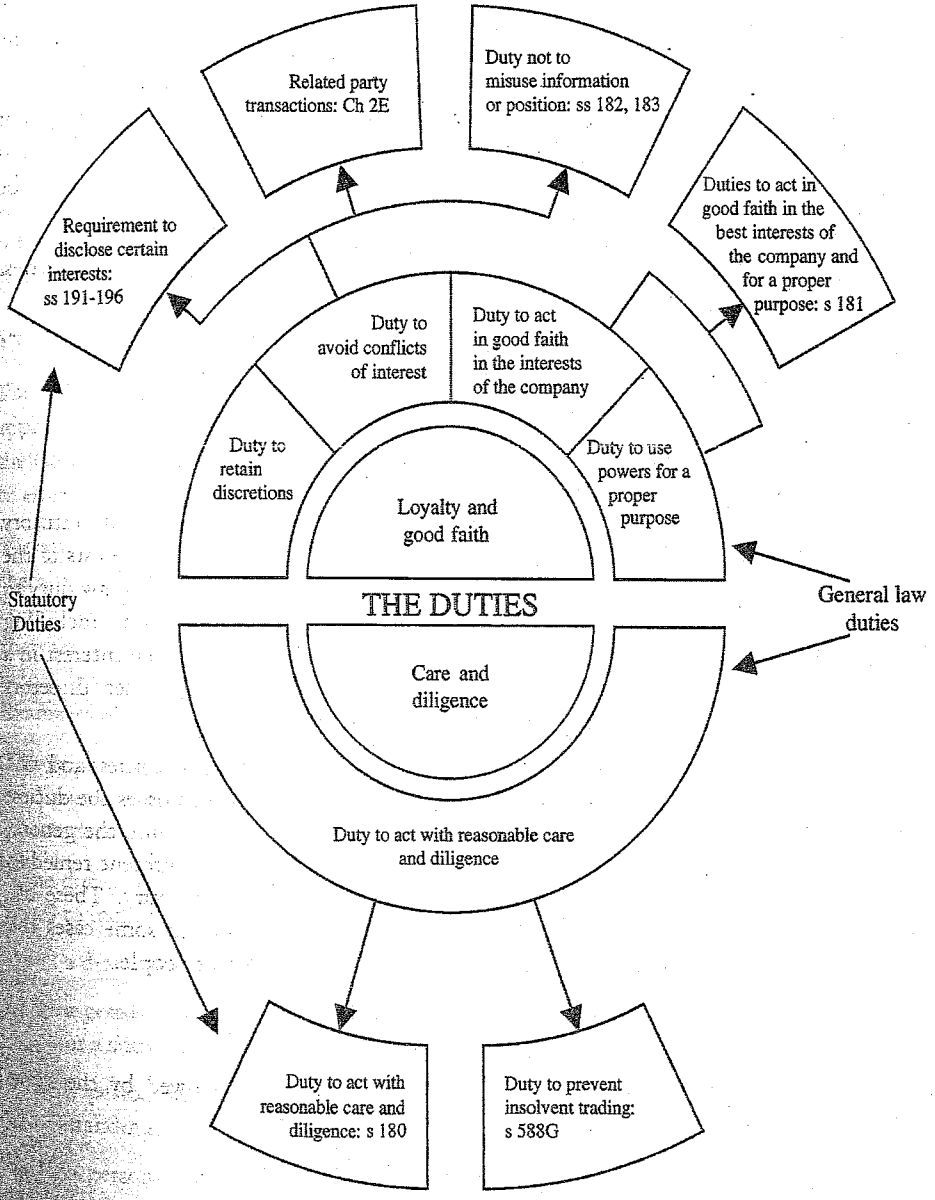
FIGURE 10.1 — CLASSIFICATION OF DUTIES



The duties can be divided into two broad categories:

- care, skill and diligence, and
- loyalty and good faith.

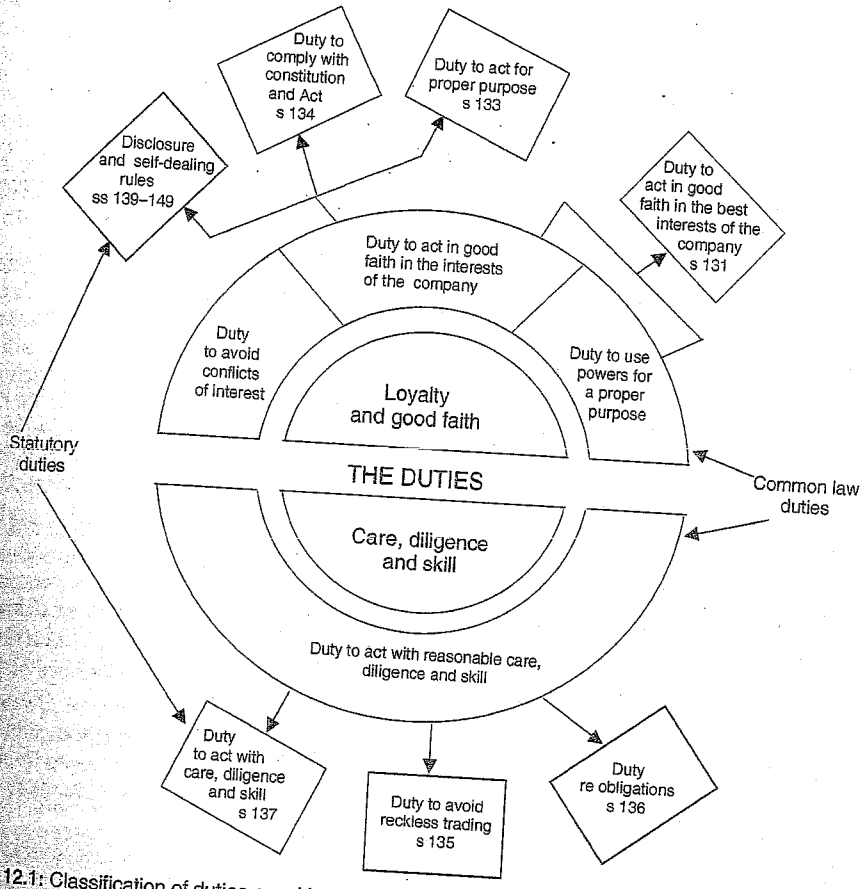


Figure 12.1: Classification of duties owed by directors

¶1204 Who owes the duties?

Common law duties

Traditionally, common law duties were owed by the following people:

- directors, and
- senior executive officers who, like directors, can be regarded as fiduciaries.

Who is a fiduciary? A ***fiduciary*** is a person who is expected to act in the interests of another person. The fiduciary cannot use his or her knowledge or position to benefit him- or herself rather than the person on whose behalf the fiduciary is required to act.

Division 2—Offers that need disclosure to investors

706 Issue offers that need disclosure

An offer of securities for issue needs disclosure to investors under this Part unless section 708 or 708AA says otherwise.

707 Sale offers that need disclosure

Only some sales need disclosure

(1) An offer of securities for sale needs disclosure to investors under this Part only if disclosure is required by subsection (2), (3) or (5).

Off-market sale by controller

(2) An offer of a body's securities for sale needs disclosure to investors under this Part if:

(a) the person making the offer controls the body; and

(b) either:

(i) the securities are not quoted; or

(ii) although the securities are quoted, they are not offered for sale in the ordinary course of trading on a relevant financial market;

and section 708 does not say otherwise.

Note: See section 50AA for when a person controls a body.

Sale amounting to indirect issue

(3) An offer of a body's securities for sale within 12 months after their issue needs disclosure to investors under this Part if:

(a) the body issued the securities without disclosure to investors under this Part; and

(b) either:

(i) the body issued the securities with the purpose of the person to whom they were issued selling or transferring the securities, or granting, issuing or transferring interests in, or options over, them; or

(ii) the person to whom the securities were issued acquired them with the purpose of selling or transferring the

securities, or granting, issuing or transferring interests in, or options over, them;

and section 708 or 708A does not say otherwise.

Note 1: Section 706 normally requires disclosure for the issue of securities. This subsection is intended to prevent avoidance of section 706. However, to establish a contravention of this subsection, the only purpose that needs to be shown is that referred to in paragraph (b).

Note 2: The issuer and the seller must both consent to the disclosure document (see section 720).

The purpose test in subsection (3)

(4) For the purposes of subsection (3):

(a) securities are taken to be:

(i) issued with the purpose referred to in subparagraph (3)(b)(i); or

(ii) acquired with the purpose referred to in subparagraph (3)(b)(ii);

if there are reasonable grounds for concluding that the securities were issued or acquired with that purpose (whether or not there may have been other purposes for the issue or acquisition); and

(b) without limiting paragraph (a), securities are taken to be:

(i) issued with the purpose referred to in subparagraph (3)(b)(i); or

(ii) acquired with the purpose referred to in subparagraph (3)(b)(ii);

if any of the securities are subsequently sold, or offered for sale, within 12 months after issue, unless it is proved that the circumstances of the issue and the subsequent sale or offer are not such as to give rise to reasonable grounds for concluding that the securities were issued or acquired with that purpose.

Sale amounting to indirect off-market sale by controller

(5) An offer of a body's securities for sale within 12 months after their sale by a person who controlled the body at the time of the sale needs disclosure to investors under this Part if:

(a) at the time of the sale by the controller either:

(i) the securities were not quoted; or

(ii) although the securities were quoted, they were not offered for sale in the ordinary course of trading on a relevant financial market on which they were quoted; and

(b) the controller sold the securities without disclosure to investors under this Part; and

(c) either:

(i) the controller sold the securities with the purpose of the person to whom they were sold selling or transferring the securities, or granting, issuing or transferring interests in, or options over, them; or

(ii) the person to whom the securities were sold acquired them with the purpose of selling or transferring the securities, or granting, issuing or transferring interests in, or options over, them;

and section 708 does not say otherwise.

Note 1: Subsection (2) normally requires disclosure for a sale by a controller. This subsection is intended to prevent avoidance of subsection (2). However, to establish a contravention of this subsection, the only purpose that needs to be shown is that referred to in paragraph (c).

Note 2: See section 50AA for when a person controls a body.

Note 3: The controller and the seller must both consent to the disclosure document (see section 720).

The purpose test in subsection (5)

(6) For the purposes of subsection (5):

(a) securities are taken to be:

(i) sold with the purpose referred to in subparagraph (5)(c)(i); or

(ii) acquired with the purpose referred to in subparagraph (5)(c)(ii);

if there are reasonable grounds for concluding that the securities were sold or acquired with that purpose (whether or not there may have been other purposes for the sale or acquisition); and

(b) without limiting paragraph (a), securities are taken to be:

(i) sold with the purpose referred to in subparagraph (5)(c)(i); or

(ii) acquired with the purpose referred to in subparagraph (5)(c)(ii);

if any of the securities are subsequently sold, or offered for sale, within 12 months after their sale by the controller, unless it is proved that the circumstances of the initial sale and the subsequent sale or offer are not such as to give rise to reasonable grounds for concluding that the securities were sold or acquired (in the initial sale) with that purpose.

708 Offers that do not need disclosure

Small scale offerings (20 issues or sales in 12 months)

(1) Personal offers of a body's securities by a person do not need disclosure to investors under this Part if:

(a) none of the offers results in a breach of the 20 investors ceiling (see subsections (3) and (4)); and

(b) none of the offers results in a breach of the $2 million ceiling (see subsections (3) and (4)).

This subsection does not apply to an offer for sale to which subsection 707(3) (sale amounting to indirect issue) or (5) (sale amounting to indirect sale by controller) applies.

Note 1: Subsection 727(4) makes it an offence to issue or transfer securities without disclosure to investors once 20 issues or transfers have occurred or $2 million has been raised.

Note 2: Under section 740 ASIC may make a determination aggregating the transactions of bodies that ASIC considers to be closely related.

(2) For the purposes of subsection (1), a personal offer is one that:

(a) may only be accepted by the person to whom it is made; and

(b) is made to a person who is likely to be interested in the offer, having regard to:

(i) previous contact between the person making the offer and that person; or

(ii) some professional or other connection between the person making the offer and that person; or

(iii) statements or actions by that person that indicate that they are interested in offers of that kind.

(3) An offer by a body to issue securities:

(a) results in a breach of the 20 investors ceiling if it results in the number of people to whom securities of the body have been issued exceeding 20 in any 12 month period; and

(b) results in a breach of the $2 million ceiling if it results in the amount raised by the body by issuing securities exceeding $2 million in any 12 month period.

(4) An offer by a person to transfer a body's securities:

(a) results in a breach of the 20 investors ceiling if it results in the number of people to whom the person sells securities of the body exceeding 20 in any 12 month period; and

(b) results in a breach of the $2 million ceiling if it results in the amount raised by the person from selling the body's securities exceeding $2 million in any 12 month period.

(5) In counting issues and sales of the body's securities, and the amount raised from issues and sales, for the purposes of subsection (1), disregard issues and sales that result from offers that:

(a) do not need a disclosure document because of any other subsection of this section; or

(b) are not received in Australia; or

(c) are made under a disclosure document.

Note: Also see provisions on restrictions on advertising (section 734) and securities hawking provisions (Part 6D.3).

(7) In working out the amount of money raised by the body by issuing securities, include the following:

(a) the amount payable for the securities at the time when they are issued;

(b) if the securities are shares issued partly-paid—any amount payable at a future time if a call is made;

(c) if the security is an option—any amount payable on the exercise of the option;

(d) if the securities carry a right to convert the securities into other securities—any amount payable on the exercise of that right.

Sophisticated investors

(8) An offer of a body's securities does not need disclosure to investors under this Part if:

(a) the minimum amount payable for the securities on acceptance of the offer by the person to whom the offer is made is at least $500,000; or

(b) the amount payable for the securities on acceptance by the person to whom the offer is made and the amounts previously paid by the person for the body's securities of the same class that are held by the person add up to at least $500,000; or

(c) it appears from a certificate given by a qualified accountant no more than 6 months before the offer is made that the person to whom the offer is made:

(i) has net assets of at least the amount specified in regulations made for the purposes of this subparagraph; or

(ii) has a gross income for each of the last 2 financial years of at least the amount specified in regulations made for the purposes of this subparagraph a year; or

(d) the offer is made to a company or trust controlled by a person who meets the requirements of subparagraph (c)(i) or (ii).

Note 1: Section 9 defines ***qualified accountant.***

Note 2: A financial services licensee has obligations under Division 3 of Part 7.7 when providing financial advice. ASIC has a power under section 915C to suspend or cancel a licensee's licence.

(9) In calculating the amount payable, or paid, for securities for the purposes of paragraph (8)(a) or (b), disregard any amount payable, or paid, to the extent to which it is to be paid, or was paid, out of money lent by the person offering the securities or an associate.

(9A) In addition to specifying amounts for the purposes of subparagraphs (8)(c)(i) and (ii), the regulations may do either or both of the following:

(a) deal with how net assets referred to in subparagraph (8)(c)(i) are to be determined and valued, either generally or in specified circumstances;

(b) deal with how gross income referred to in subparagraph (8)(c)(ii) is to be calculated, either generally or in specified circumstances.

(9B) In determining the net assets of a person under subparagraph (8)(c)(i), the net assets of a company or trust controlled by the person may be included.

Note: ***Control*** is defined in section 50AA.

(9C) In determining the gross income of a person under subparagraph (8)(c)(ii), the gross income of a company or trust controlled by the person may be included.

Note: ***Control*** is defined in section 50AA.

(10) An offer of a body's securities does not need disclosure to investors under this Part if:

(a) the offer is made through a financial services licensee; and

(b) the licensee is satisfied on reasonable grounds that the person to whom the offer is made has previous experience in investing in securities that allows them to assess:

(i) the merits of the offer; and

(ii) the value of the securities; and

(iii) the risks involved in accepting the offer; and

(iv) their own information needs; and

(v) the adequacy of the information given by the person making the offer; and

(c) the licensee gives the person before, or at the time when, the offer is made a written statement of the licensee's reasons for being satisfied as to those matters; and

(d) the person to whom the offer is made signs a written acknowledgment before, or at the time when, the offer is made that the licensee has not given the person a disclosure document under this Part in relation to the offer.

Professional investors

(11) An offer of securities does not need disclosure to investors under this Part if it is made to:

(a) a person covered by the definition of ***professional investor*** in section 9 (except a person mentioned in paragraph (e) of the definition); or

(b) a person who has or controls gross assets of at least $10 million (including any assets held by an associate or under a trust that the person manages).

Division 3—Types of disclosure documents

709 Prospectuses, short-form prospectuses, profile statements and offer information statements

Prospectus or short-form prospectus

(1) If an offer of securities needs disclosure to investors under this Part, a prospectus must be prepared for the offer unless subsection (4) allows an offer information statement to be used instead. Under section 712, the prospectus may simply refer to material already lodged with ASIC instead of including it.

Note: See sections 710 to 713 for the contents of a prospectus.

Profile statement

(2) A profile statement for an offer may be prepared in addition to the prospectus if ASIC has approved the making of offers of that kind with a profile statement instead of a disclosure document.

Note 1: See section 714 for the contents of a profile statement.

Note 2: Subsection 729(2) provides that there is still liability to investors on the prospectus when a profile statement is used.

(3) ASIC may approve the use of profile statements for offers of securities of a particular kind. The approval may specify information to be included in the profile statement (including information about a matter referred to in paragraphs 714(1)(a) to (d)).

