offer and they are also the vendors. Cooke J stated:

> With regard to moulding of the precise scope of the obligation here, it must be important to remember that directors are free to profit from their position, in the sense that there is no reason why they should not make a profit from dealings with shareholders. The obligation has to be worked out in terms of representations and disclosures. Particularised in those respects … there must be an obligation not to make to shareholders statements on matters material to the proposed dealing which are either deliberately or carelessly misleading. And in my opinion there must be at least an obligation to disclose material matters as to which the director knows or has reason to believe that the shareholder whom he is trying to persuade to sell is or may be inadequately informed. As to what matters are material, there was some debate in argument before us. In his judgment Mahon J uses sometimes the expression *might* influence the shareholder, sometimes *would*. Mr Williams prefers *would*. I think it is often easier to assess whether a statement is in the circumstances truly significant than to propound a watertight test. If forced to a formula I would select one somewhere between the alternatives just mentioned.75

Cooke J then set out his broad test of materiality as “those considerations which can reasonably be said, in the particular case, to be likely materially to affect the mind of a vendor or of a purchaser.”76 Cooke J relied on the United States Supreme Court decision *TSC*
Industries Inc v. Northway Inc\textsuperscript{77} where Marshall J considered proxy solicitation and commented that:

An omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote. This standard is fully consistent with Mills’ general description of materiality as a requirement that ‘the defect have a significant propensity to affect the voting process’. It does not require proof of a substantial likelihood that disclosure of the omitted fact would have caused the reasonable investor to change his vote. What the standard does contemplate is a showing of a substantial likelihood that under all the circumstances the omitted fact would have assumed actual significance in the deliberations of the reasonable shareholder. Put another way, there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor having significantly altered the ‘total mix’ of information made available.\textsuperscript{78}

While the \textit{TSC Industries} case involved proxy solicitation, a more recent Supreme Court decision based on Rule 10 b - 5 (which covers insider trading and fraudulent disclosure suits) is \textit{Basic, Inc v. Levinson}.\textsuperscript{79} The United States Supreme Court also adopted the reasonable investor standard for materiality: An omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important.

Cooke J’s consideration of the meaning of “materiality” shows a close parallel with the philosophy of disclosure under the Act. While Cooke J was dealing with an issue arising out of common law rather than statute, his reasoning would still appear to be very relevant given that he found that directors had a duty not to make misleading statements and had an obligation to disclose material matters. Both of these duties parallel the definitions of "untrue statement" in section 55. Also, the common law position for promoters or directors of a securities offering was one requiring "utmost candour and honesty" which is similar to the obligations that Cooke J found for directors who purchase shares in a \textit{Coleman v. Myers} situation. As such Cooke J’s comments should be considered to form the basis for determining "materiality" in prospectus statements even though he was dealing with directors’ common law obligations. For Cooke J the information had to be “likely to materially affect the mind” of an investor of average prudence.\textsuperscript{80}

\begin{footnotes}
\item[77] 426 US 438 (1976).
\item[78] \textit{Coleman v. Myers} [1977] 2 NZLR 225, 334.
\item[79] 485 US 224 at 231 (1988).
\item[80] Ibid.
\end{footnotes}
On the basis of Coleman v. Myers "material information" does not have to be such as to determine the outcome of the investor’s decision. However, it appears Cooke J was inclined to the view that the information had to be such that the investor would take into account in making his or her decision. Initially Cooke J commented that he thought that the test as to whether or not information was material lay between whether it “might” or “would” influence an investor, but he subsequently adopted Marshall J’s approach who clearly considers that information is material if it would influence a shareholder. From the viewpoint of certainty it would be preferable if the test was the higher test of “would” influence a reasonable investor. This is consistent with the United States position, although in Australia the lower test of “may” has been used. Hazen commented that in the United States, “the test of materiality is whether a reasonable investor would have considered the matter significant; it is not necessary to show that the investor would have acted differently”. As he pointed out once materiality is established the investor still has to show cause or connection between the violation, the transaction and the loss suffered.

Coleman v. Myers also indicated that the perspective from which "materiality" was to be determined was that of the reasonable shareholder, not an actual shareholder. Hazen pointed out that in the US in the context of Rule 10b-5 that the test of materiality “depends not upon the literal truth of statements but upon the ability of reasonable investors to become accurately informed.”

The use of the “reasonable” investor is consistent with Maslen v. Shaw, and with earlier common law authority on share offerings. For example, Lord Halsbury LC commented in Arnison v. Smith:

It is an old expedient, and seldom successful, to cross-examine a person who has read a prospectus, and ask him as to each particular statement what influence it had on his mind, and how far it determined him to enter into prospectus and determines to take shares on the faith of it can appropriate among the different parts of it the effect produced by the whole. This can rarely be done even at the time, and for a shareholder thus to analyse his mental impressions after an interval

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81 Id., 333.
82 Id., 334.
85 TL Hazen, op. cit., 793 (emphasis added).
87 See Broome v Speak [1903] 1 Ch. D 586, 629.
of several years, so as to say which representation in particular induced him to take shares, is a thing all but impossible. A person reading the prospectus looks at it as a whole, he thinks the undertaking is a fine commercial speculation, he sees good names attached to it, he observes other points which he thinks favourable, and on the whole he forms his conclusion. You cannot weigh the elements by ounces. It was said, and I think justly, by Sir G Jessel in *Smith v. Chadwick* that if the Court sees on the face of the statement that it is of such a nature as would induce a person to enter into the contract, or would tend to induce him to do so, or that it would be a part of the inducement to enter into the contract, the inference is, if he entered into the contract, that he acted on the inducement so held out, unless it is shown that he knew the facts, or that he avowedly did not rely on the statement whether he knew the facts or not. 88

**New Zealand Case Law on section 58 of the 78 Act**

Section 55(a)(ii) provides that a statement is untrue if it omits a particular which is material in the form and context in which it is included. Section 58 imposes criminal liability for untrue statements in any advertisement, investment statement or registered prospectus.

The first decision to consider section 58 and section 55(a)(ii) involved an offer of shares by Prorada Properties Limited, a subsidiary of Rada Corporation Limited. 89 A prospectus issued by Prorada Properties Limited in 1987 stated that Rada Investments Limited, another subsidiary of Rada Corporation Limited, would take up $50 million in share capital in the offeror company in effect on behalf of Rada Corporation. Rada Investments borrowed $50 million from a bank and subscribed for $50 million in shares. Prorada Properties in turn lent the $50 million to Rada Nominees Limited which in turn deposited the $50 million on term deposit with the lending bank and acted as guarantor for Rada Investments Limited’s loan obligations. This meant that the issuer could not use for its own purposes the $50 million it had received from Rada Investments. Neither were funds placed on either the official short term money market or any unofficial money market as promised in the prospectus. In addition, the prospectus stated that investments would begin as soon as possible after the date of registration of the prospectus but in fact Prorada could not use the $50 million from Rada Investments and there was evidence that it had been decided before the prospectus was issued that no investments would be made by the company until a chief executive had been found. However, the prosecution only alleged that the statement in the prospectus that the $50

88 (1889) 41 Ch D 348,369.
89 *R v Rada Corporation Limited (No 2)* [1990] 3 NZLR 453.
million payable by Rada Investments was misleading since it omitted a material particular, that is, that it did not have the cash or a firm arrangement to obtain the $50 million. Barker J hinted strongly that these other statements could have been the subject of an action.

Barker J found that at the relevant time Rada Corporation had shares in other investments in excess of $50 million which could readily have been converted into cash within a matter of days. Effectively he treated Rada Corporation and Rada Investments as one party and treated the term “cash” as including that held in the Bank but also the cash that could be gained through Rada Corporation. He took the view that looking at the position from “commercial reality” there was cash available if needed. Barker J was relatively liberal in terms of finding that “cash” included liquid assets held by a parent company, in effect removing the corporate veil to do away with the distinction between the subsidiary and the parent company, although the prospectus did indicate that Rada Corporation was investing through Rada Investments.

On the issue of “materiality” Barker J held that:

The omission was immaterial because, on 14 October 1986, Rada Corporation both had the $50 million in readily available assets or could have borrowed $50 million from a variety of sources. Investors reading the prospectus would have assumed that Rada Corporation would be funding the Prorada Properties share money either from its own sources or else from borrowings. They would have known of NZFP’s interest in Rada Corporation and assumed that NZFP would never let Rada Corporation default in its obligations.

Given the nature of the disclosure in the prospectus of Rada Corporation's involvement Barker J's decision would appear to be correct as materiality of an omission has to be determined on the basis of the statement "in the form and context in which it is included". His comments on the matters that he hinted may have been more appropriate for a prosecution provide greater insight into his views on materiality. On the issue that the money "invested" by Rada Investments was loaned to a related company rather than placed on the short-term money market he commented:

I should have thought that the average investor, seeing a statement about investment in the short-term money market, would take it to mean just that.

90 Id., 455.
91 Id., 462-463 and 465-466.
92 Id., 471 - 472.
93 For criticism of this decision, see Walker, “Lifting the Corporate Veil to Avoid Criminal Liability for Misstatements in Registered Prospectus” (1993) 11 Company and Securities Law Journal 58.
Possibly the expression could be stretched to include reputable unofficial short-term money market dealers as well as official dealers.

The average investor would not have envisaged a loan to an in-house company which was really not a loan at all. I am not clear about Mr Gunn's reference when he said the directors could invest in anything. In fairness, I note that the interest earned by Prorada Properties was probably the equivalent of what it would have received in the short-term money market. The more weighty objection is that the money was unavailable for Prorada Properties' use.95

Barker J's approach is consistent with Cooke J, in that the focus is on the "average" or "reasonable" investor. In addition, he would have clearly have expected disclosure of the in-house loan even though the interest actually received was equivalent to that on the short-term money market. In other words, investors may have received the same return as on the short-term money market but they should have been advised of this intention in the prospectus. In addition, it is clear that he thought the issue was a matter for the court as he did not accept the views of witnesses who stated that the statement relied upon by the Crown was material.96

The second decision to consider the second limb of section 55 was Department of Justice v. Witehira.97 Witehira was managing director of Powerbeat International Limited which issued a short form prospectus. The prospectus included a forecast of income and a substantial component of the forecast income was a series of payments from a licensee of Powerbeat’s technology. The prospectus stated that the forecasts were based on a number of assumptions including that the Powerbeat “expected” to receive the forecast income. At the same time the directors did not accept liability for any forecast for the level of expenditure and had included a statement that “the projections made in this forecast statement may be varied at the Director’s discretion in response to changing commercial consideration”.98 The Department of Justice claimed that the prospectus contained an untrue statement by way of a material omission by its failure to refer to a deteriorating relationship with the licensee and in particular that a cheque for US$500,000 had not been honoured at the time the prospectus was signed. A second attempt to lodge the cheque was not known by the directors to be unsuccessful at the time the prospectus was distributed.