Offer information statement

(4) A body offering to issue securities may use an offer information statement for the offer instead of a prospectus if the amount of money to be raised by the body by issuing the securities, when added to all amounts previously raised by:

(a) the body; or

(b) a related body corporate; or

(c) an entity controlled by:

(i) a person who controls the body; or

(ii) an associate of that person;

by issuing securities under an offer information statement is $10 million or less.

Note 1: See section 715 for the contents of an offer information statement. The statement must include financial statements that are less than 6 months old.

Note 2: Under section 740, ASIC may make a determination aggregating the transactions of bodies that ASIC considers to be closely related.

(5) In working out the amount of money to be raised by a body or entity by issuing securities, include the following:

(a) the amount payable for the securities at the time when they are issued;

(b) if the securities are issued partly-paid—any amount payable at a future time if a call is made;

(c) if the securities are options—any amount payable on the exercise of the options;

(d) if the securities carry a right to convert the securities into other securities—any amount payable on the exercise of that right.

However, do not include an amount payable for securities, or payable on the exercise of options, if the securities or options are issued under an eligible employee share scheme.

Division 4—Disclosure requirements

710 Prospectus content—general disclosure test

(1) A prospectus for a body's securities must contain all the information that investors and their professional advisers would reasonably require to make an informed assessment of the matters set out in the table below. The prospectus must contain this information:

(a) only to the extent to which it is reasonable for investors and their professional advisers to expect to find the information in the prospectus; and

(b) only if a person whose knowledge is relevant (see subsection (3)):

(i) actually knows the information; or

(ii) in the circumstances ought reasonably to have obtained the information by making enquiries.

Disclosures		[operative]
	Offer	**Matters**
1	offer to issue (or transfer) shares, debentures or interests in a managed investment scheme	• the rights and liabilities attaching to the securities offered • the assets and liabilities, financial position and performance, profits and losses and prospects of the body that is to issue (or issued) the shares, debentures or interests

Section 710

Disclosures		[operative]
	Offer	**Matters**
2	offer to grant (or transfer) a legal or equitable interest in securities or grant (or transfer) an option over securities	• the rights and liabilities attaching to: - the interest or option - the underlying securities • for an option—the capacity of the person making the offer to issue or deliver the underlying securities • if the person making the offer is: - the body that issued or is to issue the underlying securities; or - a person who controls that body; the assets and liabilities, financial position and performance, profits and losses and prospects of that body • if subsection 707(3) or (5) applies to the offer—the assets and liabilities, financial position and performance, profits and losses and prospects of the body whose securities are offered

Note: Section 713 makes special provision for prospectuses for continuously quoted securities.

(2) In deciding what information should be included under subsection (1), have regard to:

(a) the nature of the securities and of the body; and

(b) if the securities are investments in a managed investment scheme—the nature of the scheme; and

(c) the matters that likely investors may reasonably be expected to know; and

(d) the fact that certain matters may reasonably be expected to be known to their professional advisers.

(3) For the purposes of this section, a person's knowledge is relevant only if they are one of the following:

(a) the person offering the securities;

(b) if the person offering the securities is a body—a director of the body;

(c) a proposed director of the body whose securities will be issued under the offer;

(d) a person named in the prospectus as an underwriter of the issue or sale;

(e) a person named in the prospectus as a a person named in the prospectus as a financial services licensee involved in the issue or sale;

(f) a person named in the prospectus with their consent as having made a statement:

(i) that is included in the prospectus; or

(ii) on which a statement made in the prospectus is based;

(g) a person named in the prospectus with their consent as having performed a particular professional or advisory function.

Note: Section 729 says who is liable for misstatements in, and omissions from, a disclosure document.

711 Prospectus content—specific disclosures

Terms and conditions of offer

(1) The prospectus must set out the terms and conditions of the offer.

Disclosure of interests and fees of certain people involved in the offer

(2) The prospectus must set out the nature and extent of the interests (if any) that each person referred to in subsection (4) holds, or held at any time during the last 2 years, in:

(a) the formation or promotion of the body; or

(b) property acquired or proposed to be acquired by the body in connection with:

(i) its formation or promotion; or

(ii) the offer of the securities; or

(c) the offer of the securities.

(3) The prospectus must set out the amount that anyone has paid or agreed to pay, or the nature and value of any benefit anyone has given or agreed to give:

(a) to a director, or proposed director, to induce them to become, or to qualify as, a director of the body; and

(b) for services provided by a person referred to in subsection (4) in connection with:
  (i) the formation or promotion of the body; or
  (ii) the offer of the securities; and
(c) if the prospectus is for interests in a managed investment scheme—to the responsible entity:
  (i) to procure acquisitions of interests in the scheme; or
  (ii) for services provided under the constitution of the scheme.

To comply with this subsection it is not sufficient merely to state in the prospectus that a person has been paid or will be paid normal, usual or standard fees.

(4) Disclosures need to be made under subsections (2) and (3) in relation to:
(a) any directors and proposed directors of the body;
(b) a person named in the prospectus as performing a function in a professional, advisory or other capacity in connection with the preparation or distribution of the prospectus;
(d) a promoter of the body;
(e) an underwriter (but not a sub-underwriter) to the issue or sale or a financial services licensee named in the prospectus as a financial services licensee involved in the issue or sale.

Quotation of securities

(5) If the prospectus for an offer of securities states or implies that the securities will be able to be traded on a financial market (whether in Australia or elsewhere), the prospectus must state that:
(a) the securities have been admitted to quotation on that financial market; or
(b) an application for admission of the securities to quotation on that financial market has been made to the operator of that market; or
(c) an application for admission of the securities to quotation on that financial market will be made to the operator of that market within 7 days after the date of the prospectus.

Note 1: Paragraph 724(1)(b) gives times within which the person should seek and obtain admission to quotation.

Note 2: Subsection 716(1) requires the prospectus to be dated.

Expiry date

(6) The prospectus must state that no securities will be issued on the basis of the prospectus after the expiry date specified in the prospectus. The expiry date must not be later than 13 months after the date of the prospectus. The expiry date of a replacement prospectus must be the same as that of the original prospectus it replaces.

Note 1: Subsection 716(1) requires the prospectus to be dated.

Note 2: Section 719 deals with replacement prospectuses.

Lodgment with ASIC

(7) The prospectus must state that:
(a) a copy of the prospectus has been lodged with ASIC; and
(b) ASIC takes no responsibility for the content of the prospectus.

Prescribed information

(8) The prospectus must set out the information required by the regulations.

712 Prospectus content—short form prospectuses

Prospectus may simply refer to material lodged with ASIC

(1) Instead of setting out information that is contained in a document that has been lodged with ASIC, a prospectus may simply refer to the document. The reference must:
(a) identify the document or the part of the document that contains the information; and
(b) inform people of their right to obtain a copy of the document (or part) under subsection (5).

(2) The reference must also include:
(a) if the information is primarily of interest to professional analysts or advisers or investors with similar specialist information needs:
(i) a description of the contents of the document (or part); and

Extract from CACL (2012)

¶19-001 Introduction

In this chapter, we continue our discussion of shares and shareholding, focusing on:

- the rules governing the issue of new shares by a company
- the capital maintenance rules, which impose restrictions on companies reducing their share capital.

INCREASING ISSUED CAPITAL

¶19-100 How are shares issued to the first shareholders?

When a company is formed, the person or people registering the company will decide on the number and classes of shares to be issued. Under s 117(2)(k) of the *Corporations Act 2001*, the application for registration of a company limited by shares must specify, among other things:

- the number and class of shares each member agrees in writing to take up
- the amount (if any) each member agrees in writing to pay for each share
- if that amount is not to be paid in full on registration — the amount (if any) each member agrees in writing to be unpaid on each share.

The shares to be taken up by the members as set out in the application are taken to be issued to the members on registration of the company: s 120(2). This is the company's initial issued capital.

The company may decide, after registration, to increase the number of shares on issue. The rules governing the increase in a company's share capital are described below.

¶19-120 What is the process for issuing new shares?

This section describes the process for issuing new shares once a company is already in existence.

Who decides whether the company will issue shares?

For existing companies, the decision to issue new shares is made, initially, by the board of directors. The directors will decide the number of new shares to be issued, the terms on which they will be issued, and the subscription price. Where the new shares are in a class of shares already on issue, member approval of the decision to issue additional shares is required only in certain limited circumstances, which are mentioned below. Where it is proposed to create a new class of shares not previously provided for in the company's constitution or otherwise, member approval of the

rights attaching to the shares, although not of the issue itself, will usually be required.[1]

How are directors' duties relevant?

In exercising their power to issue shares, directors must act in accordance with their duties owed to the company. The impact of the duties to act in good faith in the interests of the company, and to exercise powers for proper purposes, in the context of share issues is discussed at length in Chapter 12. You will recall from Chapter 15 that the exercise by the directors of the share issue power for an improper purpose may give a member a personal remedy under the principles established in *Residues Treatment & Trading Co Ltd v Southern Resources Ltd.*[2]

What other legal requirements are there?

In proposing an issue of new shares, a company needs to be aware of the restrictions imposed by law on the types of people to whom the shares can be offered. These restrictions are discussed in ¶19-240. In addition, companies and their participants and advisers must comply with the Corporations Act disclosure requirements for new share issues. These requirements are discussed in ¶19-300–¶19-320.

Who must be notified?

Within one month after a new share issue is made, the company must notify ASIC of the details of the issue in accordance with s 254X. If the company is a listed company, it must also notify ASX and, if the shares are in a class of securities that is quoted, apply for quotation of the new shares.[3]

¶19-140 What are the main types of share issues?

An offer of shares may be made privately or to the public at large. Large scale public offerings by public companies may involve many millions of dollars and hundreds of thousands of potential investors. Some of the commercial terminology used in relation to large offers is defined below.

Business people use a variety of shorthand expressions to describe different types of share issues, especially by larger public companies. It is useful to understand these expressions and the contexts in which they are used. Among the most common are the following.

1 If the rights attaching to the new shares are to be set out in the constitution, a special resolution will be required to amend the constitution. Where it is not proposed to amend the constitution, member approval will be required if the issue amounts to a variation of the class rights of the existing members — see Chapter 6.

2 (1988) 6 ACLC 913; 14 ACLR 375.

3 ASX Listing Rule 2.4.

- ***Initial public offering*** or ***new float***. These expressions are usually used to describe a new issue of shares (or sale of existing shares) on a large, public scale, generally coinciding with an application to list the company on ASX.
- ***Private placement.*** This refers to the issue of a large parcel of shares to a small number of investors, generally professional investors like financial institutions or venture capitalists. Often the placement will be made at a slight discount to the current market price of the shares (that is, the subscription price is lower than the current market price).
- ***Rights issues.*** A rights issue is an issue of shares made to the company's existing members pro rata[4] to their shareholding at the time of the offer. Again, rights issues are usually priced at a slight discount to the current market price of the shares. The issue may be ***renounceable***, which means the investor who receives the offer can sell the right to subscribe for shares contained in the offer, or ***non-renounceable***, which means the investor must exercise the right itself or the right will lapse. In listed companies, renounceable rights themselves (which represent a valuable contractual entitlement to subscribe for shares at a discount to the current market price) may be separately listed and traded on ASX.
- ***Dividend reinvestment plans.*** Some companies allow their members to elect to receive their dividends in the form of additional shares in the company, rather than in cash. This is referred to as a dividend reinvestment plan. Again, the new shares are generally issued at a slight discount to the current market price.
- ***Bonus issues.*** Bonus issues are generally issues of shares that involve capitalisation of some of the company's profits. Shares are issued to existing members pro rata to their shareholding, without requiring any payment by the member.[5]

The ways in which Australian listed companies have made new share issues over recent years are summarised in Table 19.1.

TABLE 19.1 — EQUITY CAPITAL RAISING BY TYPE ($ BILLION)

ASX Capital Raising	FY2011 ($B)	FY2010 ($B)
Primary Raisings	–	–
IPOs	29.4	11.5
Secondary Raisings	–	–
Rights issues	7.4	23.2
Placements and SPPs	16.3	28.6

4 "Pro rata" means in proportion. Assume a company has issued ordinary share capital of $100, made up of 10 shares issued at $10 each. A owns seven of these shares and B owns three. If there is only $10 left for the ordinary shareholders when the company is wound up, A would receive $7 and B would receive $3.

5 Bonus issues are provided for under s 254A(1)(a) and 254S.

ASX Capital Raising	FY2011 ($B)	FY2010 ($B)
DRPs	7.8	10.2
Calls	0.1	0.7
Options	0.3	0.1
Prospectus	0.1	0.0
Staff share plans	1.9	2.3
Total raisings	63.1	76.5
Other capital changes	–	–
Share repurchases	–23.2	–3.3

Source: www.asx.com.au/documents/resources/australian_cash_equity_market.pdf.

¶19-160 What is underwriting?

Many large share issues made by public companies are "underwritten". In an underwriting agreement, the underwriter (or group of underwriters) agrees to subscribe for (or "take up") any shares offered by the company that are not subscribed for by other people during the offering. Usually, the underwriter will be a stockbroking firm or financial intermediary. In return for this promise (which effectively guarantees the success of the offer), the underwriter will be paid a fee by the company. The amount of the fee will depend on the assessment by the parties of the risk that the offer will be under-subscribed.

Underwriters will attempt to transfer part of their risk by contracting with sub-underwriters to take up some of the shares that the underwriter has agreed to take. Again, the sub-underwriters will be paid a fee by the underwriter for making this commitment.

LEGAL RULES GOVERNING SHARE ISSUES

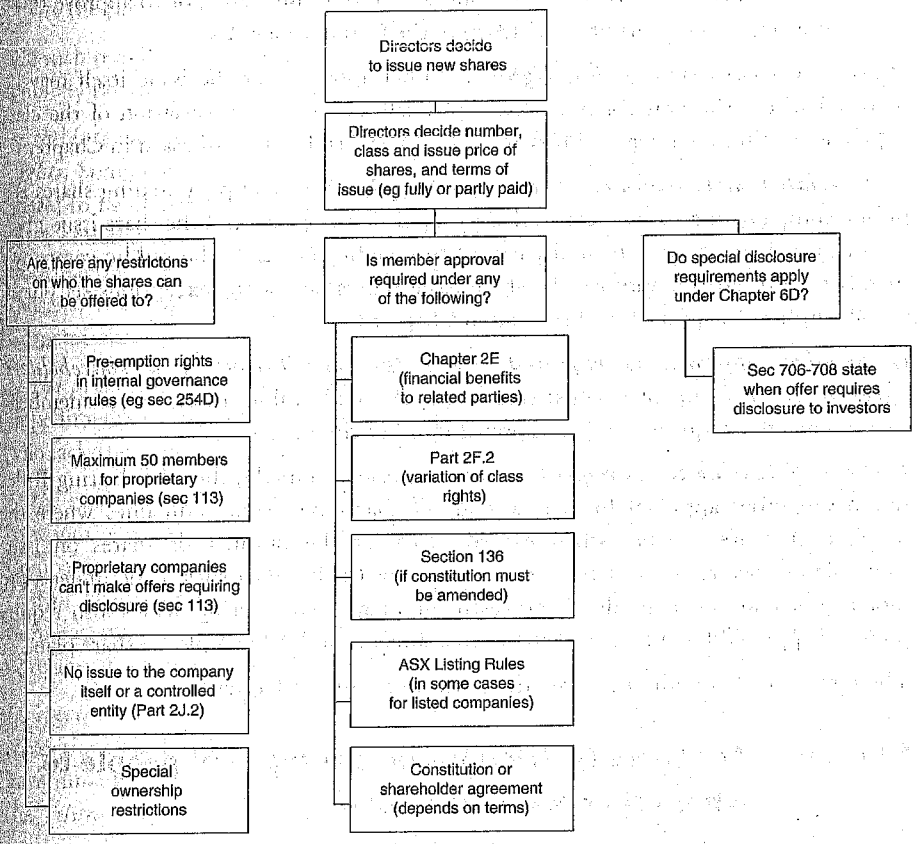
¶19-200 Overview

We saw in Chapters 10–13 that, in exercising their share issue power, directors must act in good faith in the interests of the company and for proper purposes, with reasonable care and without conflict. Having properly decided to make a share issue, the board of directors of the company must then establish whether:

- member approval of the proposed issue is required
- there are any restrictions on the people to whom the shares can be offered
- the disclosure requirements in Ch 6D of the Corporations Act apply.

These matters are summarised in Figure 19.2.

FIGURE 19.2 — ISSUING NEW SHARES



¶19-220 When is member approval required?

Generally, the power to issue new shares belongs to the company's board of directors. We saw in Chapter 5 that the directors generally have the power to manage or oversee the management of the company's business and exercise all the company's powers except those expressly given to the members in general meeting.[6] The power to issue shares is a power of the company exercisable by the board of directors. Member approval for the issue of new shares is generally not required.

However, in the following exceptional circumstances, member approval for a new issue of shares may be required.

If creating a new class of shares requires amending the constitution. The creation of a new class of shares may require member approval to amend the company's constitution to set out the rights attaching to the shares. If the new issue is an issue of preference shares where the rights attaching to the new preference shares are not set

6 See, for example, the replaceable rule in s 198A. Article 66 of the old Table A articles of association is similar. The powers given to the members in general meeting are discussed in detail in Chapter 6.

out in the company's constitution, a special resolution of members will be required either to amend the constitution to set out certain of those rights, or to approve those rights (but not the issue itself): s 254A(2) of the Corporations Act.[7]

If there is a variation of class rights. Member approval for the issue itself may be required where the issue of new shares of itself amounts to a variation of the class rights of existing members: s 246B and 246C. Class rights are discussed in Chapter 6.

If the related party transactions provisions apply. If the company issuing shares is a public company or an entity controlled by a public company, and the share issue gives a "financial benefit" to a related party of the public company, the public company's members will have to approve the share issue unless one of the exceptions set out in Ch 2E applies. Chapter 2E is discussed in Chapter 6.

If member approval is required under the constitution or a shareholders' agreement. A company's constitution or the replaceable rules, or a members' agreement, may require member approval in other circumstances.[8]

If the ASX Listing Rules require member approval. Finally, the ASX Listing Rules require member approval for a new issue of shares by listed companies where the number of shares to be issued exceeds 15% of the number of shares on issue immediately before, subject to certain exceptions (including issues made under a pro rata rights issue or a dividend reinvestment plan).[9] The Listing Rules also require member approval for the issue of shares to a director under an employee share plan.[10]

The Listing Rule requirements are discussed in detail in Chapter 6.

¶19-240 Are there restrictions on the types of people to whom shares can be issued?

Company law imposes certain restrictions on the types of people to whom shares can be issued. These restrictions are described below.

If the company is a proprietary company. We saw in Chapters 2 and 3 that an important restriction applies to proprietary companies proposing to issue new shares. Section 113(3) of the Corporations Act says that a proprietary company must not engage in any activity that would require disclosure to investors under Ch 6D, except for the offer of its shares to existing members of the company or employees of the company or a subsidiary of the company. In practice, this limits the classes of people to whom proprietary companies can offer their shares to existing members, employees

7 The Corporations Act does not define what constitutes a "preference share" for the purposes of this section. The Explanatory Memorandum to the Company Law Review Bill 1997 states that "a preference share is a share that gives its holder some right or preference (for example, a guaranteed minimum dividend entitlement) not enjoyed by the holder of a share of another type", but this definition may be broader than the common law.

8 For example, the replaceable rule in s 254D requires member authorisation for the directors to make a share issue that does not reflect the pre-emption rights of existing members contained in the rule.

9 ASX Listing Rules 7.1 and 7.2. Rights issues and dividend reinvestment plans were described in ¶19-140.

10 ASX Listing Rule 10.14.

and certain professional or sophisticated investors. A proprietary company cannot invite the public to subscribe for shares.

No such restrictions apply to public companies, which are allowed to offer their shares publicly provided they comply with the disclosure requirements described below.

If the internal governance rules or a shareholders' agreement contain pre-emption rights. Some companies have in place "pre-emption" arrangements that require new shares to be offered pro rata to the existing holders of shares in that class before they can be offered to outsiders. This mechanism is useful for protecting existing members from having their shareholding "diluted" by the issue of new shares without their consent. Pre-emption rights are included in the replaceable rules by s 254D of the Corporations Act.

If the proposed shareholder lacks legal capacity. In ¶18-320 we discussed the legal impediments to the issue of shares to people under 18 years of age and to other people who lack the legal capacity to enter into binding contracts.

If the rules against self-acquisition apply. A final restriction on the types of people to whom new shares can be offered can be found in the rules against self-acquisition. Companies are not permitted to own shares in themselves or in the entities that control them, except in certain very limited circumstances: see Pt 2J.2 of the Corporations Act. For this reason, new shares cannot be issued to the company itself or to any of its controlled entities.

If special ownership restrictions apply. In some companies, special ownership restrictions apply under other laws. These are rare and generally occur in privatised government enterprises or in companies engaged in media ownership. For example, the *Telstra Corporation Act 1995* (Cth) restricts foreign ownership of Telstra. Foreign persons collectively cannot control more than 35% of the non-Commonwealth owned Telstra shares, and individual foreign persons cannot control more than 5% of them.

DISCLOSURE IN RELATION TO SECURITIES OFFERS

¶19-300 What are the disclosure requirements?

The third matter that the directors must consider is whether Ch 6D of the Corporations Act applies to the proposed offer of shares.

A company proposing to offer new shares for subscription must comply with the extensive disclosure obligations contained in Ch 6D of the Corporations Act, except in certain limited circumstances.

Generally, a company offering new shares for subscription must provide investors with a prospectus[11] containing detailed information about the company and the shares before the investors decide to subscribe for those shares.

The Corporations Act imposes significant penalties and sanctions on companies and their directors and advisers where the prospectus requirements are not complied with. In addition, anyone who has subscribed for shares without a prospectus (where one is required) or on the basis of a defective prospectus may be entitled to substantial civil remedies.

¶19-320 When is disclosure required?

Disclosure must be provided to investors in connection with an offer of shares unless that requirement is excluded by s 708 or 708AA of the Corporations Act. Broadly speaking, disclosure is required for all offers other than those described below.

- ***Small-scale, personal offers.*** Section 708 states that disclosure is not required if the offer is part of a small-scale, private offering that does not result in more than 20 new members subscribing for shares, or subscriptions totalling more than $2 million, in a 12-month period.
- ***Offers to sophisticated investors.*** Disclosure is not required if the offer is made to a sophisticated investor. Section 708 treats an offer that involves subscribing at least $500,000 as being an offer to a sophisticated investor. Also, a person who has net assets of $2.5 million or a gross annual income of at least $250,000 is treated as sophisticated. Finally, s 708 treats offers made through licensed dealers to persons whom they reasonably believe to be sophisticated as excluded, provided certain requirements are met.
- ***Offers to professional investors.*** Offers to certain professional investors including Australian Financial Services licensees acting on their own behalf, trustees of certain superannuation funds, and people with more than $10 million to invest in securities, are also excluded from the disclosure requirements.
- ***Offers to persons associated with the company.*** Disclosure is not required where the offer is made to the company's executive officers or the executive officers of a related body corporate, or certain people closely related to them.
- ***Offers under dividend reinvestment plans and bonus share plans.*** These types of offer are also excluded from the disclosure requirements.
- ***Offers for no consideration.*** Offers for the issue of shares for free are also excluded.
- ***Certain offers made in special circumstances.*** For example, offers made in connection with a takeover or a scheme of arrangement are excluded.
- ***Rights issues by listed companies.*** Certain rights issues by listed companies do not require a prospectus, because of s 708AA of the Act.

If the offer does not fall within one of these exemptions, then disclosure is required under s 706 in connection with an offer to potential investors to subscribe for new shares in a company.

A more detailed discussion of the prospectus laws is contained in Chapter 20.

intermediaries, market operators and traders) involved in securities and related markets, both primary and secondary." [1]

Chapter 6D also contains provisions regulating the conduct of the offer, to ensure that potential investors are provided with the necessary information and can consider and act on it free from inappropriate sales practices.

¶20-110 Which offers are subject to the disclosure and other requirements in Ch 6D?

We noted in ¶20-100 that Ch 6D is mainly concerned with ensuring that those who are offered company securities have sufficient information to make an informed judgment as to whether to take up the offer and subscribe for the securities.

However, not all securities offers attract the mandatory disclosure obligation. In some cases, the law leaves the offering company and the potential investor free to agree between them the amount and nature of the information required. In some cases this is because the relationship between the investor and the company is such that there is no need for compulsory disclosure. In other cases the investor is treated as sufficiently sophisticated to determine and negotiate its own information requirements. Finally, in some situations, the law recognises that the costs of extensive mandatory disclosure may outweigh the benefits, interfering with the ability of companies to raise capital efficiently.

An offer by a company to issue securities attracts the mandatory disclosure obligation unless s 708 says that disclosure is not required. Broadly speaking, disclosure is required for all primary offers of securities other than:

- small-scale, personal offers[2]
- offers to sophisticated investors[3]
- offers to professional investors[4]
- offers to those closely associated with the company[5]
- offers to existing members under dividend reinvestment plans and bonus share plans

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1 Baxt, Black and Hanrahan, *Securities and Financial Services Law* (7th edn, 2008), 1.8.

2 Personal offers are offers made to particular people rather than to the world at large. An offer is considered small scale if it falls under the 20 investors/$2 million threshold. An offer falls outside this threshold if it results in securities being issued to more than 20 people, or in the company raising more than $2 million by issuing securities, in a 12-month period.

3 Section 708 treats some experienced or wealthy investors as sophisticated. If the offer requires a person to subscribe at least $500,000, or takes a person's total investment in those particular securities to $500,000, the person is treated as sophisticated. A person is also treated as sophisticated if an accountant has certified that they have net assets of at least $2.5 million or a gross income of over $250,000. Finally, established clients of securities dealers can be treated as sophisticated, where the dealer is satisfied that the client understands what they are doing and certain other requirements are met.

4 For these purposes, professional investors include insurance companies and some other financial institutions, securities licensees acting on their own behalf, trustees of larger superannuation funds, and those with at least $10 million to invest in securities.

5 Offers to executive officers of the company or its related bodies corporate, and certain of their close associates, are covered by this category.

- offers involving no consideration
- offers made in circumstances where disclosure is already provided to investors under other laws, for example in connection with a takeover or scheme of arrangement.[6]

In addition to prescribing the information to be included in the disclosure document (see ¶20-120), Ch 6D regulates the procedure for offering securities in circumstances where the offer does not fall within one of these exempt categories. The offering process is described in ¶20-140.

Section 727 prohibits a person from conducting a securities offer that requires disclosure under Ch 6D, unless the required disclosure document has been prepared and lodged with ASIC.

¶20-120 What must be disclosed?

If an offer by a company to issue securities does not come within one of the categories of exempt offers set out in s 708 of the Corporations Act, the disclosure obligation in s 706 is triggered.

Depending on the size or nature of the offer, the issuing company will be required to prepare:

- a prospectus, or
- an offer information statement.[7]

An offer information statement (OIS) is a more limited form of disclosure document than a prospectus. A company is allowed to use an OIS, rather than a prospectus, if the amount of capital to be raised by the company through the issue, when added to all amounts previously raised by that company and certain entities connected with it under OISs, does not exceed $10 million: s 709(4). OISs were introduced into the securities laws in March 2000 in an attempt to make it easier for SMEs to raise (relatively) small amounts of start-up capital without having to prepare a full prospectus.

What must be included in a prospectus?

Section 710 contains a general disclosure requirement that applies to most prospectuses. 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 in order to make an informed assessment of:

- the rights and liabilities attaching to the securities
- the assets and liabilities, financial position and performance, profits and losses and prospects of the company.

6 For a detailed discussion of the exemptions, see Baxt, Ramsay, Renard, Simkiss and Webster, *"CLERP" Explained* (CCH 2000), ¶4-200.

7 Chapter 6D also allows a third kind of disclosure document — a profile statement. However, at the time of writing profile statements may only be used for certain offers of interests in managed investment schemes, and not for offers of company shares and debentures. Therefore we do not deal with profile statements in this book.

The information must be included only to the extent that it is reasonable for investors and their professional advisers to expect to find the information in the prospectus, and only if a relevant person[8] actually knows the information or in the circumstances ought reasonably to have obtained the information by making enquiries.

The requirement that the prospectus include information that the company, its directors and advisers *ought* to know (as well as what they actually know) places an obligation on the people preparing the prospectus to undertake reasonable enquiries to find out and verify any relevant information. This is often done by a process known as "due diligence". An issuer company may form a due diligence committee comprising directors, management and advisers to review the available information (internal and external) about the company and make sure that the prospectus is complete and correct. In addition to helping to ensure the prospectus meets the content requirements in s 710, this due diligence process can also be important in establishing defences to liability for defective disclosure (see ¶20-160).

A prospectus must also include certain specific items of information, under s 711. These include information about the terms and conditions of the offer, and disclosure of the interests of, and fees payable to, certain people involved with the offer.

The information in a prospectus must be worded and presented in a clear, concise and effective manner: s 715A.

What is a short form prospectus?

The issuing company is not required to reproduce in the prospectus information that has been lodged with ASIC, such as financial reports previously lodged with ASIC under Ch 2M. Instead, the prospectus can refer to this information, and describe the document in which it appears. People can then request a copy of the document if they wish to see it.

A disclosure document that incorporates material lodged with ASIC in this way is called a short form prospectus. The information included in the prospectus, together with the information lodged with ASIC, must together be sufficient to satisfy the content requirement in s 710.

What special content rules apply to further issues of quoted securities?

The general content requirement in s 710 applies to most, but not all, prospectuses. More limited disclosure requirements apply where the offer relates to continuously quoted securities (that is, securities that have been quoted on ASX for at least 12 months and have been subject to continuous disclosure requirements).[9]

For these offers the law assumes that all material information about the company and its prospects is already available in the market and is reflected in the market price of securities in that class already on issue and being traded on the ASX.

8 The company, its directors and any proposed directors, and underwriters, stockbrokers, experts and advisers named in the prospectus: s 710(3).

9 The continuous disclosure requirements are discussed in ¶16-500.

To reflect this fact, s 713 provides for a more limited disclosure requirement for these offers. It requires that the prospectus contain all the information investors and their professional advisers would reasonably require to make an informed assessment of:

- the effects of the offer on the company
- the rights and liabilities attaching to the securities.

People interested in acquiring the securities, and who want more information, have the right to request copies of the company's most recent annual and half-year financial reports and any continuous disclosure notices, under s 713.

What must be disclosed in an offer information statement?

We explained above that an OIS can be used instead of a prospectus if the offer falls within the terms of s 709(4). Broadly speaking, this allows the use of an OIS by a company to raise its first $10 million in public capital.

The contents of an OIS are prescribed by s 715. It must:

- identify the company and the nature of the securities
- describe the company's business
- describe what the funds raised are to be used for
- state the nature of the risks involved in investing in the securities
- give details of all amounts payable to acquire the securities
- state that the document has been lodged with ASIC
- state that the document is not a prospectus and has lower disclosure requirements
- state that investors should obtain professional advice
- include a copy of the company's financial report.

The OIS was introduced into the then Corporations Law in March 2000. Before that, such offers would have required a full prospectus. The OIS is intended to enable small business to raise capital without going to the (sometimes prohibitive) expense of preparing a full prospectus. However, this reduces the level of disclosure, and therefore the level of protection, for investors in these circumstances.

What if the information changes during the offer period?

We will see in ¶20-140 that a disclosure document, once prepared, must be lodged with ASIC. The company must specify the expiry date of the document, which can be up to 13 months from the date of the document: s 711(6) (prospectuses) and s 715(3) (OIS).

Sometimes the information included in a disclosure document becomes out of date during the period between lodgment and expiry, or new developments occur that should be disclosed. In this case the company must lodge a supplementary or replacement document with ASIC under s 719, that corrects the defect in the original document.

The obligation to lodge a supplementary or replacement document is triggered if the company becomes aware of any of the following (if it is materially adverse from the point of view of an investor):

- a misleading or deceptive statement in the disclosure document
- the omission of information required to be included under whichever of s 710 to 715 applies to the document, or
- a new circumstance, arising since the original disclosure document was lodged with ASIC, that would have required disclosure under whichever of s 710 to 715 applies.

Once a supplementary document is lodged, the original disclosure document as modified by it becomes the disclosure document for the offer, to be distributed to investors. If a replacement document is lodged, it becomes the disclosure document for the offer.

¶20-140 What procedure must be followed for an offer?

An offer that requires disclosure to investors must be conducted in accordance with the procedure contained in Div 5 of Pt 6D.2 of the Corporations Act. That procedure is summarised in Table 20.1.

TABLE 20.1 — SECTION 717: OVERVIEW OF PROCEDURE FOR OFFERING SECURITIES

Offering securities (disclosure documents and procedure)

	Action required	Sections	Comments and related sections
1	Prepare disclosure document, making sure that it: • sets out all the information required • does not contain any misleading or deceptive statements • is dated and that the directors consent to the disclosure document.	710 711 712 713 714 715 716	Section 728 prohibits offering securities under a disclosure document that is materially deficient. Section 729 deals with the liability for breaches of this prohibition. Sections 731, 732 and 733 set out defences.
2	Lodge the disclosure document with ASIC.	718	Section 727(3) prohibits processing applications for non-quoted securities for 7 days after the disclosure document is lodged.
3	Offer the securities, making sure that the offer and any application form is either included in or accompanies: • the disclosure document, or • a profile statement if ASIC has approved the use of a profile statement for offers of that kind.	721	Sections 727 and 728 make it an offence to: • offer securities without a disclosure document • offer securities if the disclosure document is materially deficient. Section 729(3) deals with liability on the prospectus if a profile statement is used. The securities hawking provisions (s 736) restrict the way in which the securities can be offered.

	Action required	Sections	Comments and related sections
4	If it is found that the disclosure document lodged was deficient or a significant new matter arises, either: • lodge a supplementary or replacement document under s 719, or • return money to applicants under s 724.	719 724	Section 728 prohibits making offers after becoming aware of a material deficiency in the disclosure document or a significant new matter. Section 730 requires people liable on the disclosure document to inform the person making the offer about material deficiencies and new matters.
5	Hold application money received on trust until the securities are issued or transferred or the money returned.	722	Investors may have a right to have their money returned if certain events occur (see s 724, 737 and 738).
6	Issue or transfer the securities, making sure that: • the investor used an application form distributed with the disclosure document, and • the disclosure document is current and not materially deficient, and • any minimum subscription condition has been satisfied.	723	Section 721 says which disclosure document must be distributed with the application form. Section 729 identifies the people who may be liable if: • securities are issued in response to an improper application form, or • the disclosure document is not current or is materially deficient. Sections 731, 732 and 733 provide defences for the contraventions. Section 737 provides remedies for an investor.

How are sales practices controlled?

Securities are often distributed by professionals such as stockbrokers and advisers. People who deal or advise in securities are required to hold a licence under Ch 7 of the Corporations Act and their conduct is extensively regulated under Pt 7.6 to 7.9. For example, if a broker makes a recommendation to a client about securities, that recommendation must be made in accordance with Div 3 of Pt 7.7.