Spear J noted that the particular statement in the prospectus was:

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95 Id., 465.
96 Id., 475-476. This is consistent with Pancontinental Mining Ltd v Goldfields Ltd (1995)16 ACSR 463, 466.
97 (1996) 7 NZCLC 261,184.
98 Id., 261,191.
... a forecast couched in very cautionary terms as expected income. It is expressly stated to be conditional upon payment being made.99

He was of the view that the omission to refer to the cheque not having been met was not material because the directors did not fully appreciate that the cheque was worthless. They believed that there was some administrative or banking difficulty had led to the cheque not being met.100 He also held that, on an objective basis, the dishonouring of the cheque the first time was not material "to that particular financial forecast statement in the form and context in which that statement is included in the prospectus". Accordingly, he held that the Crown had not proved that the particular statement as to expected income was untrue, even though the income from the licensee represented $500,000 out of the forecast $2,700,000.

Spear J made no attempt to define materiality, nor did he refer to earlier authorities on this point. His approach would appear to be inconsistent with Coleman v Myers in that he concentrated on the directors’ belief in determining materiality. In effect he substituted the "reasonable grounds for belief" defence under section 58(4) with the preliminary issue under section 55 as to whether or not the omission was material.101 Given that an earlier payment by the licensee had been late and the first cheque had been dishonoured the use of the forecast without reference to these facts would arguably be material to a reasonable investor.102 The directors’ belief would only then became relevant to the defence under section 58(4). Spear J’s focus on the directors’ views rather than a reasonable investor’s view is at odds with both Coleman v Myers and Rada.

The third decision involving section 58 was District Registrar of Companies v Heenan.103 In this case the Registrar laid seven charges against Heenan, a director of a company which had issued two prospectuses. The second prospectus stated that $3,000 in fees had been paid to Heenan when in fact by the time the second prospectus was registered he had received $10,000. Callaghan J found there was an untrue statement and the issue was whether the defendant could successfully argue that the statement was “immaterial” under section 58.

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99 Id., 261,191.
100 Id., 261,191.
101 Spear J held that in any event even if he had found that the statement was untrue he would have had no difficulty in finding that the statutory defence was met in that Witehira honestly held a belief that the company would receive that income. He also found the defendant was an impressive witness and that his position was supported by other members of the company including directors.
102 Id., 261,189.
103 (1996) 1 BCSLR 264.
Heenan led witnesses who stated that they had not taken the statement into account and argued that, as a result, it could not be material. Callaghan J referred to the “materiality” test in *Coleman v. Myers* and *TSL Industries Inc v. Northway Inc* and noted that these cases showed:

… that there is an objective element in the ascertaining of whether an omitted fact is material or not. Thus it is the reasonable shareholder the Court is to consider, i.e. an objective approach.\(^ {105}\)

Callaghan J was of the view that *Coleman v. Myers* was not concerned with the relevant statutory provision when he came to consider “materiality” or “immateriality”. As discussed earlier, it is true that Cooke J was dealing with an issue arising out of common law rather than statute but his reasoning would still appear to be very relevant given that he found that directors had a duty not to make misleading statements and had an obligation to disclose material matters and the common law position for promoters or directors of securities offering was similar to the obligations that Cooke J found for directors who purchase shares in a *Coleman v. Myers* situation.

Callaghan J turned to the dictionary definition of "immaterial" instead and stated:

Immaterial” in s. 58(4) is not related or compared to any particular circumstance or circumstances. I accept that it can be considered in relation to potential investors who are the people s58 is designed to protect.

Whether the misstatement is “immaterial” is to be looked at not only from an actual investor standpoint but also from the reasonable investor’s standpoint. “Immaterial” is defined in the *Oxford Dictionary* as meaning ‘of no essential consequence, unimportant’.\(^ {106}\)

Callaghan J then went on to say:

It was quite clear that none of the witnesses called for the informant had in fact turned their mind to this [statement]. While it is correct that the investors who gave evidence may not have altered their decision I cannot say viewed from the standpoint of a reasonable investor that the misstatement was immaterial. In my view it cannot be said that the difference between the $3,000 which was referred to in the second prospectus, and the $10,000 which was in fact the sum paid is unimportant or of no essential consequence. Here the difference between the two

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104 Id., 281.
105 Id., 282.
106 Ibid.
amounts is quite significant being $7,000. In considering this, the misstatement cannot be characterised as immaterial.\textsuperscript{107}

Callaghan J’s view that materiality is to be determined from a reasonable investor’s view and that the views of actual investors are not decisive is consistent with earlier authority. Despite Callaghan J’s views, the dictionary definition he relied upon would not appear to be inconsistent with the approach in \textit{Coleman v Myers} since reasonable investors would be unlikely to take into account information that was inconsequential or unimportant. It would merely appear to be another way of expressing the same approach.