Chapter 6D also regulates sales practices and advertising. Restrictions on advertising and publicity are contained in s 734. In particular, the Corporations Act is concerned with ensuring that offers are not marketed before the disclosure document is available.

Section 736 prohibits securities hawking, which involves selling securities through cold calling or door to door.

¶20-160 What if the disclosure document is wrong or incomplete?

We saw in ¶20-140 that defects in a disclosure document can be cured by the company lodging a supplementary or replacement document under s 719. But what happens when the company fails to do so, and a person subscribes for securities on the basis of a defective disclosure document?

Section 728(1) of the Corporations Act says that a person must not offer securities under a disclosure document if there is:

— 13 —

Case-study of an Initial Public Offering in New Zealand

Gordon Walker

INTRODUCTION

This chapter is a case-study of an initial public offering (IPO) of equity securities in New Zealand. An IPO is a first time offering of securities utilising the primary market, usually accompanied by a listing on the New Zealand Stock Exchange (NZSE). The case-study's origins date back to 1991 when I was searching for materials for a lecture on IPOs to my first securities regulation class at Canterbury University School of Law. The prospectus of The Mount Cavendish Gondola Company Limited (now The New Zealand Experience Limited), presented as a good candidate. Legal counsel to the issue were Buddle Findlay of Christchurch and the hand of David Stock (sometime member of the Securities Commission and master securities regulation practitioner), was evident in the technical brilliance of the prospectus. The gondola project was Christchurch-based, so the case-study had a local resonance.

Why a case-study? First, because a case-study provides a good teaching tool for law and commerce students. For example, in teaching this

subject, I deliberately conflate the commercial and legal stages of an IPO—hence, for example, the characterisation of the first two phases as "start-up" and "acquisition"—since it is my experience that students need to understand something of the commercial rationale driving an IPO and the case-study method enables the various phases of an IPO to be highlighted. Secondly, the case-study demands a practical examination of the full reach of the *Securities Act* 1978 (NZ) together with the relevant parts of the *Securities Regulations* 1983-1997.[1] Thirdly, this method requires consideration of a set of related legal issues (for example, choice of vehicle for shareholding), and, as a corollary, introduces students to the art of transaction planning for capital formation. It also provides a starting-point for more sophisticated analysis.[2]

The chapter identifies key commercial and legal phases of an IPO of equity securities in New Zealand.[3] The initial purpose was to provide a paradigm of an IPO that exhibited a close fit with contemporary practice and had explanatory, diagnostic, and heuristic properties. Pursuit of that goal required conceptual, descriptive, and analytical examination of salient elements of an IPO. The result was a five-part model made up of the following phases: start-up; acquisition; prospectus; selling the issue; and closing the issue. Each phase has distinct characteristics, profoundly influencing subsequent phases and the future life of the company. Such "billiard ball" causality implies the need for careful planning, especially in the early phases of an IPO. Although such planning properly assumes a linear sequence, it is inappropriate to assume linear causality in the execution of an IPO. One must be alive to internal, endogenous, and exogenous factors which may disrupt the planned sequence. Examples of such factors are: instability in the share register of the vendor company; the overhang on the Australian market of the Westpac rights issue in 1992, which delayed the Woolworths float until 1993; the sharemarket crash of 1987 and the "Asian crisis" of 1997-1998.

Five phases of an IPO are considered with particular reference to The Mount Cavendish Gondola Company Limited (Cavendish), a Christchurch-based public company which listed on the NZSE on 11 December 1991 and commenced trading in October 1992. Cavendish is now known as New Zealand Experience Limited following the acquisition of Rainbow's End Adventure Park in 1995.[4]

1. For an overview, see Walker and Fitzsimons, "New Zealand" in Walker (ed), *International Securities Regulation: Pacific Rim*, Vol II (Oceana, 1998) Release 98-1.
2. See *Wasabi Ranchers* (MBA Case-Studies, Canterbury University, 1995).
3. For Australia, see Earp and McGrath, *Listed Companies: Law and Market Practice* (LBC, 1996).
4. For analysis of Cavendish post-listing, see Kinnell, *The Mount Cavendish Gondola Company Limited* (LLB (Hons) thesis, Canterbury University, 1996).

The company law regime governing Cavendish was that of the *Companies Act* 1955 (NZ). In September 1993 a number of company law changes were enacted in New Zealand. The distinction between private companies, public companies and public listed companies deriving from the *Companies Act* 1955 was finally abolished by the *Companies Act* 1993 (NZ) on 30 June 1997. The only meaningful distinction for our purposes is between companies and listed companies (that is, companies listed on the NZSE). Although Cavendish was a 1991 listing, its history provides concrete and readily intelligible illustrations of each phase of an IPO.

In 1996, changes to the law relating to the offering of securities were made in New Zealand. The legislative package giving effect to the recommendations of the Working Group on Improved Investment Product and Investment Adviser Disclosure was enacted on 2 September 1996. The legislation making up the new law comprises the *Securities Amendment Act* 1996 (NZ), the *Investment Advisers (Disclosure) Act* 1996 (NZ), the *Financial Reporting Amendment (No 2) Act* 1996 (NZ), the *Superannuation Schemes Amendment Act* 1996 (NZ) and the *Unit Trusts Amendment Act* 1996 (NZ).[5] This legislation came into effect on 1 October 1997. In order to give effect to the new regime, the *Securities Regulations* 1983 were expanded and modified.[6] As far as "greenfields" IPOs of equity securities are concerned, the key changes are:

- a registered prospectus need only be provided to a security holder or prospective investor on request prior to subscription: s 54B(3) of the *Securities Act* 1978;
- securities must not be allotted unless a current investment statement has been received by the investor prior to subscription: s 37A(1)(a) of the *Securities Act* 1978.

FIVE PHASES OF AN INITIAL PUBLIC OFFERING

START-UP PHASE

The term "start-up" is used frequently in the literature on entrepreneurship and small business management. It is the generic name for the beginnings of a variety of venture types.[7] Consider the start-up

5 For comment, see Kavanagh and Dell, "Securities Law Reform in New Zealand" (1996) 11(12) JIBL 535. As to investment statements, see Ayers, "Practical Problems in Framing an Investment Statement" (1997) 3 (2) NZBLQ 82. As to the link between the *Securities Act* 1978 and the *Investment Advisers (Disclosure) Act* 1996, see Fitzsimons, "The Investment Adviser (Disclosure) Act and the Securities Act 1978: The Cornerstone Definition of 'Security'" (1997) BC & SLB 67.

6 *Securities Amendment Regulations* 1997 (SR 1997/151).

7 Vesper, *New Venture Strategies* (Prentice-Hall, 1990), pp 96-126.

phase of Cavendish. The initial concept of a gondola system operating on the Port Hills above Christchurch in the South Island of New Zealand was developed by Peter Yeoman in 1973, when he was coordinating the development of the Mount Hutt Ski Area, an international ski resort near Christchurch. Yeoman was a shareholder and director of Davis Ogilvie & Partners Limited, Engineering, Planning and Surveying Consultants of Christchurch. In 1984, Yeoman discussed the gondola concept with Richmond Paynter of Paynter Corporation Limited (Paynter), a Christchurch-based, publicly listed company with interests in timber and property development, and with Ray West, a partner in Deloitte Ross Tohmatsu, Chartered Accountants, Christchurch. These discussions led to the formation in 1985 of Payeo Developments Limited (Payeo), a private company formed under the *Companies Act* 1955 which represented the interests of Yeoman and Paynter and initiated full feasibility studies for the gondola project.

The Cavendish start-up gave rise to few problems in later phases of the flotation. This is not to say that the start-up phase was without difficulty—there were seven court hearings for planning approvals and related matters. One matter which might have caused difficulty was the refunding of planning and development costs incurred by Payeo upon the successful flotation of Cavendish: because of the length of time between start-up and flotation, significant holding costs were incurred by Payeo in respect of moneys expended. Had the holding costs been refunded in cash, they would have been taxable in the hands of Payeo. This is one reason why Payeo took reimbursement of costs in cash and shares in Cavendish. Another reason is that part of this expenditure was referable to professional services.

While Cavendish is distinguished by an absence of significant legal problems deriving from start-up, IPOs may show a high degree of what chaos theorists describe as "sensitive dependence on initial conditions", where small differences in input can quickly become large differences in output. In meteorology this translates into the so-called butterfly effect—the notion that a butterfly stirring the air today in Peking can transform into storm systems next month in New York. In Cavendish, chaos theory is apt to describe the effects flowing from the decision taken in the prospectus phase to set the minimum subscription at $5.9 million. Actual subscriptions were just above the minimum, and the resultant under-capitalisation gave rise to significant problems for the company in its first months of operations. For example, because of financial strain, foreign exchange exposure was not forward-covered, which resulted in losses of $463,000. In this way, decisions made in start-up may have a profound impact on subsequent phases of an IPO.

In New Zealand, the start-up phase leading to an IPO falls into two broad categories. First, in the government trading sector, start-up may begin with a decision to corporatise a State trading activity pursuant to

the *State-Owned Enterprises Act* 1986 (NZ). The process may culminate in full privatisation accompanied by an IPO—Telecom Corporation of New Zealand Limited (Telecom) is a good example—but this type of flotation will not be discussed here, because they are seasoned ventures, businesses with a trading history. Secondly, in the private sector, start-up emerges at some point as the business becomes progressively more established. Only a few of these start-ups will lead to an IPO and, again, these fall into two main categories. The first category comprises seasoned corporate ventures. These are companies which can refer (externally or internally) to a trading history—Fruitfed Supplies Limited which listed on the NZSE in 1992 is an example. Here, a subset is the "spin-off": the flotations of the various "Baby Brierleys" were spin-offs from Brierley Investments Limited, a large New Zealand listed multinational. The second category comprises unseasoned corporate ventures. These companies have no trading history and are called "greenfields" flotations in New Zealand. Cavendish was a greenfields IPO.

In the start-up phase of a greenfields flotation in New Zealand, a private company was the usual choice of vehicle for holding entrepreneurial shareholdings and for acquiring a particular asset or assets. The private company was principally governed by Pt VIII of the *Companies Act* 1955. From the entrepreneurial perspective, the private company under the 1955 Act had a number of attractive features. These included: limited liability; the ability to have only one, "governing" director; the requirement of two to 25 shareholders; the low degree of financial disclosure; the ability to dispense with an auditor; the low maintenance costs, and taxation benefits, such as the ability to carry losses forward. From 30 June 1997, however, all companies in New Zealand have been governed by the *Companies Act* 1993 and the private company/public company distinction is abolished. The reforms introduced by the *Companies Act* 1993 offer greater flexibility to entrepreneurs as only one shareholder and one director are required for a company.

Control questions are important in the formation of a company as an entrepreneurial vehicle. Assets may be accumulated in or around a company (Puntco), which conditionally contracts to sell those assets to another unlisted company (Floatco) when that company becomes a listed company by virtue of a successful IPO. The vendor consideration for the sale of assets in Puntco will usually comprise cash and shares in the listed company, Floatco. The quantum of shares in the listed company received by the vendor company may amount to a controlling interest in the listed company: in New Zealand, a 30 per cent shareholding generally amounts to control. This means that control of Puntco is effective control of the listed company. Control of the shareholders' meeting of Puntco will typically require control of 50.1 per cent of the issued capital. Hence, the composition of the share register of Puntco must be closely examined for potential instability. For example, a register split 49 per cent, 49 per cent, and 2 per cent is potentially unstable

because any combination of the 49 per cent and 2 per cent shareholdings will control the company and may result in a "squeeze out" of the minority. This possibility neatly illustrates the notion of "sensitive dependence on initial conditions". In the result, close examination of the register may lead to amendment of the constitution of Puntco so as to require unanimity at a shareholders' meeting and a mandatory arbitration clause. In practice, seasoned corporate ventures are less likely to strike problems deriving from the composition of the share register in start-up, since the passage of time will generally resolve such difficulties prior to flotation.

Another important issue in start-up is the mode of shareholding. From the point of view of the individual entrepreneur, mode of shareholding has an impact in two areas: bankruptcy and sale of shareholding. First, since entrepreneurial endeavour is high-risk activity, shareholdings should be made bankruptcy-remote by shielding them in a special purpose vehicle (SPV), such as a trust or a company controlled by a trust.[8] Secondly, sale of shareholding may result in a taxation liability. New Zealand does not impose capital gains tax on the sale of shares unless the vendor is in the business of buying and selling shares, profit is the dominant purpose of the acquisition, or the sale is an avoidance mechanism. But an offshore-resident, individual taxpayer might wish to hold shares via a New Zealand-resident SPV if the taxpayer's country of residence taxes capital gains and has a worldwide tax net.

ACQUISITION PHASE

Here, Puntco, entrepreneur or commercial actor contemplates the acquisition of assets and a subsequent IPO. To further define the problem, the commercial actor sees an opportunity but has insufficient cash or other assets to acquire or exploit the opportunity. One solution is resort to conditional contracts or options followed by an IPO. The attraction of the conditional contract or option is that it conserves cash but provides leverage. In essence, the commercial actor buys time to finance the acquisition and commercially exploit it. Having entered into conditional contracts or options, the commercial actor must review a variety of funding options. Broadly, these options break down to a choice between debt or equity, or a combination of debt and equity. Typically, debt is unavailable because the nature of the asset precludes debt financing or the commercial actor is unwilling to provide other security. In any event, equity financing may be the preferred funding decision since equity carries no initial servicing cost: the servicing cost comes later in the form of dividends.

8. Holmes, *Protect Your Assets* (Ross Holmes, 1996); Cotter (ed), *Offshore Trusts* (Kluwer, 1996); Brown, *Offshore Financial Services Handbook* (Gresham Books, 1996).

In countries with strong capitalist cultures, the obvious action at this point is to seek venture capital. In the United States, for example, there is a well-established, highly professional, venture capital industry.[9] In New Zealand, there is one government-sponsored fund, The Greenstone Fund, and a variety of "dating" agencies and brokers of venture capital. The Canterbury Development Corporation is a dating agency which issues a directory enabling venture capital seekers to make contact with providers.[10] These and other sources of initial funding are reviewed in the literature.[11] As to brokers, private and public merchant and investment bankers sometimes source funds for venture capitalists for a fee. In addition, there are now listed companies which specialise in investments in unlisted companies, such as Direct Capital Partners Limited. In all such contexts, a successful match or investment requires avoiding the "offer to the public" provisions of the *Securities Act* 1978.

Section 33 of the *Securities Act* prohibited the making of an "offer to the public" in the absence of an authorised advertisement that is an investment statement, or an authorised advertisement that is not an investment statement, or a registered prospectus. Formerly, s 37A(c) demanded that application forms for securities be distributed in or with a registered prospectus relating to the security. The requirement was that all investors receive the registered prospectus before subscribing for the securities. Section 54B(3), inserted by the *Securities Amendment Act* 1996, now requires that a registered prospectus need only be provided on request, but an investment statement must be received prior to allotment: see s 37A(1)(a). The policy rationale is that adequate disclosure leads to informed (but not riskless), investment choices.

Section 3 attempts to explicate the troublesome term, "offer to the public". Section 3(2) *excludes* offers made to: relatives or close business associates of the issuer; persons whose principal business is the investment of money or who habitually invest money in the course of their business; persons selected otherwise than as a member of the public; underwriters and subunderwriters; and takeover offers.[12] A commercial actor might wish to attract the *exclusion* provisions of s 3(2), when seeking moneys for a project, in order to avoid compliance and other costs associated with the preparation of a registered prospectus.

Issuance costs for IPOs are not insignificant.[13] Two types of costs are incurred in IPOs. First, the *direct costs* of the issue. These include:

9. *The Economist* (25 January 1997), p 19.
10. The e-mail address is cdc@cdc.org.nz.
11. See Fox and Walker, "Sources of Funding for Small and Medium-sized Companies in New Zealand" [1994] NZLJ 421; Austin, Fox and Hamilton, *A Study of Small and Medium Sized Business Financing in New Zealand* (Wellington: Ministry of Commerce, 1996); Walker, Francis and Fox, "Raising Finance for Small Business" [1997] NZLJ 293.
12. See chapter 12 "Public offerings of securities in New Zealand" by Peter Fitzsimons.
13. See generally, Anderson, Beard and Born, *Initial Public Offerings* (Kluwer, 1995); Fox and Walker, "Total Costs of Initial Public Offerings on the NZSE" [1995] 6 ICCLR 106.

accounting fees, brokerage and commission; legal fees; financial advisory fees; prospectus printing costs; public relations and marketing. A large proportion of these costs are *compliance costs*—the cost of complying with the Act. This is sometimes called the *net regulatory burden*. A second cost is *underpricing*. Suppose that the issue price of a share is $1 but that the opening price on listing is $1.20. The issue price of the share was underpriced by 20 cents (16.66 per cent), because the price discovery mechanism of the aftermarket (the secondary market), has shown that a share which cost $1 to the subscriber has been valued by the market at $1.20. Adding direct costs and underpricing costs produces the *total costs* of an IPO. Such data can provide a useful benchmark for those advising on IPOs. Direct costs have implications for policy makers because they indicate the cost of compliance with the securities regulation regime. The Fox and Walker (1995) study referred to above found average direct costs of 4.29 per cent of funds raised and total costs of around 15 per cent, but these results should be interpreted with caution as the sample size was small.

Why should compliance costs bother the commercial actor? Suppose, for example, that a commercial actor wishes to raise $1 million, and that this money is available from five high-net-worth individuals who could be described as close business associates or habitual investors. Suppose, further, that total costs in producing a registered prospectus amount to $100,000. Clearly, the commercial actor would seek to avoid the prospectus provisions in order to dispense with costs of $100,000. The same consideration would weigh with potential investors: $100,000 in compliance costs is $100,000 less into the transaction and this may be critical. This is a troubling cost of capital problem applicable to small raisings. What is required is an exemption for investments above, say, $250,000 where the investor has taken independent professional advice. The investor protection policy of the Act is fulfilled where the investor can protect her or his own interests.

If the s 3(2) *exclusion* provisions are unavailable, the commercial actor might wish to attract the provisions of the *Securities Act* relating to *exempt offerings*: see ss 5, 6 and 7 of the Act. Three of the principal exemptions are discussed below.

1. The most general exemption is that contained in s 5(5), which gives the NZSC a discretionary power to exempt *any* offeror from the obligation to issue a prospectus. For example, the Canterbury Development Corporation (and a number of similar bodies), have been granted an exemption pursuant to the Securities Act (Local Authority and Other Venture Capital Schemes) Exemption Notice 1997 (SR 1997/238, gazetted 30 September 1997). For overseas issuers the three significant exemption notices of general application are: the Securities Act (Australian Issuers) Exemption Notice 1997, the Securities Act (Overseas Companies) Exemption Notice 1997, and the Securities Act (Overseas Listed Issuers) Exemption Notice 1997.

2. Under s 7(1)(a), offers of securities made *only* to persons outside New Zealand are exempt from the prospectus provisions. This section is particularly useful for private transactions requiring off-shore participation. For example, suppose an entrepreneur wishes to establish a wasabi-growing operation. Japanese participation will be critical since Japan is the principal market for wasabi and access to a Japanese distribution network is best obtained via Japanese residents. The issuer, however, must comply with the relevant Japanese law. Section 7(1)(b) exempts offers to persons outside New Zealand *and* persons in New Zealand who in all the circumstances can properly be regarded as having been selected otherwise than as members of the public. Note that the latter limb of s 7(1)(b) is identical to s 3(2)(a)(iii) of the Act and the relevant case law will apply. When considering the application of s 7(1), be alert to the notice and filing requirements of s 7(2).

3. Section 6(1) *exempts* previously allotted securities. Where s 6(1) applies, the terms implied in s 6A attach to the offer. There are two exceptions. First, the exemption does not apply if the security was originally allotted with a view to its being offered for sale to the public in New Zealand (see s 6(2)) and, here, a deeming provision applies: see s 6(5). Secondly, s 6(3) applies to equity securities and is designed to attract the prospectus provisions of the Act where a holder or offeror of securities, not being the original allotter, offers the security for sale to the public in New Zealand and the original allotter advises, encourages or knowingly assists in connection with the offer or sale. Section 6(4) then goes on to create three safe harbours from s 6(3): see s 6(4)(a)-(c). These are: offers in accordance with preemptive rights under a company's constitution; sales of less than $200,000 in a twelve month period; and offers to no more than six members of the public.

The exemption in s 6(4)(c) may well extend beyond a mere six members of the public, since the exemption applies to an offer "by the holder of the security". Suppose on Day One there are five allottees. The five allottees are each holders of the security and can arguably each make offers to six members of the public so long as s 6(2) and (5) are satisfied. Further, and again arguably, s 6(6) cannot apply since this deeming provision (view to acceptance by six persons deemed where more than six persons acquire securities within 12 months of the offer), only applies "to securities of the same class offered to the public for subscription *by the holder*". Thus, six acceptances from one holder are exempt, and also, therefore, six acceptances from each of five holders.

Section 6(4) thus raises the possibility of hybrid private offerings in a two-step process. First, attract s 3(2) and allot securities to, say, five habitual investors. In the case of Maori, the allotment might be to members of the *iwi* who fall within the definition of relative as contained in Pt O of the *Income Tax Act* 1994 (NZ) since connection by blood relationship goes to the fourth degree and, significantly, includes a

trustee for a relative. At this point, there would need to be cogent evidence that s 6(2) was inapplicable. Secondly, attract the safe harbour of s 6(4)(c), since the five habitual investors (or relatives) are now holders of previously allotted securities who can arguably each make offers to s members of the public.

An IPO may be driven by strategic reasons, because the exclusionary provisions of s 3 are unavailable, the exempt offering provisions do not apply, or because moneys cannot be obtained from venture capitalists. Often, the necessity for a greenfields IPO flows from an inability to obtain other financing on favourable terms or at all. As to the latter point, note that an IPO may be driven by the desire to recoup otherwise irrecoverable expenditure. Generally, this is an inauspicious omen for the future of the company since the immediate interests of the promoter/vendor are satisfied at listing. In all cases, future financing alternatives should be weighed carefully prior to entry into conditional contracts or options. If an IPO is a possibility, then the commercial actor should consider immediately obtaining Floatco, a "clean" unlisted company (one that has never traded), as the vehicle with which to contract. Alternatively, a listed "shell" might be acquired for a "backdoor" listing.[14] Floatco will be the issuer of equity securities in an IPO and, upon attaining the minimum subscription provided for in the prospectus, may be admitted to the official lists of the NZSE.

'Why use Floatco to enter into the conditional contracts and options? Why not have Puntco enter into these contracts and later assign them to Floatco? Or why not have Puntco contract directly with Floatco? The short answer is that using Floatco as the contracting party removes problems with assignment of contracts and liability for stamp duties, goods and services tax (GST), and taxation liabilities generally as far as Puntco is concerned. This is desirable from the promoter's viewpoint but there are other good reasons. First, it may be difficult to obtain a clause which enables assignment without consent, and no prudent commercial actor would risk outright refusal of consent or a demand for further consideration in the absence of such a clause. Secondly, if Puntco contracts directly with Floatco, Puntco may be assessed for stamp duty and GST on a subsequent asset transfer, and incur a taxation liability on any profit accruing. A third reason for using Floatco as the contracting vehicle goes to terms and consideration. Floatco can make settlement dependent upon flotation and have consideration include cash and paper (shares in the issuer). In practice, such contracting is never clear-cut and assets may be assembled by both Puntco and Floatco. Cavendish provides a good illustration of such an acquisition phase and the variety of contractual and non-contractual strategies that may be used to acquire the requisite assets.

14. See Earp and McGrath, op cit, n 3, p 138.

The Cavendish prospectus, under the heading "Statutory Information" discloses a range of acquisition strategies. These are noted below.

Acquisition Techniques

Conditional Contract

In 1985, Payeo entered into a conditional contract to purchase a property intended for development as the base station at the bottom of the gondola. This agreement and subsequent amendments were consolidated in another agreement in 1990 which provided for Payeo to purchase the requisite land. The benefit of the 1990 agreement was held by Payeo for Cavendish. There were a number of noteworthy terms in the agreement. These included: an escalator clause on the quantum of the purchase price ($450,000), which provided for a 15 per cent increase per annum from 1 November 1988; forfeited deposits ($55,000 in total), to be deducted from the purchase price; payment of a further $50,000 upon the project finance becoming available, such sum to be on account of the purchase price (obviously not paid), and the vendors' right to subscribe for shares in Cavendish.

Option to Purchase

The option agreement related to two parcels of land (4.25 and 18 hectares each) at the top of the gondola. The option was entered into in 1985. The option was between the vendors and Project Consultants Limited, as nominee, and the benefit of the contract was nominated to Cavendish. The consideration paid for the option was $1000, and the purchase price was $80,000 inflating at 16 per cent per annum from May 1986 on a monthly basis. The option could be exercised within six months of all consents being obtained. On exercise, $15,000 was payable as a deposit. Full payment was then due within 60 days. The option also provided for the creation of easements giving access to the land and the right to construct and operate an aerial cableway over the land. A performance bond of $5000 was payable prior to any work commencing in respect of the easement rights.

Agreement to Provide a Lease

Cavendish entered into an agreement with the Minister of Conservation in 1991 to provide a lease and grant certain easements. The granting of the lease was subject to the project proceeding (in effect, subject to flotation), and covered land at the top of the gondola, the route and area of the towers from the base station to the top, and

associated walkways and easements. Consideration for the lease comprised a base rental plus a further rental calculated as a percentage of turnover and reviewed every three years. An interesting condition of the lease was the requirement that Cavendish gift the Crown the 18 hectares at the top of the gondola which was to be acquired pursuant to the option (see above), and this land was to be vested as a reserve.

Heads of Agreement

In 1991, heads of agreement (strictly, an agreement to agree) were entered into between Cavendish and Doppelmayr Lifts (NZ) Limited to acquire a gondola system as a turnkey operation on a deferred payment basis. The heads of agreement were expressed to be subject to flotation. There were two important conditions in the heads of agreement. First, the purchase price was subject to exchange rate variation, which implied an active hedging programme by Cavendish. A logical implication was that the cost of managing foreign exchange exposure should have been specifically provided for in the prospectus. No such provision was made. Secondly, Doppelmayr were prepared to leave NZ$2 million owing, secured by a second debenture repayable two years from date of flotation (that is, on 11 December 1993). The latter term was tied to a provision whereby any change of 50 per cent of the directors could trigger an acceleration clause in repayment of the debenture.

Reimbursement of Costs

An agreement for reimbursement of costs, as between the promoters (Yeoman, Paynter, and Payeo) and Cavendish, was a critical part of the acquisition strategy. This is a matter which impinges on vendor consideration and is considered further below, but note here that the promoters were transferring the benefit of the Mount Cavendish Project to Cavendish in consideration of full reimbursement of all costs and expenses incurred (part of which was to be taken in shares).

Consider the commercial strategy of the acquisition phase. Strategic goals are:

- keep cash expenditure to a minimum;
- shift the burden of paying cash consideration to Floatco and, where possible, blend cash and paper (shares in Floatco), when determining consideration in order to preserve cash in Floatco;
- negotiate long time-frames to raise equity finance;
- impose conditions which entrench the promoters in Floatco and ensure reimbursement of costs and expenses expended by the promoters from Floatco upon flotation.

Most of these strategies figure in the Cavendish acquisition phase.

PROSPECTUS PHASE

Prospectus phase proper commences when the commercial actor has assembled (or "packaged", in the industry jargon) an asset or collection of assets in a form suitable for an IPO. Clearly, preparatory work on a prospectus may commence well before this time if the requisite commercial decision is made. The third phase of an IPO is labour-intensive since the involvement of a wide range of professionals and others is required. It is also costly: in small flotations in the United States, direct costs were recently calculated at 7.4 per cent and underpricing at 11.5 per cent of moneys raised, giving total costs of 19 per cent.[15]

Going public has advantages and disadvantages. Public listing permits diversification, increases liquidity, facilitates the raising of further cash, and establishes a value for the business. Disadvantages include the cost of reporting, disclosure, difficulties with self-dealings, the possibility of a non-liquid market, and dilution of control.

It is not mandatory to seek listing on the NZSE in order to make an IPO, but it is necessary to issue a prospectus. An example is provided by the prospectus issued by Software of Excellence Limited in 1992. Commercial pragmatism favours the listing of a greenfields flotation because investors seek liquidity in the secondary market and there is the possibility of a capital gain provided by a listing.[16] Normally, there is no great incentive to invest in an unlisted company where there is no ready market or possibility of a capital gain. There are notable exceptions: in the United States, an example is provided by the early life of Microsoft Corporation founded by Bill Gates. In Australia, an example is Split Cycle Technology, an unlisted company, formed by expatriate New Zealander, Rick Mayne. Investment in unlisted companies is generally the preserve of venture capital companies.

The Decision to List

Although there is an over-the-counter (OTC) market in New Zealand, there is only one official stock exchange, the NZSE. In order to obtain admission to the official lists of the NZSE, an unlisted company must make an application for listing, comply with the listing rules of the NZSE, and enter into a listing agreement with the NZSE. The resulting agreement between issuer and the NZSE is a private contract.

Compliance with the NZSE listing rules involves terms and conditions such as the minimum value of the company for listing, the size of the "spread" (minimum number of public shareholders), independent

300-500

15. See SEC, *Report of the Advisory Committee on the Capital Formation and Regulatory Process* (1996), Appendix A, Table One.
16. Fox, Roy and Walker, "Underpricing and Aftermarket Performance of IPOs on the NZSE" (1994) 12 C&SLJ 397.

vetting, the number of directors, and certain mandatory provisions as t takeovers in the company's constitution.[17] While the listing agreeme is a private contract between the company and the NZSE, upon listing th listing rules form part of the contract between the company and NZS and are enforceable by shareholders.

Human resources: allocating responsibilities and establishing the critical path

Once the decision to proceed with an IPO has been made, a range o professionals must be engaged to supply the component parts of th prospectus. The main statutory requirements are contained in th *Securities Act* 1978, the *Securities Amendment Act* 1988, and th *Securities Regulations* 1983-1997. Since a lawyer is usually the firs professional approached by the commercial actor, the task o recommending other professionals and coordinating their activities ofte falls to the law firm. The commercial actor contracts directly with th various professionals for services but, since lawyers assemble th prospectus for registration, reporting lines typically flow from thes other professionals to the lawyer. When the full complement of humai resources has been established, a critical path showing responsibilitie and milestones should be created and distributed to ensure that th contributions of all parties are synchronised.[18] The followin paragraphs outline the persons involved and indicate their roles.

The Commercial Actor

The entrepreneur will spend the majority of the time liaising with a range of professionals, briefing them on the desired commercial goals and providing them with the requisite information to produce, fo example, financial and statutory information.

The Accountant

The First Schedule of the *Securities Regulations* 1983-1997 requires that financial statements be prepared: see cl 8. In addition, accountants may prepare financial forecasts: see cl 9. Clause 10(1)(c) makes a special requirement for an IPO to produce a prospective statement of cash flows of the issuing group which the directors of the issuer expect to occur in the year commencing on the date the prospectus is delivered in registrable form to the Registrar of Companies in Auckland (prospectus vetting is now centralised in Auckland). Detailed requirements in respect of financial statements are contained in cll 22-38.

17. See McKenzie, "Takeovers Regulation" [1996] NZLJ 428.
18. See Earp and McGrath, op cit, n 3, pp 54-59 for a sample timetable.

The Auditor

It is a statutory requirement that an auditor's report be prepared: cl 42.

The Solicitor

Solicitors generally act as the coordinating professionals in an IPO since it is their responsibility to ensure compliance with all aspects of the Act, lodge the prospectus with the Registrar of Companies in Auckland, and negotiate the terms of the listing agreement with the NZSE.

The Underwriter

Typically, the commercial actor will initiate discussions with an underwriter (usually a bank, merchant bank, financial intermediary, or sharebroker) and, sometimes, subunderwriters (for example, sharebroker or high-net-worth individual), with a view to obtaining underwriting for a fee. The terms of the underwriting and subunderwriting contracts will be negotiated between the parties' respective solicitors.

The Sharebroker

Sharebrokers may or may not be underwriters or subunderwriters and brokers to the issue. Alternatively, they may simply be brokers to the issue and receive commission for processing applications for shares. In each case, the sharebroking house and its client advisers will need to be familiar with the terms of the offer and the management of the issuer.

Other Professional Experts

Expert opinion may be required for insertion in the prospectus (for example, the advice of a consulting geologist), or expert advice may be required for costings, so as to ascertain with some degree of precision the application of the proceeds of the issue. In Cavendish, architects and engineers were required to provide advice on the construction of the gondola and the base and top stations. Sections 38A and 40 contain requirements relating to the qualifications of and consents by an expert.

Public Relations

The *Securities Act* prohibits initial publicity except to the extent allowed in s 3(6).[19] Nonetheless, it is prudent to engage and brief public relations consultants at an early stage in order that they may prepare a

19. NZSC, *Preparing to Go Public* (1984).

campaign for the selling of the issue. In Cavendish, the costs of pub relations and marketing were estimated in the prospectus to be $72,3 A notable instance of a full-blown public relations effort was the IPO Telecom where an extensive television campaign was mounted and train hired to travel the length of New Zealand to extol the virtues of t offer. It may be critical to the success of the issue to ensure good me coverage and this requires careful preparation.

Print Media

The commercial actor and lawyers liaise with printing, productio photographic, artwork, and other print media specialists in t preparation and printing of the prospectus. Production and printi costs may run as high as $8-$10 per prospectus. Note that from 1 Octob 1997 it may be possible to reduce such costs by the use of an electron prospectus. This is because the definitions of words such as "distribute and "document" in s 2(1) have been amended to enable electron communications.

The preceding description is designed to highlight the number professionals involved and indicate their roles. It also points to th logistical problems which may arise when the critical path goes awry an the financial risk assumed by the promoters in the event that the IP does not proceed. In Cavendish, costs of the issue were estimated in th prospectus at $307,000. The promoters were risking this amount addition to the $1.5 million already expended in packaging the deal.

Structuring the Prospectus

The process of structuring the prospectus is twofold. First, a set preliminary decisions about the amount of money to be raised, the typ of securities to be issued, the portion of Floatco to be sold, and th presence of an underwriter must be made. Secondly, a re-evaluation the preliminary decisions will be made either with the underwriter, if th issue is underwritten, or in consultation with other professional adviser if the issue is not underwritten.

Preliminary decisions

How much cash is needed?