A recent decision under section 58 is \textit{R v Baxter}. Mr Baxter mounted an expedition to search for the wreck of the \textit{General Grant}, a ship which founded on the west coast of the Auckland Islands in 1866.\textsuperscript{108} The wreck was alleged to contain gold thought to be valued between $5 million and $50 million. Persons associated with Mr Baxter issued a prospectus but raised less than the amount required. The subscription monies were returned at the same time as investors were sent a letter inviting them to indicate their interest in investing in a further expedition on a smaller scale ($425,000 rather than $600,000). Baxter received around $80,000 which was initially put into a trust account and was later paid into his own account from which he paid for work to be done on the salvage ship which he now owned. On advice from his solicitor he registered a prospectus but did not advise his solicitor that he had already received funds. With those funds the refit went ahead and two unsuccessful attempts were made to recover the gold. The ship was finally seized for unpaid debts.

The Crown charged Baxter with having had signed a registered prospectus which included an untrue statement and which was distributed. The untrue statement Baxter was said to have made was the statement required by clause 40 of the First Schedule of the Securities Regulations (“the clause 40 statement”). This clause requires a director to state that there are no “material matters” not already disclosed in the prospectus, when in fact in the \textit{Baxter} case there were three undisclosed material matters. These matters were that the prospectus omitted to refer to the fact that prior to the distribution of the prospectus over $234,500.00 which had been raised from those investors had already been spent by Baxter on refitting his boat, purchasing equipment, personal expenditure and wages, that the prospectus implied that “almost all the funds raised from the shares issued would be applied to the actual conduct of

\textsuperscript{107} Ibid.  
\textsuperscript{108} \textit{R v Baxter} [1998] 3 NZLR 144.
the salvage expedition”, and the prospectus omitted to refer to the fact that as 27 June 1995 the ship did not meet deep sea survey requirements and did not have the required certification for the expedition. The jury found that all three were untrue statements.

Blanchard J giving the judgment for the Court in upholding the convictions, stated that:

The failure to mention that the Seafarer was still undergoing a refit and had not, only a few days before the commencement of the critical weather period of July/August obtained a deep sea certificate, was so obviously a material omission. The conviction almost seems to have been inevitable. That piece of information was one which the recipients of the prospectus certainly needed in order properly to be able to assess the risk of the investment. It was also going to be a highly speculative and hazardous investment. The investors understood that. But they also knew that the exploration licence would be expiring at the end of September and that there was a critical weather period. The risks relating to weather, expiry of exploration licence, the location of the wreck, the gold and the ownership of the gold were set out in the document. But there was a striking absence of any mention that on 27 June the vessel was not ready and, indeed, still at Westport. Mr Atkinson would attribute the unreadiness of the Seafarer until well into August to problems with electrical systems which emerged after 27 June. We are prepared to assume that it is debatable whether Mr Baxter was aware of them when he signed and registered the prospectus. However, he certainly knew that there was no marine certificate and still work to be done to obtain it. It was not necessary for the Crown to show that he acted dishonestly, merely that putting his signature to a statement that there were no other material matters, he was making an untrue statement. It was for him to prove that the statement was immaterial or that he had reasonable grounds to believe that it was true (s58 (4)) and the jury was fully entitled to find that he had not done so. In our view it was open to them to make such findings also in relation to the other statement specified in particulars. The inaccuracies and omissions in them were important and glaring.109

Blanchard J’s assessment of the materiality of the information was that it was information that "recipients of the prospectus certainly needed in order properly to be able to assess the risk of the investment”. This statement supports the view that the information needed to be such that it "would" be taken into account, which is consistent with Cooke J’s view in Coleman v. Myers, but that it is not necessary that the information is decisive or determinative in that process. It perhaps also indicates that information needed to assess the risks of an investment is by its nature material. At the end of the passage quoted above Blanchard J pointed out that the “accuracies and omissions were important and glaring” which is also consistent with Callaghan J’s view of materiality as a matter which of important or consequence. Accordingly, the test, however expressed, requires the court to take the standpoint of the
reasonable investor and assess the value of the information to the investor’s decision-making process.

Materiality and Financial Statements

The New Zealand Society of Accountants (“NZSA”) has also considered the issue of “materiality” in the context of financial statements. Their view is helpful as financial statements have to be included in prospectuses where an entity has already been in business, and have to be audited.\(^\text{110}\)

The Statement of Standard Accounting Practice No. 6 (SSAP6), “Materiality in Financial Statement” establishes the criteria for applying the materiality test to information for inclusion in the external financial statements of any reporting entity.\(^\text{111}\) It provides that:

> A statement, fact, or item is material if, given full consideration of the surrounding circumstances at the time of completion of the financial statements, it is of such a nature that its disclosure, or the method of treating it, would be likely to influence the making of decisions by the users of the financial statements.\(^\text{112}\)

This definition would appear to go beyond that established in the cases. It requires the item to “influence the making of decisions” whereas the New Zealand cases only require the item to be relevant to the investment decision or such that it would be taken into account by a reasonable investor.

SSAP6 also sets out factors which may assist in determining materiality. These include the surrounding circumstances, the likely users of the particular financial statements, and the information needs of those users, its nature and its amount.\(^\text{113}\) It suggests as guidelines that a variation in amount by more than 10 per cent is material (unless there is contrary evidence), a variation less than 5 per cent is immaterial, and that a variation between 5 per cent and 10 per cent “is a matter of judgment and depends upon the particular circumstances of the case.”\(^\text{114}\)

This is helpful for items that can be quantified (although SSAP6 points out that these

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\(^{109}\) Id., 157.
\(^{110}\) Clauses 23 and 42, First Schedule.
\(^{111}\) SSAP6, para 1.1.
\(^{112}\) SSAP6, para 3.1.
\(^{113}\) SSAP6, paragraphs 31, 43 and 44.
\(^{114}\) SSAP6, Appendix.
percentages are not “magic numbers”), but obviously do not help for non-quantifiable matters such as whether or not the past business record of a director should be disclosed (for example, a bankruptcy twenty years ago).

Summary

In summary, the courts in determining whether information that has not been disclosed is material have, with the exception of *Witehira*, focused on whether a *reasonable* investor would take into account that information in making an investment decision, although the information does not have to be decisive in making that decision. The failure to make any mention of an otherwise material matter will not save a director from making an untrue statement because of the requirement for the directors to make a clause 40 statement in the prospectus.

In New Zealand, matters which have been considered material include: the market value of assets as compared to book values (*Coleman v Myers*), the fate of companies (liquidations, receiverships) for which a director of an issuer had been a director (*Power NZ*), the placement and timing of investments (*Rada*), the level of fees paid to a director/promoter (*Heenan*), the use of funds by a promoter, the state of preparations for a venture and the risks involved in a venture (*Baxter*), the valuation of assets (*Agricola* and *Sovereign Mines*), the existence of contrary valuations (*Agricola*), and the prior relationship of an issuer with a valuer (*Agricola*). As already noted, however, at the end of the day the application of the materiality test is highly case specific (and perhaps even court specific).

In the United States, matters such as the failure to disclose advanced negotiations for a merger, but not preliminary negotiations, the failure to disclose a substantial dividend reduction, the significant understatement of assets value, a substantial overstatement of revenue, and a mineral find by an exploration company have been considered material in the context of takeovers. For public offerings inadequate disclosure of potential tax and environmental liability have been held to be material, as was the failure to disclose that underwriters could purchase out of an offering.
12.2.2 Criminal Liability for Offering, Distributing, or Allotting in Contravention of the Act

Criminal liability is imposed by s. 59(1) of the 78 Act upon the following persons if an offer of a security is made, a registered prospectus is distributed or a security is allotted in contravention of the Act:

- the issuer and each of its principal officers
- every promoter of the security
- every person who with his or her authority is named in an advertisement or registered prospectus as a director of the issuer.

Penalty: A fine not exceeding $300,000 on summary conviction.

Defences: Conviction may be avoided where the Court finds that the contravention was immaterial or should reasonably be excused. In the case of a person other than the issuer, it is a defence that the contravention did not take place with his knowledge or consent.

Section 59 of the 78 Act was considered in van Niewkoop v Registrar of Companies [2005] 1 NZLR 796.

12.2.3 Other Offences under the 78 Act

Section 59A imposes criminal liability for obstructing the exercise of the powers of the NZSC.

Where an offence is not otherwise specified in the 78 Act, section 60 applies.

First, section 60(1) states that every person commits an offence who contravenes any provision of the following sections of the 78 Act: sections 35, 47, 50, 51, 52, 54 and 67 (5).

On summary conviction for these offences, a fine not exceeding $5,000 may be imposed.

Under section 60(2) of the Act, a fine of up to $300,000 may be imposed on persons who contravene or fail to comply with the following provisions: sections 7, 37(4), 48, and 53 to 53E, 54A and 54B.

Defences to a charge under s. 60(2) arise where the Court is of the opinion that the contravention or failure to comply was in respect of immaterial matters or if the person ought
reasonably be excused. In addition, no principal officer can be convicted where the contravention took place without that person’s knowledge or consent.

12.2.4 Criminal Liability under the Securities Markets Act 1988

Criminal liability attaches to, inter alia:

- the insider conduct prohibitions: section 8F;
- false or misleading statement or information: section 11A;
- false or misleading appearance of trading: section 11D;
- failure to comply with directors’ and officers’ disclosure obligations: section 19ZD;
- failure to keep interests register: section 19ZF;
- failure to comply with substantial holding obligation: section 35BA;
- failure to keep register of substantial holdings: section 35E;
- failure by public issuer to publish information on substantial holdings: section 35H.
- holding out as registered exchange without registration: section 36A.
- operation of securities markets without registration: section 36B.
- operation of registered exchange without conduct rules: section 36G, 36P and 36Q;
- exceeding control limit on registered exchange: section 36U;
- breach of terms of authorisation of overseas exchange: section 36Z;
- offences by registered exchange in relation to continuous disclosure process obligations: section 36ZX
- holding out as futures exchange without authorisation: section 37A;
- operation of futures markets with authorisation: section 37B;
• authorisation of persons dealing in futures contracts: section 39;

• offences in relation to investment advisers and brokers disclosure: sections 41p, 41Q, 41R and 41S;

• failure to comply with NZSC’s orders: section 42J;

• contravention of management banning order: section 43H, and,

• contravention of investment adviser or broker banning order: section 43M

A new Part 5, Subpart 4 of the SMA was introduced by the Securities Markets Amendment Act 2006. It lists the criminal penalties for failure to comply with parts of the SMA

12.2.5 Crimes Act 1961

Section 65 of the Act states that nothing in the Act shall limit or diminish any liability that any person may incur under any rule of law or other enactment. Some provisions of Part X of the Crimes Act 1961 may hence be relevant. Attention is drawn to the following criminal offences under the Crimes Act, 1961: s. 246 (obtaining by false pretence); s. 250 (false statement by promoter); s. 252 (false accounting); and s. 257. Section 257 creates a criminal offence for conspiracy to defraud. The section reads, in part, “[e]very one is liable to imprisonment for a term not exceeding 5 years who conspires with any other person by deceit or falsehood or other fraudulent means ... to affect the public market price of stocks, shares ... or anything else publicly sold ...”.