In the Cavendish prospectus, major capital expenditure was estimate at $11.105 million. There, the major items of capital expenditure wer the buildings ($3.7 million) and the gondola facility ($3.6 million) Accordingly, Cavendish sought to raise $7.890 million by the issue o equity securities to the public. A further $2 million of debt finance wa

to be supplied by Doppelmayr and $706,000 by bank facilities. The sum of $7.890 million was a best case number, or the maximum subscription to be raised. The minimum amount of share capital to be raised to provide for the major capital expenditure was $5.9 million, and, on this basis, some $1.990 million of debt (in addition to the $2 million Doppelmayr debenture) would be required. In the event, Cavendish listed with a raising of $5.953 million, barely over the minimum subscription.

How much of Floatco will be sold to raise the maximum subscription?

This question is important because it affects control of the listed company. In New Zealand, control of 30 per cent of the issued capital is generally reckoned to be effective control of a listed company. Promoters issuing in excess of 70 per cent of the issued capital to the public may face the prospect of a takeover from a determined predator. Ideally, the promoters of Floatco would seek to retain the requisite 30 per cent and ensure control. In order to do so, Floatco would have to value at a figure whereby 70 per cent of that valuation matched (at best) maximum subscription. In the case of Cavendish, $7.890 million was sought from the public. This would imply a valuation of $11.27 million for the project if the promoters were to retain a 30 per cent interest of $3.381 million, satisfied by way of the issue of shares as part of vendor consideration ($7.890m plus $3.381m equals $11.27m). By contrast, if the project were operational and returning $2 million per annum, then, on a price/earnings (P/E) ratio of five, a valuation of $10 million would be possible. In Cavendish, the only realistic value which could be placed on the project was the value of moneys expended on the project.

In a hot issue market, it might have been possible to discount forecast future cash flows (DCF) to give a net present value (NPV) of the project.[20] Even so, the resultant NPV would not amount to $10 million, thereby justifying a vendor consideration of $3 million (taken in vendors' shares credited as fully paid), on an issue of $7 million. Such a figure could not be obtained even if the financial forecasts appearing in the Cavendish prospectus were so discounted. In any event, there were other good reasons for not attempting to take vendors' shares "up front".

The Cavendish project commenced in 1985, well before the share-market crash of 1987. There followed six years of preparation and planning, which cost some $1.528 million, including holding costs on moneys. Prior to the crash of 1987, the promoters could feel comfortable

20. See generally, Brigham and Gapinski, *Financial Management* (1994) and the discussion of valuation methodologies in Earp and McGrath, op cit, n 3, pp 109-114.

about these expenditures as they were made in the late stages of the greatest bull market in the history of New Zealand, and because, based on current commercial practice at the time, they would have had good reason to expect a healthy vendor consideration on a flotation, a fully subscribed prospectus, and a positive aftermarket. After the crash, an IPO was the only way by which the planning costs of $1.528 million could be recouped. There seems little doubt that this was a powerful consideration in the way vendor consideration was structured, that is, $500,000 was reimbursed in shares and the balance taken in cash. The only other vendor consideration was the right to be allocated bonus ordinary shares in the company, based on the achievement of certain profit figures. In this way, vendor consideration was tied to the performance of the company.

On the surface, the structure of vendor consideration in Cavendish reflected the commercial reality of the time. It was obviously going to be very difficult to float in New Zealand in 1991, and hence vendor consideration was framed in a way which helped to sell the issue. The promoters could say in reply to questions on adequacy of vendor consideration: "We have spent six years and $1.5 million in cash and professional time putting this deal together. We only want $1 million back in cash. We will take the balance in shares. If the company is profitable, we will get bonus shares. But remember, if the company is profitable the share price will increase and you will also profit." In the event, it seems ironic that the timing of the reimbursement of cash contributed to the post-listing problems of Cavendish. This leads us to another significant consideration: underwriting. There was no way a greenfields IPO would be underwritten in 1991 because of the depressed state of the economy. Because Cavendish was not underwritten, the promoters were exposed to the risk of the issue closing undersubscribed. In that event, the promoters would be out of pocket to the extent of the costs of the issue, some $307,000. Hence, decisions on vendor consideration, which (superficially, at least) assisted in the selling of the issue, were critical.

✳ *Will the issue be underwritten?*

An IPO may or may not be underwritten. Very rarely, an underwriting may be unconditional or "bankable" (in the sense that a bank will be prepared to lend on the security of the underwriting agreement). Usually, however, the underwriting agreement is subject to a "market out" clause. The market out clause permits the underwriter to withdraw at any time prior to the public offering in the event that any one of a range of contingencies occur. These might include: the outbreak of war between the major powers; suspension of trading on the NZSE; a nominated per centage decline in the NZSE40; or a material, adverse event affecting the issuer. If the IPO is underwritten and the market out clause is not

triggered, the underwriter will pick up any shortfall on the issue. Thus, if the minimum subscription is $5 million and only $4 million is subscribed for by the public, the underwriter must take and pay for the remaining $1 million shares. Accordingly, the question of "selling the issue" (finding buyers for the IPO) is answered upon the execution of the underwriting agreement. In effect, the underwriter has bought the issue since the company can now look to the underwriter to meet any shortfall. If the issue is not underwritten, then it is up to the promoters and directors of the issuer to sell the issue. In Cavendish, the issue was not underwritten and accordingly it fell to the company to sell the issue.[21]

Rethinking the Initial Decisions

If the IPO is underwritten, firm decisions regarding the size of the issue, the type and price of securities to be offered will be made jointly by the issuer and the underwriter. This requires an understanding of the commercial position of issuer and underwriter, the essence of which is a trade-off between costs of certainty and uncertainty in closing the issue. In turn, this requires some assessment of the market's reception to the IPO and the logistical effort required to sell the issue to the public. At one extreme is the "blue chip", seasoned IPO where oversubscription may be confidently predicted: Telecom provides an example. One might expect such an issuer to forgo an underwriting. Why pay an underwriter's commission (effectively, a form of insurance in the event that the issue is undersubscribed), when one can be confident that the issue will be fully subscribed? There are two answers. First, in such a case the issuer might well dispense with an underwriter: Fruitfed Supplies Limited is a good example. Secondly, the issuer might consider dispensing with an underwriter but engage one for logistical reasons (generally with a reduced commission to reflect the lower degree of risk associated with selling the issue), because of the size of the issue and a desire for a wide spread of shareholders. Again, Telecom was this type of issue. At the other extreme is the speculative, unseasoned IPO: junior mineral exploration companies are a good example. Here, the issuer's main concern is to achieve minimum subscription and it will happily pay a high underwriting commission to achieve this. Underwriting for this type of IPO would normally be available only in a bull market. Even so, the underwriter might seek a high commission, risk spreading via subunderwriting agreements, a small-sized issue with substantial underpricing, and an attractive capital structure (for example, shares with a free option attached).

In Cavendish, an underwriting was unavailable. If an IPO was to proceed, the company and promoters would be exposed to the risk of

21 For a discussion of underwriting questions, see Earp and McGrath, op cit, n 3, p 91.

undersubscription. In that event, all subscriptions received by the company would have to be repaid pursuant to s 37(5) and (6) of the *Securities Act*, and the company (and probably the directors and promoters personally) would be liable for costs of the issue. A key factor influencing the decision to proceed with a flotation without an underwriter was the result of a market survey commissioned in 1990.

In the chairman's statement in the Cavendish prospectus, Mr Ray West stated:

> "Greater Christchurch itself has a population of 312,000 and an AGB McNair survey conducted during December, 1990 revealed that 88% of those surveyed indicated that they could be potential customers of . . . Cavendish . . . [r]esponses to the same survey also indicated that 9296 of those surveyed felt that the project should be principally owned and operated by New Zealanders. The Directors are therefore determined to give the public of New Zealand, and in particular Christchurch residents, the opportunity to participate in this project which is designed to be of benefit to the Canterbury and South Island region . . . [i]nvestment in the ordinary share capital of . . . Cavendish . . . is an equity decision within the reach of most households . . .": *Prospectus*, 3.

The AGB McNair survey provided good reason for the promoters to suppose that an IPO would be well supported in Canterbury. The finding was reflected in the theme of the selling campaign, "Support Business in the South". Hence, the survey provided some basis for the decision to make an IPO in the absence of an underwriter. If the issue reached minimum subscription, the costs of the issue and reimbursement of a substantial portion of cash expended would be met by the company. In these circumstances, there were powerful reasons to make the offering as attractive as possible: "as they say on Wall Street, new issues are sold, not bought".

There is an inherent contradiction at the core of every prospectus. The prospectus is simultaneously a selling document and a disclosure document. Can these functions ever be reconciled? The prospectus is the document used by promoter or underwriter to sell securities to the public. For this purpose, it is necessary to put the best possible gloss on the company's prospects. In Cavendish, parochial pride, rising tourist numbers, favourable profit forecasts, and a projected dividend of 10 per cent after the first full financial year of operation were emphasised as positive factors. On the other hand, the prospectus is a disclosure document, the primary means by which the investor protection policy of the *Securities Act* is discharged. The Act and the Regulations contain specific requirements as to the content of registered prospectuses. The First Schedule of the Regulations, in particular, lists numerous matters required in a registered prospectus for equity securities. These disclosure requirements are backed by civil and criminal sanctions for misstatements in advertisements or registered prospectuses: see ss 55-58 of the Act.

Close scrutiny of the Cavendish prospectus might have deterred investors. The most serious contingency was undercapitalisation: what if the prospectus only attracted minimum funding? This was a real risk in 1991. The full subscription was $7.890 million; the minimum was $5.9 million, a difference of approximately $2 million. Detailed financial forecasts and assumptions were included in the prospectus on the basis of a full subscription. Only a summary of forecast financial figures on the assumption of minimum subscription was provided, but those figures showed net profit before tax at $300,000 negative in 1992 and $1.44 million positive in 1993.[22]

Cavendish listed with the bare minimum subscription, and analysis of the annual report for 1992 and the interim report of 31 March 1993 shows a marked deficiency between actual and forecast profit. Key reasons appear to be lack of initial funding, underestimation of costs, poor visitor numbers, and weather conditions. Lack of initial funding, however, was the salient problem and stemmed from the decision to peg the minimum subscription at $5.9 million. This points to a potential conflict between the interests of the promoters and those of potential investors. As far as the promoters are concerned, the lower the minimum subscription, the better the chance of closing the issue, recouping moneys expended on the project, and shifting liability for costs incurred on the IPO from promoters to issuer. Potential investors would prefer the issue to close oversubscribed in order to enhance the prospects of the company and the share price, and to enable completion of capital works.

The Cavendish IPO closed with the minimum subscription, causing problems in the first year and a half of operations. An indication of problems appeared in the annual report for the year ending 30 September 1992. The directors' report noted a loss of $1.276 million as opposed to the forecast loss of $524,000, and commented:

> "The . . . variations are substantially due to the difficulties experienced in the initial public issue which only just exceeded the minimum subscription level. This situation resulted in additional issue expenses, considerably higher funding costs and exchange losses incurred as a consequence of the company's inability to take forward exchange cover due to the lack of financial facilities available during the construction period. Forward exchange cover is now in place and no further exchange losses will be incurred": *Annual Report 1992* p 5.

None of this is entirely surprising, although it can scarcely be said that the company was unaware of the potential consequences of going naked (uncovered) on foreign exchange exposure. Rather it shows how

22. As to well-known problems with earnings forecasts, see Fox and Walker, "The Accuracy of Earnings Forecasts in New Zealand IPO Prospectuses, 1992-1993" (1995) 13 C&SLJ 284.

sensitive the company was to the initial condition of minimum subscription. Minimum subscription exacerbated the effect of vendor reimbursement—$1 million approximately taken in cash immediately, as part refund of expenses incurred, reduced the $5.9 million raised by the IPO to $4.9 million. Then the costs incurred in obtaining the minimum subscription escalated from $307,000 to $423,000. The resultant paucity of cash led Cavendish into expensive financing options. For example, it was claimed that, because of lack of cash, foreign exchange exposure was not forward-covered, and this resulted in losses of $463,000. One obvious solution to this problem would have been to defer or spread repayment of vendor consideration until or from the end of the first year of operations, thereby freeing up funds to cover foreign exchange exposure. The proposed solution gathers force from examination of related party transactions in the notes to the accounts in the annual report for 1992. The relevant note reads as follows:

> "RELATED PARTY TRANSACTIONS
>
> Businesses in which Directors have a substantial interest and which provided services/supplies to the company on arms length commercial basis were as follows:
>
> [*details of professional services supplied to Cavendish by businesses associated with four of the directors follow*]
>
> The aggregate amount of these services totalled $2,137,000, including $198,000 owing at balance date, which will be settled in the ordinary course of business.
>
> These charges are inclusive of the original costs and disbursements incurred by the promoters during 6 years of planning . . . [which] costs were detailed in the Company's Prospectus and totalled $1,528,000. The net costs and disbursements incurred during the period of construction was therefore $609,000": *Annual Report 1992* p 14.

A continuation of problems flowing from initial funding was noted in the interim report for the six months ending 31 March 1993. An analysis of this document, extrapolated for the full year ending 30 September 1993, again shows a deficiency between actual and forecast profit. At the same time, in order to remedy the undercapitalisation problem (and take advantage of favourable market conditions in mid-1993), Cavendish announced a one for five underwritten cash issue at par value of $1 to raise a further $1.420 million.

SELLING PHASE

The presence of an underwriter is one way of ensuring that minimum subscription will be met. Clearly, if an underwriter is available, the issuer will try and set the minimum subscription as high as possible. In the absence of an underwriter, the promoters and directors must sell the

issue. In Cavendish, this problem was recognised and addressed in the prospectus phase. In a highly innovative selling technique, the prospectus was produced as a broadsheet in newsprint, and delivered, in effect, as a local newspaper. This technique appears as a logical consequence of the AGB McNair survey. Similarly, the prospectus made a strong appeal to parochial pride. Another innovative selling technique in the prospectus was provision for payment of shares by credit card (Visa, Bankcard, and Mastercard).

The public relations and marketing budget for the IPO was estimated in the prospectus at $72,000. The actual figure was almost certainly higher. The Cavendish prospectus was dated 17 July 1991. Section 37(2) of the *Securities Act* required that the minimum subscription be met within four months of date of prospectus. According to the 1992 annual report, public subscription for shares closed on 6 December 1991, after two extensions. There was no explicit provision for extending the date of a registered prospectus in the Act, but s 43 operated to that effect by providing for amendment of a registered prospectus by delivery of a memorandum of amendments to the Registrar of Companies and registering the amendments under that section. The grounds for refusing a memorandum of amendments are limited (see s 43(4) and (5)) but two extensions appeared to be the maximum permissible, if only because the accounting information in the prospectus would become dated. As of 1 October 1997, however, the life of a prospectus will range from 6 to 9 to 18 months: see ss 37A(1)(c)(i), 37A(1)(c)(iii) and 37A(1A).

Cavendish experienced difficulties in reaching minimum subscription within four months and the vigorous selling campaign accelerated at the time of first extension. An intensified public relations and marketing effort was demonstrated by the following actions: the IPO received increased and favourable coverage in local newspapers; a gondola and large free-standing sign were placed adjacent to a main traffic artery; the promoters held a series of public meetings in the Christchurch area (a local "road show") and hosted private briefings ("dog and pony shows") to assist the selling effort.

A desirable strategy in the selling phase is to attract large and influential investors ("anchors") before or in the first week after registration of the prospectus. The presence of anchor shareholders assists in marketing to smaller investors. In Cavendish, large investors, who were also construction contractors to the company, invested at a late stage. From a selling viewpoint, it would have been preferable for these investors to subscribe at an earlier stage. There is no impediment to a contractor subscribing for shares and subsequently receiving moneys for contracting works even if the sums involved exactly matched each other. But the subscription must be in cash (see s 37(2)) there must not be a swapping of services for shares. Allotments in contravention of the Act attract criminal liability: s 59.

Presumably, the paragraph is intended to deal with the situation where cheques for small amounts have not been met. In practice, of course, cheques are banked into a designated account and will have been met or the payee issuer advised otherwise well before the close of the issue. Normally, an issuer would not close the issue with uncleared cheques in the banking system. Hence, in practice, s 37(2)(a) may offer the semblance of an exemption for the directors of an issuer when they seek to close an issue notwithstanding that minimum subscription has not, in fact, been received.

In the Cavendish IPO, s 37(2) of the *Securities Act* should be read in conjunction with s 62 of the *Companies Act* 1955 (see now s 76 of the 1993 Act). Section 62 prohibited the provision of financial assistance by a company for the purchase of its shares. In order to close an IPO, directors might offer an arrangement to a subscriber whereby funds are received from the subscriber by the company in order to close the issue and, shortly thereafter, are returned to the subscriber in the form of, for example, an investment or loan. The commercial vice of such an arrangement is that the issuer does not have the minimum funds required to achieve its business objectives. A graphic example of a scheme breaching s 62 is suggested by the fact-pattern in *R v Rada Corporation (No 2)* [1990] 3 NZLR 453 (HC).[25] In that case, the promoter arranged for a $50 million subscription in the IPO of Prorada Properties Limited to be effected via a fully-owned subsidiary, which borrowed the entire $50 million from the Bank of New Zealand (BNZ) and paid the amount to Prorada, who simultaneously on-lent the moneys to a subsidiary, who, in turn, placed the moneys on deposit with the BNZ. The practical effect was that the Prorada issue closed $50 million short of the minimum subscription. Breach of s 62 of the *Companies Act* 1955 carried a $200 penalty, but s 59 of the *Securities Act* imposes criminal liability and a maximum fine of $15,000 for allotting in contravention of the Act. Section 59(2) provides defences of immateriality or other grounds for reasonably being excused and absence of knowledge and consent: see *District Registrar of Companies v Heenan* (1996) 1 BCSLR 264. But s 37(2)(a) of the Act provides a better vehicle for those determined to breach s 37, since the sum required to close the issue is deemed to have been paid (assuming proof of receipt in good faith and absence of reason to suspect the cheque will not be paid) and the requisite "round robin" for breach of s 62 of the *Companies Act* 1955 is unnecessary.