E. RECENT DEVELOPMENTS

The most significant new development in New Zealand securities regulation is the use of the MOU between the Government of New Zealand and the Government of Australia on Coordination of Business Law signed in August 2000 (the 2000 MOU) as a vehicle to advance reform of New Zealand securities regulation.115 The 2000 MOU is part of the CER

115 See Jane Diplock, “Public Sector Reform in New Zealand and Australia” (30 August, 2004). Available at the NZSC website.
Agreement between New Zealand and Australia discussed earlier. The 2000 MOU was updated and re-executed on 22 February 2006.\textsuperscript{116}

Coordination in the realm of securities markets is the salient example of an area where the principles of the 2000 MOU are being actively pursued from the New Zealand end. This is confirmed in the stated policy statements of the New Zealand government.\textsuperscript{117} In July 2003, the Ministry of Commerce made explicit reference to these principles when announcing further reform to New Zealand’s securities regulation regime including the proposed reform of New Zealand’s insider trading provisions along Australian lines.\textsuperscript{118} We also see these principles directly addressed in, for example, section 19A(2)(i) of the SMA and section 24 of the \textit{Takeovers Act} 1993 (NZ).\textsuperscript{119}

In a Media Statement dated 24 July 2003, the Hon. Lianne Dalziel, then New Zealand’s Commerce Minister, announced proposals to strengthen New Zealand’s secondary market regulation.\textsuperscript{120} According to the Media Statement, a \textit{Securities Trading Law Review} and a \textit{Securities Trading Law Reform Bill} were to be released in late 2004 for comment. In the result, new legislation was introduced in February 2008. It contained:

- A new insider-trading regime similar to Australia;
- More prohibitions on market manipulation;
- Amendments to the law relating to investment advisers;
- Increased penalties for violating secondary market regulation;
- Fine-tuning of the substantial security holder disclosure regime, and,
- Improvements to the application of secondary market regulation.


\textsuperscript{117} For example, in March and May 2003, the New Zealand government stated that it was committed to further coordination of business laws of the two economies: see \textit{The Australian Financial Review}, 12 March 2003, 3; 22 May 2003, 14.


\textsuperscript{119} They are also reflected in the appointment of the Australian commercial lawyer, Dennis Byrne, to the Takeovers Panel and of Australian Jane Diplock, AO, as Chairman of the Securities Commission. (Prior to her appointment to the Securities Commission, Jane Diplock was the Australian Investments and Securities Commission’s (ASIC) National Director Infrastructure and Strategic Planning and New South Wales Regional Commissioner).

\textsuperscript{120} Hon. Lianne Dalziel, op.cit
The Media Statement contains a hyperlink through to the website of the Ministry of Economic Development where the Cabinet papers relating to these proposals are cached.\textsuperscript{121} The substantive documents\textsuperscript{122} are prefaced by an overview document entitled, \textit{Review of Securities Trading Law}. The overview document and the Cabinet Paper entitled, \textit{Review of Securities Trading Law: Overview and Application Issues} by the Hon. Lianne Dalziel provide us with a clear view of the New Zealand government’s overall plan for securities regulation reform.

It is plain that the Labour Party led coalition government in New Zealand has embarked on the most comprehensive reform of securities regulation in over a decade. The four-step reform agenda presents a striking contrast to the inaction of the National government in this area during the 1990s.

The key document is Hon. Lianne Dalziel, \textit{Review of Securities Trading Law: Overview and Application Issues}\textsuperscript{123} addressed to the Chair of the Cabinet Economic Review Committee. Part of this document states as follows:

The government has identified as one of its key objectives promoting confidence in the New Zealand market. This objective involves strengthening the regulatory framework in order to encourage investment and enhance the performance of the New Zealand market. In order to achieve this objective a four-step programme of reform relating to securities law has been developed and has been in progress since 2000. This includes:

\textit{The introduction of the Takeovers Code:} The Takeovers Code was implemented on 1 July 2001. The intention of the Code is to align our takeovers regime with international best practice, at the same time giving greater confidence to small and minority investors by providing them with fair and equal treatment and participation in takeover situations;

\textit{The Securities Markets and Institutions Bill:} The Securities Amendment Act 2002 and the \textit{Securities Markets Amendment Act} 2002 were passed on 1 December 2002 (these acts were the result of the Securities Markets and Institutions Bill). The purpose of the legislation was to promote confidence in the New Zealand market by increasing the effectiveness and efficiency of the law and regulatory

\textsuperscript{121} See \url{www.med.govt.nz/buslet/bus_pol/bus_law/securities/index.html} for downloadable copies of all documents.

\textsuperscript{122} Cabinet Papers; Regulatory Impact and Business Compliance Cost Statements; Discussion Documents and Media Statements.

institutions governing securities markets and aligning the law with international best practice;

The Review of Securities Trading Law [this refers to the three volumes of discussion documents on insider trading, market manipulation and penalties available at the Ministry of Economic Development website] and,

The Review of the Securities Act 1978 and other issues: The substantive work on this review will be undertaken after the Review of Securities Trading Law is completed. The review will consider possible changes to the regulation of securities offerings, whether there should be licensing of financial intermediaries, reviews of the Unit Trusts Act and the provisions relating to contributory mortgages and other security law issues that are necessary to achieve a consistent and cohesive package of securities laws.124

As of September 2008, we are at the end of the third step of the reform programme.

The overt policy rationales for reforming securities regulation in New Zealand appear in the paragraph quoted above. Generally, however, they can be reduced to one overarching rationale – investor protection. The precise detail or shape of reform is best explained by an increasing New Zealand focus on the principles of the 2000 (now 2006) MOU. These desiderata are confirmed by recent reports of the policy position of the New Zealand government.125

Thus, the New Zealand Exchange (NZX) has adopted a continuous disclosure regime that closely resembles Australia.126 The most striking example of this trend, however, is the introduction of an insider-trading regime127 and market manipulation provisions that follow the Australian position.

125 The New Zealand Minister of Finance, Hon. Michael Cullen, has stated that, as far as possible, common regulatory systems as between New Zealand and Australia are desirable: see David Bassanese, “Living History” The Australian Financial Review, 21 July 2003, 52; A. Wood, “To CER, with Love”, The Weekend Australian, March 15-16, 2003, 29. Australia is the largest investor in New Zealand and Australia is the second largest destination for New Zealand investment. Total bilateral trade between Australia and New Zealand in 2002 was over $A16.2 billion: The Australian Financial Review, 21 February 2003, 12.
127 See Hon. Lianne Dalziel, Review of Securities Trading Law: Insider Trading (Office of the Minister of Commerce, File No: RCP 3.3.4.4) addressed to the Chair of the Cabinet Economic Review Committee. Para 13 of this document states that, ‘[T]he proposed insider trading regime is similar to that in the Australian Corporations Act 2001 … The introduction of the insider trading regime would contribute to
The 2000 MOU talks about achieving greater compatibility in disclosure regimes in relation to financial products (the latter terminology anticipated the passage of the Financial Services Reform Act in 2001 in Australia.). This may occur in the fourth step of securities regulation reform. It is important, however, to appreciate that New Zealand and Australia have fundraising regimes that diverge in significant respects.

First, in New Zealand, section 33 of the 78 Act prohibits the offering of a security ‘to the public’ in the absence of a registered prospectus or an investment statement. Australia, however, has abandoned the ‘offer to the public’ requirement. Thus, section 706 appearing in Chapter 6D of the Corporations Act 2001 (Cth.) states that an offer of securities for issue needs disclosure unless section 708 says otherwise. In this way, Australian law establishes a ‘bright line rule’.

By contrast, New Zealand excluded offers as contained in section 3 (2) of the 78 Act (broadly, the types of offers contemplated in section 708 of the Corporations Act 2001) may be susceptible to subsequent challenge as constituting a public offer and hence requiring registration.128

Second, the prospectus content rules differ. In New Zealand, a registered prospectus requires the information prescribed in the Securities Regulations 1983. In Australia, the general disclosure test that applies to most prospectuses is set out in section 710 of the Corporations Act 2001 (Cth.). It states that a prospectus issued in connection with an offer of securities for subscription must include all the information that investors and their professional advisers would reasonably require to make an informed assessment of (a) the rights and liabilities attaching to the securities and (b) the assets and liabilities, financial position and performance, profits and losses and prospects of the company.

The requisite information must be included to the extent that it is reasonable for investors and their professional advisers to expect to finds the information in the prospectus and only if the relevant person actually knows the information or in the circumstances ought reasonable to

have obtained the information by making enquiries. The latter requirement imposes a due diligence obligation.

It is immediately apparent that the disclosure obligations imposed under Australian law are more onerous than the New Zealand equivalent. In turn, this raises questions about mutual recognition of registered prospectuses where disclosure standards are lower in one jurisdiction than in the other.

The solution appears obvious: New Zealand should abandon the ‘offer to the public’ test for prospectus registration and follow the Australian practice. It is notorious that section 3 of the 78 Act has been an unmitigated disaster and is long overdue for consignment to the boneyard. (Hong Kong, Malaysia and Singapore have all abandoned the concept).

Similarly, New Zealand prospectus content requirements should be aligned with Australia. The 2003 Dalziel and Coonan Joint Statement indicated that Australian and New Zealand officials had reached preliminary agreement on detailed proposals for mutual recognition of securities offerings. Prima facie, this was puzzling since – as we have seen - there are long-standing pre-existing arrangements for mutual recognition of securities offerings. This proposal, however, extends existing arrangements. The Joint Statement elaborates:

- Under these proposals an issuer should be able to offer securities in both countries using a single disclosure document that satisfies the requirements of the home country and investors should be able to take action in the courts of either country;
- Legislation will be required to implement the proposal in Australia and regulations will be required in New Zealand, and,
- A joint discussion paper will be issued by 30 November 2003 and a finalised proposal should be ready by 30 June 2004.

New Zealand has established a mechanism to effect this proposal via legislation as a result of the Securities Act Amendment Act 2002 (NZ). It introduced, amongst other things, a new Part 5, Subparts 1-4 to the Securities Act 1978 (NZ). The purposes of the new Part 5 are fully stated in section 71 of the Act. However, one key purpose is to introduce recognition and application regimes that provide for exemptions from Part 2 of the 78 Act and Regulations so

that foreign issuers may offer securities in New Zealand in accordance with the laws of their home countries.  