CONCLUSION

One purpose of this case-study is to provide a paradigm of an IPO that fits contemporary commercial practice and has explanatory, diagnostic,

25 For comment, see Walker, "Lifting the Corporate Veil to Avoid Criminal Liability for Misstatements in Registered Prospectuses" (1993) 11 C&SLJ 58.

and heuristic properties. The resulting five-phase model works satisfactorily in explaining the Cavendish IPO, suggesting that the model fits contemporary commercial practice and, in particular, greenfields flotations. The model should apply equally well to IPOs of seasoned companies, providing that the acquisition phase is connoted not simply as the purchasing of assets but as the building up, by a variety of means including acquisition, of a business suitable for flotation. As to the desired properties, explanatory power requires that insights provided by the model are not unique but are common to other IPOs. Identifying a large gap between maximum and minimum subscription and realising that this may be explicable by reference to desire for vendor reimbursement is one way the model suggests explanatory power. The diagnostic aspect of the model denotes a capacity to discern areas of potential difficulty in an IPO—the discussion of instability in the register of a vendor company is an example. Heuristic properties are suggested by the ability to apply this model to other IPOs and identify their key elements.

There is a wider context, also. Capital raising by the public and private sectors continues to be of immense significance for the future development of New Zealand. In the late 19th and the first half of the 20th centuries, large scale capital investment transformed New Zealand into an efficient producer and exporter of primary products. As these industries decline in importance, capital investment in new and developing industries is required to sustain the economy. A striking example in 1993 was new investment in the timber industry. Because New Zealand is a capital importer and net borrower in relation to the rest of the world, the manner in which it regulates capital raisings is a survival issue.[26] This may be one reason why New Zealand has moved quickly to allow capital raisings by electronic means.

26. See Chapter 1 herein.

CLOSING PHASE

The closing phase of an IPO is principally governed by s 37 of the *Securities Act*. Section 37(2) stipulates that no allotment of an equity security shall be made unless the minimum subscription is paid and received within four months (or as extended pursuant to s 43). If allotment cannot be made, subscription moneys are to be held in a trust account and refunded as soon as practicable: s 37(5). In practice, subscription moneys are usually held in a separate, designated account at the sharebroker's or issuer's bank, at least until minimum subscription is reached. In a bull market, maximum subscription may be achieved quite easily. Here, the prudent issuer should make provision in the prospectus to accept oversubscriptions. When the issuer is legally able to close the issue, verification of the amount standing in the designated account is sought from the banker. The Registrar of Companies and the NZSE are then advised of the quantum of moneys and the closure of the issue. At this point, the issuer may transfer moneys from the trust or separate account to the company's account. Usually, the first cheques written will be those required to cover the costs of the issue and cash reimbursement to vendors. All original forms of applications for securities are then assembled, photocopied, and forwarded (generally, together with an alphabetical list of subscribers) to the professional share registrar engaged by the issuer. In the Cavendish IPO, the share registrar was Registry Managers (NZ) Limited. The share registrar completes the share certificates, compiles the list of shareholders, and physically records secondary market transactions. In small IPOs, share certificates are usually sent to the issuer for the affixing of the company's seal and the signatures of the director(s) and secretary. Upon completion of the allotment process, share certificates are mailed to shareholders. Listing occurs a week or so later.

Sections 37 and 37A contain provisions which deal with void and voidable irregular allotments. There has been some case-law on s 37 in the context of debt securities, the effect of which is to hold that there is nothing inconsistent between s 37(4) of the *Securities Act* (which declares a contravening allotment to be invalid and of no effect) and s 7 of the *Illegal Contracts Act* 1970 (NZ) which enables a court to validate same or grant other relief.[23] But the principal concern of s 37 derives from subs (2) which requires that the minimum amount stated in the prospectus must be raised before the issue can be closed.[24]

Section 37(2)(a) contains a curious provision. It provides:

> "A sum shall be deemed to have been paid to, and received by, the issuer if a cheque for that sum is received in good faith by the issuer and the directors of the issuer have no reason to suspect that the cheque will not be paid."

23. *Re AIC Merchant Finance Ltd (in rec); National Mutual Life Nominees Ltd v Watson* [1990] 2 NZLR 385 (CA).
24. *District Registrar of Companies v Heenan* (1996) 1 BCSLR 264 (DC).

Planning an overseas legal career

Professor Gordon Walker, La Trobe University, Melbourne urges students to analyse their choices and plan their futures

There are many reasons why lawyers go overseas; adventure and change are two of them. You could say (doubtless with a straight face) that we first encounter the "Wild Wood" at law school or in practice. The "Wild World" comes after the Wild Wood and its call — as Kenneth Grahame writes in the childhood classic, *The Wind in the Willows* (1908) — is strong indeed. (To this extent, I am writing for those who take the adventure — wayfarers all.) In this article, it is assumed the "call of the South" is a key factor in the decision to go overseas; the central focus is accordingly on the strategy of overseas legal career planning. Of course, going overseas is never for the faint-hearted and holding your nerve when things go wrong — as they inevitably do — is critical. The New Zealand novelist, Ruth Park, had this to say about her departure to Australia in a flying boat in the 1940s:

> Thereafter I took for my banner those words Harry Tawhai had brought to mind: *He toa piki pari ma te pari*. He who climbs a cliff may die on the cliff, so what? Always a risk-taker by nature, now I became one by intent: R. Park, *A Fence Around the Cuckoo* (1992), 293.

As we shall see, the key words in the quotation from Ruth Park are "by intent" because they alert us to the importance of strategic planning for an overseas legal career.

This article is a revised and updated version of "The Legal OE" [2000] NZLJ 436. The 2000 version of the article grew from my experience as a law teacher at Canterbury University School of Law in the mid-1990s. Because of the economic climate prevailing at that time, I found myself regularly giving advice to former law students who were leaving New Zealand to seek legal opportunities overseas. I later formalised the advice in writing and the 2000 NZLJ article was the result.

The 2000 NZLJ article proved popular with law students and younger solicitors seeking to study or practise law offshore. The reason is straightforward: the subject matter speaks directly to self-interest. For this and other good reasons, I present an Australian version of this analysis to first year law students at La Trobe University School of Law in Melbourne annually. There is a good case for including this presentation at first year in law school because it starts law students thinking about the trajectory of their legal careers at an early stage thereby enabling a degree of forward planning.

It is now five years since the original NZLJ article was published so an update seems timely. (Once again I have been greatly assisted by comments from an outstanding group of my former Canterbury University law students whose names appear at the end of next month's article.) Over that time, however, three main developments stand out. First, since 2000 we have experienced a pronounced and compressed "boom to bust to boom" wave in the business cycle. A key consequential lesson is that, as regards offshore options, legal career planning must be even more sensitive to the wave pattern of the business cycle. There is little to be gained moving offshore if the market is not hiring. Hence, while a move to the US in the buoyant economy of the late 1990s was feasible, a move after the "tech wreck" of March 2000 and the terrorist attacks of 11 September 2001 was more difficult. A similar point applies to the UK legal services market which nose-dived in 2001-2002: see *Lawyers Weekly*, 22 July 2005, 13. Second, we need to consider the rise of China and the resurgence of the East-Asian economies post their 1997-1998 financial crises. For this reason, I have ranked two Asian jurisdictions (Singapore and Hong Kong) slightly ahead of the UK as potential overseas destinations. Third, there is now a great deal of quality intelligence on the global market for legal services. So, for example, the New Zealand legal services market was analysed in *Australasian Legal Business*, Issue 2.10 (2004). The Australian publication, *Lawyers Weekly* www.lawyersweekly.com.au and its New Zealand counterpart, *NZ Lawyer*, now offer regular updates on the state of the legal services market offshore: see, for example, "The London Report: The Capital's Calling", *Lawyers Weekly*, 15 July 2005, 16.

The first part of this article discusses the general problem — the lack of a legal career strategy as regards overseas options. The second part sketches a way of using the tools of corporate strategy to create a personal strategic plan to address overseas legal career options; the third part introduces strategic analysis for the individual. The fourth part of the article looks at the question of strategic choice. Overseas destinations such as Australia, UK, US and Asia are examined in next month's piece, and some issues regarding strategic implementation are assessed with particular reference to the US.

LACK OF CAREER STRATEGY

Few New Zealand law students focus on any medium-to-long term career strategies during the first years of law studies. Interest grows in the last two years of university study when law students interview for summer clerkships and first year associate positions in New Zealand. However, there is little collective student or "institutional" memory about overseas options because there is no

economy is the spectacular growth of the services industries: see Dicken, *Global Shift: Transforming the World Economy* (4th ed, 2003), 43. For example, the global financial services industry is an industry that requires high-level legal inputs. Financial market globalisation is also a paradigmatic example of the globalisation process since it is a factual process based on the observable dynamics of the market. A salient aspect of globalisation is the irrelevance of national borders in markets that can truly be described as global. So, for example, there is evidence to suggest that some large corporations with a presence in New Zealand are shifting their legal work out of New Zealand: see *Lawyers Weekly*, 10 September 2004, 1. There is hence good evidence to suggest that the market for legal services is truly global: see Lee, "The global players revealed", International Financial LR, November 1998, 23; McArtney, "A Global Law Firm" [1999] NZLJ 358. Indeed, high status US law schools actively promote themselves as "global" law schools. The Legal Education and Training Committee of the International Legal Services Advisory Council in Australia recommended in 2004 that strategies be adopted to promote the development of an internationalised legal education that prepares Australian graduates for the provision of legal services in a global market: see Council of Australian Law Deans Briefing Paper (5 July 2005).

It is now notorious that legal service providers look globally to recruit personnel (here, "global" connotes OECD countries). The first wave of this phenomenon hit New Zealand in the mid-to-late 1990s when London-based and Australian law firms stepped up recruiting from New Zealand. The anecdotal evidence is that some major New Zealand law firms experienced a "hollowing out" of substantial layers of fourth year associates attracted by higher pay offshore. In 2000, a second wave of offshore recruitment occurred; for example, Sydney-based Australian law firms recruited first year associates and summer clerks from New Zealand law schools. This wave broke with the "tech wreck" of March 2000. Hence, after March 2000 (and even more so post-September 11 2001) recruitment dried up. The current "window" opened when the business cycle began to head upwards in 2004. As of 2005, New Zealand lawyers are again in demand in Australia and London: see Ruffell, "Aussie firms to hunt Kiwi lawyers", *Lawyers Weekly*, 22 July 2005, 1, 9.

Why are offshore law firms recruiting from New Zealand? First, because good New Zealand trained lawyers are valued and appreciated. A second reason is international arbitrage or pricing asymmetry between salaries paid in New Zealand and offshore. For example, a first year associate in a top tier Sydney law firm attracts a salary of about A$58-74,000 (includes employer contributed superannuation portable within Australia) and relocation expenses as against about NZ$40-55,000 at a similar firm in Auckland. A third year associate in Sydney in a top-tier firm could reasonably expect a package of A$100,000. In New York, a first year associate can expect about US$125,000 plus bonus: see www.nylj.com under the heading "Associate PayWatch" for details. When thinking about pricing differences, factor in the drop in the exchange rate of the New Zealand dollar, the additional tax imposed on graduates by the student loan scheme, offshore living costs, and tax rates. A third and less obvious reason is the arguable oversupply of lawyers in New Zealand.

The case for oversupply is best founded on salary differentials between New Zealand and offshore. There is also a structural reason — as the *New Zealand Porter Report* (at p 103) stated in 1991, "New Zealand graduates more lawyers each year than it graduates students in agriculture, forestry, horticulture and veterinary science combined ... This latter group of industries makes up over 85 per cent of New Zealand's exports and needs skilled individuals to improve their competitive position". On this view, the stream of lawyers going offshore comprises an export industry with no obvious benefit to New Zealand. Oversupply means lower compensation packages overall (but particularly in the provincial centres) because supply outstrips demand. Oversupply may also lead to domestic arbitrage. A first year associate doing tax law with an accountancy firm in Auckland may well earn more than his or her counterpart in legal practice.

When undertaking a personal strategic analysis regarding offshore options, note there is no necessary link between post-graduate study and practice offshore. A third year associate from New Zealand may go direct to Sydney or London and join a law firm and pursue no further tertiary education. Indeed, if the ultimate aim is practise in the US, a "knight's move" to a US or UK firm in London and then across to New York is one way of entering the US market without incurring the tuition costs associated with a US LLM. In reality, however, there is usually a link between study and practice in the case of the US. A typical entry path to the US is an LLM from a top tier US law school followed by the New York Bar exam. This is because an LLM from a top tier US law school greatly enhances hiring prospects and gives standing to take the New York or California State Bar exams. Elsewhere, enhanced hiring prospects are the usual reason for post-graduate study and this course is more often pursued by new graduates seeking to acquire knowledge about "sunrise" subjects not taught in New Zealand law schools such as IT outsourcing.

After completing a personal strategic analysis, the next question that arises is choice. As stated, the task here is to evaluate the various options and choose the one that best fits your personal circumstances. For the purposes of this article, the immediate choice appears to be between various offshore destinations offering opportunities for lawyers. As of 2005, major UK law firms may hire direct law graduates from law school in New Zealand. Certainly, the Australian evidence is that top law graduates are being directly hired by the so-called "magic circle" UK firms. Details may be found on the various firm websites. In next month's article, we look at Australia, the UK, the US and Asia as possible choices. In practice, of course, these choices are not mutually exclusive; indeed, the choice may involve a decision to move to three jurisdictions in a sequence — a legal version of the 19th century "Grand Tour". So, for example, one might choose to go to Australia for two years in order to upgrade legal professional experience, obtain permanent residency status and take out Australian citizenship, then to the UK to access the under 28 Highly Skilled Migrant Programme (and possibly UK citizenship), then to Hong Kong to access favourable tax rates and save and — ultimately — back to New Zealand or Australia.

Next month Gordon Walker gets down to the nitty-gritty of the various destinations. ❑

Overseas legal career destinations

Professor Gordon Walker, La Trobe University, Melbourne surveys the major overseas opportunities following on from his article at [2005] NZLJ 401

I will not discuss opportunities in Europe. This is because a move to Europe involves special considerations relating to citizenship status and language ability. In this section, we first consider a number of over-arching considerations.

A first issue is sequencing or timing. Thus, because there is reciprocal admission between Australia and New Zealand, it is possible to be admitted in Australia immediately after New Zealand admission. It is easier to find work in Australia if you have one or two years' experience but this is not essential, especially if an Australian LLM is contemplated. UK or Hong Kong admission, on the other hand, requires four to five years' post-qualification experience and this experience is best achieved in New Zealand or Australia. The lesson here is that you are best to prepare yourself in New Zealand or Australia before a move elsewhere. Going direct to the UK, Hong Kong or the US is harder and may well require local qualifications (eg an LLM from a good US law school).

A second consideration is more practical: you must obtain duly notarised copies (or originals) of your degree testamur, academic transcript and admission order. Overseas admissions bodies will demand these documents and it is prudent to take them with you.

Third consideration: if you have language skills (eg Mandarin or Japanese) then leverage that ability to the utmost. The same point applies to those who have sporting ability — recently, two Canterbury Law students defrayed the costs of their Cambridge studies by playing rugby for Cambridge.

Fourth consideration: if you are deciding to go overseas, look at the recruiters' websites and note the areas in which they are hiring. These will be areas such as banking, project finance, capital markets, private capital, IP, telecoms and so on. (You will not see many advertisements for lawyers in public international law.) If you want to appeal to firms in these areas, then direct your resumé towards them by working in the area or choosing the relevant LLM subject.

Finally, keep a re-entry strategy in mind. Although your overseas strategy may require repeated modification as events unfold, you may well wish to return home one day. Thus, as your offshore career evolves, ask yourself how it will "fit" on the return home.

Destination: Australia

Australia is the most popular migration destination for New Zealanders. According to the Melbourne newspaper *The Age* (3 September 2005) there are about 415,000 New Zealanders living in Australia and that number is growing by about 630 a week (a total of 20,000 moved in 2004). The average weekly wage in Australia is 30 per cent higher than in New Zealand. As stated, Australian top tier law firms are once again recruiting lawyers from New Zealand in 2005. The usual criteria apply. In the past, Bar admission could be obtained only via Victoria or qualifying exams: see Walker [1983] NZLJ 188, [1984] NZLJ 34. Now, due to the extension of the Closer Economic Relations Agreement, New Zealand admission is sufficient for admission in Australia pursuant to the Trans-Tasman Mutual Recognition Act 1997: see www.lawsocnsw.asn.au. Admission to the Australian Federal Courts via the High Court of Australia flows from admission in an Australian state. Prudence dictates that New Zealand admission is gained prior to a move to Australia since automatic entry to Bar admission programmes in Australia is not assured. Sydney, the most "porous" (and expensive) of the Australian big cities, has a number of New Zealand lawyers in all the large law firms. Many practise for two or more years in Sydney and then move on to Hong Kong, Singapore or London.