In brief, the proposal was that the fundraising laws of the home jurisdiction will apply to offers made to investors in the host jurisdiction. In addition, however, parts of the law of the host jurisdiction also apply. The way this scheme will operate can be illustrated by considering a prospectus offering in Australia.

- First, the Australian prospectus must comply with all applicable Australian laws (i.e., it must be a “regulated offer” in the home jurisdiction).
- Second, the Australian issuer opts in to the New Zealand mutual recognition regime by filing a notice that contains prescribed information in relation to the offer and the offeror with the Securities Commission in New Zealand.
- Third, the Australian issuer undertakes to comply with the ongoing requirements of the mutual recognition regime. These will include conditions that the issuer will comply with Australian law and any ongoing requirements imposed by New Zealand. An issuer in breach of these ongoing requirements may be subject to suit by the Securities Commission in New Zealand.
- Further, an aggrieved investor may take action in either jurisdiction.

It was envisaged that the proposed arrangements would be effected by way of a treaty and such a treaty was signed on 22 February 2006. The text of the Treaty can now be viewed on the Ministry of Economic Development website. As we have seen, the mutual offering of securities regime is now operative (as of June 2008).

In domestic law, nations pursue their own interests. In the USA context, Professor James D Cox has stated:

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Incantations regarding the pre-eminence of U.S. capital markets and the rigors of its regulation are repeatedly joined as justifications for the status quo of U.S regulatory treatment of foreign issuers. Only isolated accommodations are made for foreign issuers and with the exception of Canadian issuers, all must abide by the same standards that pertain to U.S issuers.131

Leaving aside arguments for special treatment (cf., Canada and the USA) based on proximity and de facto economic integration, the main concern about the new mutual recognition regime is the extent to which Australia’s interest in the pre-eminence of its securities regime – which has higher disclosure and reporting standards than New Zealand – is eroded or compromised by recognition of lower standards in New Zealand.

Thus, it is arguable that New Zealand prospectus disclosure and related standards need to be overhauled to align with those of Australia; otherwise, Australia will be recognising a lower standard of prospectus disclosure. For example, valuation of vendor consideration in a primary public offering is treated differently in Australia than in New Zealand. Again, if reciprocal access to the courts of the host country is to occur then presumably the remedies for defective disclosure must be the same.132 In short, the logic of this proposal points in one direction: New Zealand must adopt the Australian law.133

The 2000 MOU Work Programme for Coordination of Business Law also sought to achieve greater compatibility in disclosure regimes in relation to ‘financial products’. The new regime for financial products in Australia came as a result of the Financial Services Reform

[106] James Cox, “The Death of the Securities Regulator – Globalisation”. Unpublished manuscript on file with author. In passing, I note that the reference by Professor Cox to the position of Canadian issuers is a pointer to the multi-jurisdictional disclosure system (MJDS) adopted by the Securities and Exchange Commission (SEC) in 1991, which permits eligible Canadian issuers to satisfy SEC registration and reporting requirements by filing disclosure documents that satisfy Canadian requirements. At the same time, Canada undertook changes to its securities laws to permit U. S. issuers to satisfy its laws by filing documents prepared in accordance with SEC requirements. The MJDS is presently the best analogy with the proposed Australia-New Zealand mutual recognition regime. For this reason, it deserves closer scrutiny by trans-Tasman policymakers.

[132] Consider here sections 728 and 729 of the Corporations Act, 2001 (Cth.) and compare the liability provisions under the Securities Act, 1978 (NZ). At present, there is no liability in New Zealand for a misleading or deceptive statement in a prospectus in the Securities Act. Instead, litigants rely on the section 9 of the Fair Trading Act, 1986. See, for example, Jagwar Holdings v Julian (1992) 6 NZCLC 68, 040.

[133] I may be overstating this concern. After all, in the case of reciprocal admission of lawyers, a New Zealand lawyer with no training in Australian law may be admitted in Australia. To this extent, there is a degree of ‘satisficing’ in mutual recognition of professional qualifications and query whether a similar logic will apply in the area under scrutiny.
Act (FRSA) in 2001. The immediate prospects of New Zealand aligning with the FSRA regime in Australia are remote. New Chapter 7 of the *Corporations Act* 2001 (Cth.) was introduced by the FSRA and came into full effect on March 11 2004. Chapter 7, Part 7.9 now regulates the offer and sale of ‘financial products’ other than securities.\textsuperscript{134} It requires disclosure to investors by means of a Product Disclosure Statement (PDS).

The Australian regime goes much further than the New Zealand equivalent. This is because prospectus or investment statement disclosure in New Zealand flows – generally speaking - from the definition of a ‘security’ in section 2D (1) of the *Securities Act* 1978 (NZ) and this definition is not as expansive as the definition of a financial product in section 763A (1) of the *Corporations Act* 2001 (Cth.).

More pertinently, it is unarguable that the regulatory burden imposed on industry by the FSRA in Australia is high and ongoing.\textsuperscript{135} It is unlikely that the New Zealand government would seek to impose a similar regime on the industry in New Zealand.

\textsuperscript{134} As to the definition of ‘financial product’, see Kevin Lewis, “When is a financial product not a financial product?” (2004) 22 (2) *C&SLJ*, 103.