New Zealand citizens cannot access Australian federal government loan schemes for LLB or LLM programmes: see www.goingtouni.gov.au. However, doctoral programmes (SJD or PhD) in law are fee-exempt for New Zealanders and most law schools offer competitive scholarships and tutoring or Teaching Fellowships for doctoral students. As regards LLM programmes, only Australian citizens can access the FEE-HELP federal loan scheme. FEE-HELP is an interest-free loan programme indexed to the Consumer Price Index where repayments are made via the tax system. International students taking LLM programmes in Australia pay tuition fees ranging from A$16,500 to A$24,000. One way of defraying LLM fees is to work as a solicitor in New South Wales and take an employer-paid LLM course in order to satisfy mandatory continuing legal education requirements (MCLE), which attach to annual renewal of practising certificate. Some LLM or doctoral students choose to take a Residential Associate (RA) position in a hall of residence at a university as a means of defraying costs and this course has definite attractions for those who have few other social contacts in Australia.

Australia may be a short or long-term destination. If the UK or the US is a long-term destination, then Australia is a convenient "half way house". This is because top tier Australian firms typically have strong offshore connections. If the US (or the NY Bar Exam) is the next step after Australia, then the LLM in Global Business Law at La Trobe is a good option as this programme offers intensive classes in US law at competitive rates: see www.latrobe.edu.au/law/gbl. Another good reason for going to Australia initially is that some persons who go on to the UK or US wish to return to the Southern Hemisphere and Australia presents as a prime return destination. New Zealanders who decide to spend

some time in Australia often seek to take Australian citizenship after two years' permanent residence in Australia before leaving for London or Hong Kong.

There are good and cogent reasons for taking out Australian citizenship. For example, as stated, only Australian citizens can access Australian federal government loan schemes for university education. There is no bar to holding dual citizenship in New Zealand and Australia: see further www.citizenship.gov.au. As of 27 February 2001, however, Australian citizenship rules changed. New Zealand citizens who arrive in Australia after February 2001 must now apply for and be granted Australian permanent residence (usually under the Skilled-New Zealand Citizen category) prior to applying for citizenship. In effect, this means that New Zealanders now rank the same as any other immigrant and must qualify on a points system. It is advisable to apply when under 45: see further www.immi.gov.au/facts/17nz.htm and www.immi.gov.au/migration/skilled/nz_visa.

Another good reason for thinking about Australian citizenship flows from the introduction of a new visa category for Australians wishing to work in the US. In May 2005, the US created a new visa category (the "E-3" visa), for Australia which allows up to 10,500 Australian business people and professionals to live and work temporarily in the US. Before this change, Australian were rolled up into global quotas under different visa categories and had to compete for the 65,000 H1B work visas competed for by nationals of other countries. The new "E-3" visas have two salient advantages: first, they can be renewed indefinitely (there is no six year limit), and, second, they allow for a spouse to work in the US: see further www.austrade.gov.au.

Destination: UK

The law degree in England takes three years. Some background data follows:

Solicitors: After the law degree, new graduates undertake a one-year legal practice course (LPC). They then proceed to law firms for two years on a training contract followed by admission. Non-law graduates can do a one-year conversion course (CPE or PGDL) and then proceed to law firms for a two-year training contract followed by admission.

Barristers: New graduates apply for pupillage at chambers and then do a one-year Bar Vocational Course (BVC). They are called to the Bar after BVC and then do a one-year pupillage followed by tenancy. At the Bar, the Cambridge LLM or Oxford BCL is an unspoken prerequisite for students from other common law countries.

Visas: Generally, a work permit is required. A work permit for the Bar is difficult to come by for non-EU passport holding New Zealanders given self-employment status at the Bar. Generally speaking, special visas may be obtained if one grandparent was from the UK ("grandparent visa"), for two years if you are from a Commonwealth country and between the ages of 17-30 ("working holiday visa") or, if under the age of 28, via the Highly Skilled Migrant Programme: see S Monks, "The Antipodean Lawyer's Rough Guide to UK Immigration Rules" (2001) 75 (1) ALJ 44 and www.workpermit.com. Restrictions on the "working holiday visa" to the UK were introduced on 8 February 2005: see further www.workpermit.com/uk/working_holidaymaker.htm. In practice, this means that young lawyers on the working holiday visa who wish to stay on in the UK must shift to the Highly Skilled Migrant Programme visa.

The UK is a traditional destination for New Zealand trained lawyers. The main options are study, law firms ("private practice"), industry and commerce ("in-house").

Tuition and living expenses for an LLM in the UK. are around NZ$60,000. There has always been a trickle of New Zealand lawyers taking the Oxford BCL or the Cambridge LLM and then going on to practise in London. Some then go across to New York. Some exceptional New Zealand candidates go straight from the Oxbridge LLM/BCL to New York without practising in London. This pathway has opened via US law firms in London conducting interviews for New York positions.

UK law firms actively recruit senior and middle ranking associates from New Zealand. If recruitment is done while in employment in New Zealand, then the UK firm will normally offer a transfer package. The London legal market is much larger, more diverse and specialised than New Zealand (only New York is comparable). As a result, one needs to pay close attention to the skill set one seeks to gain in London with a view to subsequent career development. New Zealand lawyers with post-qualification experience (PQE) bargain for recognition of that experience. Typically, New Zealand lawyers suffer a one-year discount (justified by the English training contract period). Conversely, the BCL or LLM from Oxbridge is counted as one year PQE. The UK market is more open to lawyers with two or more years' experience.

US law firms in London have pushed up pay rates at English firms beginning with first year lawyers at about £48,000-£51,000: see www.rollonfriday.com and *Lawyers Weekly*, 15 July 2005, 21 for salary rates. Consider also working hours, training and support available in UK and US firms: typically, working hours are lower and training and support is greater in UK firms. This trade-off is a perennial point of discussion in the London branch of the New Zealand legal diaspora.

Industry and commerce ("in-house") opportunities are much broader in London. Avenues include financial institutions, public retail, energy, manufacturing, telecoms, property/construction and media: for a market overview and salary details, see www.michaelpage.co.uk. As in New Zealand, working hours are lower, the work less "academic" and more closely involved with the client business.

The stream of recent graduates going to London as paralegals is less well known. Here, New Zealand admission is critical because New Zealand Bar admission enables qualification as a solicitor in England by way of the Qualifying Lawyer Transfer Test (QLTT). This exam can be done in the UK or offshore. The New Zealand Lawyers' Society in the UK provides helpful information: see www.nzls.co.uk. For example, a New Zealand solicitor in Sydney can sit the QLTT in Sydney prior to departure to the UK: see www.lawsociety.org.uk.

A New Zealand paralegal in London (whether working for a law firm or a company) is typically a recent graduate who has been admitted in New Zealand. Temporary paralegals in London typically earn around £15.80 per hour (less 25 per cent if an agency is involved) and time-and-a-half to double for weekend work. Banks and other financial services firms offer similar short-term contract work. A number of professional agencies (often staffed by New Zealanders or Australians) in London specialise in placements (eg Robert Walters). The anecdotal evidence is that a permanent paralegal can easily earn up to £35,000 plus per annum in London and up to £800-£1000 a week. Some paralegals

16 per cent flat in Hong Kong and on a sliding scale of up to 22 per cent (for salaries over S$320,000) in Singapore: see www.iras.gov.sg.

To get admitted in Hong Kong, lawyers from common law countries must pass four Overseas Lawyers' Qualification Exams unless they can demonstrate five years' post-qualification experience in which case they need only pass Conveyancing. A substantial proportion of candidates (over 50 per cent in some years) fail the exams. Hong Kong admission is not always necessary. Many foreign firms employ foreigners as Registered Foreign Lawyers, without the expectation that they will seek Hong Kong admission, on the basis that they are practising the law of their home jurisdiction in Hong Kong.

Admission in Singapore as an Advocate and Solicitor of the Supreme Court of Singapore will depend on the law school attended in New Zealand. Only some New Zealand law degrees are recognised for admission purposes in Singapore: see www.lawsoc.org.sg.ble/faq.htm. However, lack of Singapore admission does not prevent New Zealand law graduates from working in Singapore. Foreign law firms in Singapore are typically engaged in cross-border transactions. As such, foreign law firms in Singapore employ Registered Foreign Lawyers who hold a practising certificate in another jurisdiction.

Making the choice

Australia presents as a natural first choice for reasons of proximity and ease of access. Today, Asia ranks as the second choice. Although it is harder to get in to Asia, remuneration is the same or better than the UK or the US and tax rates are lower. The recent anecdotal evidence is that the US firms in Asia are hiring Australians and New Zealanders. Hiring is strong in Hong Kong as a result of the booming Chinese economy. Overall, Singapore and Hong Kong present as the best Asian options. The UK is ranked as a third choice. Here, common law tradition and culture appear as salient advantages. The US is the fourth choice as it is the most difficult destination for New Zealand trained lawyers. The consensus of those who have taken either the UK or US route is that two to three years in practice in New Zealand or Australia and good grades (graduation in the top 10 per cent of the particular New Zealand law school) is normally required. Generally, accessing the network of New Zealand trained lawyers who have already moved offshore for current lore is advisable.

Suppose, however, that the choice is between the US and the UK (all other things being equal). Now, global legal practice can be viewed as a competition between the US and UK law firms. In this context, there are some reasons for preferring the US. First, a New Zealand trained lawyer can readily adapt to UK law. By contrast, US law cannot be picked up as easily and so one gains a "premium" by acquiring a new skill set in the US. Second, study or practise in the US means exposure to another dominant legal system and salary levels are higher. Third, UK law firms may pay a premium for a New Zealand trained lawyer who has gained US experience. Fourth, US training means access to the international offices of US law firms. In this regard, UK firms have a stronger presence in Europe and the Middle East, are equal with US firms in Asia, and are less prominent in the Americas.

It is pertinent to discuss the option of an academic exchange year in the US. Some New Zealand universities offer students an exchange year in the US whereby the New Zealand student pays New Zealand tuition fees. This option is taken at undergraduate level. Thus, a Canterbury University law student might undertake a year at UC Berkeley and credit results to the LLB. The cost saving is US tuition. However, living costs in the US roughly equate with tuition and a New Zealand student might spend, say, NZ$20,000 plus living costs in an exchange year. This sum is better spent on a US LLM because the LLM formally qualifies the student within the US system.

Questions arising at this level involve closer consideration of the long-term strategy. For example, the risk/reward ratio for doing an LLM in the US and returning immediately to New Zealand is not good. If higher salary or abridging the career path is the aim, a period of practice in the US is required since this improves the risk/reward ratio and enables positioning for a similar level compensation package or fast track to partner on return to the Southern Hemisphere. A question which might arise (typically, with a third or fourth year associate in New Zealand) is whether or not to skip an LLM in favour of an MBA if, for example, investment banking is a long-term goal. This option has relevance for students with quantitative skills (eg LLB, B.Com with a major in finance). As to MBA programmes, see www.registration.ft.com/CareerAdvisor/MBARankings/reception.htm.

STRATEGIC IMPLEMENTATION

Strategic plans are fine but implementation is critical; better a second-rate strategy and first-rate implementation than the converse.

If one is hired as a solicitor in Australia or the UK, questions of implementation are minimal as a relocation package will accompany the offer and salary commences upon arrival. As the path to study in the UK or Australia is well known, this part of the article focuses on post-graduate study leading to practice in the US. Here, a commonly expressed view amongst young lawyers is that 60 per cent of the effort was expended on getting to the destination. Long time horizons and careful planning are required. In addition, there is a significant level of stress involved in planning the move.

The cost of an LLM in the US consists of two components — tuition (university fees) and living costs. Tuition fees vary from about US$20,000 to US$39,000. Living costs for a nine month LLM are in the range US$15,000-20,000. At one end of the scale, an LLM at the University of Texas at Austin costs US$24,000 tuition plus US$15,000 living costs. Current costs at Duke Law School for the LLM are about US$35,000 tuition fees plus US$17,000 living costs. However, some LLM programmes offer full or partial tuition waivers. In addition, some universities offer Residential Associate (RA) positions (comparable to tutors in New Zealand halls of residence) which largely solve the living cost issue. In theory, it is possible to obtain a tuition waiver and an RA position.

Applications for US law schools and New Zealand sourced scholarships are made in December the preceding year. Offers are made March-April and can generally be deferred for one year without cost if necessary. (The same time-frames apply to UK law schools.) US law schools offer few scholarships, but partial or full tuition waivers and RA slots fulfil the same purpose. The richest scholarship is the Hauser Scholarship offered by NYU Law School. Apply for a number of schools and review offers in March. At that time, cost questions will predominate. In New Zealand dollars, a US LLM may cost

recording. (This article is an attempt to remedy that deficit.) Knowledge about offshore options can arise within a given law school year but, because there is no recording mechanism or other means of transmission, such knowledge has a limited shelf life. By contrast, information is more readily available in the US and Australia.

Law degrees in Commonwealth countries follow a broadly similar pattern; however, law is always a post-graduate degree in the US. After gaining an undergraduate degree, US students sit the Law School Admission Test (LSAT) for entry to a Juris Doctor (JD) degree programme, three years of law studies broadly equivalent to the LLB in New Zealand. From first year onwards, US law students are thinking about career paths. One compelling reason is the level of debt assumed by US law students to finance their law studies. (A "ball park" figure is US$150,000.) In any event, there is abundant institutional memory amongst US law students about global career options via handbooks and in-school career services operations (most big US law schools operate in-house employment units): see R Montauk *How to Get into the Top Law Schools* (New York: Prentice Hall, 2004).

In Australia, Dolman Legal Search and Recruitment has a website which gives basic data on the move to Australia (for New Zealand lawyers) and career moves to London, New York, Hong Kong and Singapore for Australians: see www.dolman.com.au or email dolman@dolman.com.au. Similar intelligence can be found in Taylor Root, *Guide to Working Overseas* (2005): see www.taylorroot.com.au. This information does not appear to be widely known among New Zealand or Australian law students.

Information about offshore options, however, is not sufficient on its own. Information must be deployed in a meaningful fashion. In short, a strategy is required.

STRATEGY

Strategy is a subject taught in business schools where the obvious focus is on corporate strategy: see generally, Johnson and Scholes *Exploring Corporate Strategy* (6th ed, 2002) ch 1. However, the strategy formulation process has direct relevance to individuals who seek to attain medium-to-long term goals: for a brief review of key concepts, see (1999) 17 C&SLJ 467. As with corporations, individual strategy formulation has three elements:

- *Strategic analysis:* Here, the individual seeks to understand his or her strategic position. A typical tool is the so-called "SWOT" analysis (strengths, weaknesses, opportunities and threats). This level of analysis focuses on individual capabilities. The aim is to get a clear understanding of the individual's present strategic position (the analysis looks inwards). Strategic analysis then looks outwards to the "micro" operating environment (New Zealand and the local legal services market) and the "macro" operating environment (the outside world and the global market for legal services).
- *Strategic choice:* Here, the individual formulates, evaluates and chooses between the possible courses of action. The aim is to achieve some advantage for the individual through effective positioning (eg do I practise in New Zealand or elsewhere?). Matching individual capabilities with the operating environment is called achieving "strategic fit".
- *Strategic implementation:* The individual plans how the choice of strategy can be put into effect and manages the changes required.

STRATEGIC ANALYSIS

Ask this question: what business am I in? The answer is not as simple as it might first appear. For example, on reading this article you might say that I am in the law teaching business. I might reply that I am in the transportation business. (Gerry Garcia is supposed to have said about his band, the Grateful Dead, "We're not in the music business; we're in the transportation business.") Similarly, although you are studying to be a lawyer and hope to practise law, on close examination it may appear that you are not in the law business at all. The relevance of the question is that it forces one to think about outcomes and exit strategies. Thus, one might reason as follows: "I am in the law business for the purposes of capital accumulation and I hope to own a vineyard in Marlborough in the South Island of New Zealand at age 40". In strategy terminology, the answer to the question defines the mission (overriding purpose). Thus, let us suppose the mission is capital accumulation not law (to this extent you are not in the law business). The next question is, why? The answer might be to realise the personal vision of owning a vineyard. We then ask: how do I realise the vision? The answer is by formulating a strategy and here the first task is strategic analysis.

Individual SWOT analysis is relatively straightforward. *Strengths* include such items as superior law grades and language abilities. *Weaknesses* are average law grades (which might be remedied by an LLM) or simple lack of knowledge about opportunities in the legal services market. The salient *opportunity* is the arbitrage or pricing asymmetry between compensation packages paid in New Zealand and those offered offshore. (An arbitrage arises when an identical commodity is priced differently in two markets. Thus, if a second year associate can earn $50,000 in Auckland but $75,000 in Sydney then — all other things being equal — an arbitrage opportunity arises.) A *threat* is the length of time such an arbitrage opportunity or "window" might remain open.

Strategic analysis then turns to the operating environment. The first step is a comparison of the immediate and medium term status of the New Zealand economy vis-à-vis that of Australia, the UK and the US: see current country reports by the OECD and The Economist Intelligence Unit. As to New Zealand, there is little reason to disagree with the earlier conclusion of the *New Zealand Porter Report* — New Zealand is an anomaly in the global economy because first-world living standards are largely supported by a third-world export pattern: see Crocombe, Enright and Porter, *Upgrading New Zealand's Competitive Advantage* (1991), 55. As of 2005, it is hard to find compelling evidence that actions for the requisite structural adjustment have occurred. A second step is to examine the state of the market for legal services in New Zealand and elsewhere.

The legal debate about the market for legal services has been concerned with tensions between notions of "social trustee professionalism" and law as a commercial activity: see D Dawson, "The Legal Services Market" (1996) 5 J of Judicial Admin 147. From a management or economic standpoint, however, law is a service industry. A striking phenomenon of the contemporary, "globalising" world