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ARTICLE

Creditors versus Shareholders: *Primus Inter Pares*?

David Cowling, Partner, Clayton Utz, Sydney, Australia

Legislation recently passed by the Australian Parliament aims to restore the traditional subordination of shareholders to the creditors of failed companies.

The legislation is designed to overturn the 2007 High Court of Australia decision in *Sons of Gwalia Ltd v Margaretic*; *ING Investment Management LLC v Margaretic* [2007] HCA 1. The High Court held that shareholders who claimed to have been misled into buying shares in a company could rank equally with unsecured creditors in the company's liquidation.

Slow death of a doctrine

The theoretical basis of the doctrine of the maintenance of capital of corporations was the bargain between equity investors in, and creditors of, limited liability companies. Equity investors gained protection from personal liability, but had to accept that, if the corporation failed, creditors had first call on the capital that the investors had invested in the company.

The underpinnings of this theory are amply illustrated by *Oakes v Turquand* (1867) LR 2 HL 325:

> 'it would be monstrous to say that ... a shareholder ... having held himself out to the world as such, and having so remained ... could, by repudiating the shares on the ground that he had been defrauded, make himself no longer liable.'

Of course, the doctrine of maintenance of capital has not always been applied in any absolute way. In Australia, for example, the closing years of the 20th century saw considerable erosion in the form of the legalisation of share buy-backs and the issue of no par value shares. Nevertheless, the doctrine has never been fully and officially overturned.

At the beginning of the 21st century, the doctrine manifested itself in two important ways:

– s 563A of the *Corporations Act 2001* (Australia),[1] which postponed payment of the claims of shareholders qua shareholders until all other creditors have been paid out in full;

– the rule in Houldsworth's case (*Houldsworth v City of Glasgow Bank* (1880) 5 App Cas 317), which was that a subscribing shareholder could not recover damages from the company for fraudulent misrepresentation in connection with the subscription for the shares – the shareholder's only remedy was to seek rescission of the contract of allotment of shares (which would remove his name from the shareholders' register of members) and thereby to receive restitution of his application money.

In Australian company law, all unsecured creditors rank equally in a liquidation (with a few exceptions, such as the costs of winding up or the payment of employee entitlements). If there are insufficient funds to pay all creditors the full amount of the debts owed to them, the creditors are paid *'pari passu'*. However, as mentioned above, this general proposition was altered by s 563A. At the beginning of the 21st century, this read as follows:

> 'Payment of a debt owed by a company to a person in the person's capacity as a member of the company, whether by way of dividends, profits or otherwise, is to be postponed until all debts owed to, or claims made by, persons otherwise than as members of the company have been satisfied.'

Section 563A was traditionally regarded by liquidators as being a rule that 'shareholders come last'.

As noted above, the rule in Houldsworth's case is that a subscribing shareholder can only claim a return of his subscription money (on the grounds of misrepresentation, for example) if he rescinds his subscription contract. Rescission is a problematic solution if the company is insolvent. In Oakes, the House of Lords held that, once the winding up of a company has begun, a shareholder cannot rescind the subscription contract under which he acquired his shares. It would, therefore, seem to follow that a shareholder who subscribed

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1 And its English equivalents, such as s 74(2)(f) of the *Insolvency Act 1986* (Eng) ('Insolvency Act'). In broad terms, a similar principle informs corporate insolvency law in the USA in the form of s 510(b) of the Bankruptcy Code.

for shares could not lodge a claim against the company once the company was in liquidation.[2]

Sons of Gwalia

The continuous disclosure rules of the Australian Securities Exchange (ASX) require listed companies to make immediate disclosure to the market of information that would have a material effect on the price of the company's securities.[3] Sons of Gwalia was listed on ASX.

Mr Margaretic bought shares in Sons of Gwalia on market in August 2000. A day after his name was entered on the register of members, voluntary administrators were appointed to Sons of Gwalia. Sons of Gwalia reportedly had USD 845 million-worth of unsecured creditors, including US noteholders allegedly owed USD 284 million.[4]

Mr Margaretic claimed that Sons of Gwalia had failed to disclose its financial problems to ASX, as required by the continuous disclosure rules. He asserted an entitlement to damages arising from his purchase of shares in the company.

The voluntary administrators proposed a Deed of Company Arrangement (DOCA) to Sons of Gwalia's creditors. A DOCA is a statutory compromise between a financially-troubled company and its creditors. The Corporations Act makes a DOCA binding on the company and its creditors, but does not prescribe the terms of the deed. The DOCA proposed for Sons of Gwalia effectively included a term identical to s 563A of the Corporations Act. If the deed were approved, the conventional understanding was that the s 563A clone in the DOCA would postpone Mr Margaretic's claim for damages to the debt claims of other unsecured creditors.

Mr Margaretic asserted an entitlement to rank equally with other unsecured creditors. He and the administrators went to court. The central issue for the court was whether an on-market purchaser of shares was postponed by the deed provision that mimicked s 563A. The case thus became a proxy for a debate over the meaning of s 563A.

At first instance and on appeal, the Federal Court of Australia held that shareholders who claimed damages for an on-market purchase were not restrained by s 563A and so could rank equally with other creditors in respect of such claims.[5]

The administrators then appealed to the High Court of Australia, Australia's highest court. On 31 January 2007, the High Court dismissed the appeal.[6]

What the High Court said

By a majority of 6-1, the High Court held that Mr Margaretic's claim was not postponed by s 563A.

There were a number of separate judgments, but the overall view of the majority was that there is no overriding principle that 'shareholders come last', and that any common law rule tending to that conclusion could override the words of the statute.

The leading judgement of Hayne J discussed what was meant by s 563A's reference to 'a debt owed ... to a person in the person's capacity as a member of the company':

> '[T]he obligation which Mr Margaretic seeks to enforce is not an obligation which the ... Act creates in favour of a company's members. The obligation Mr Margaretic seeks to enforce, in so far as it is based in statutory causes of action, is rooted in the company's contravention of the prohibition against engaging in misleading or deceptive conduct and the company's liability to suffer an order for damages or other relief at the suit of any person who has suffered, or is likely to suffer, loss and damage as a result of the contravention. In so far as the claim is put forward in the tort of deceit, it is a claim that stands altogether apart from any obligation created by the ... Act and owed by the company to its members. Those claims are not claims "owed by a company to a person in the person's capacity as a member of the company". For these reasons, s 563A does not apply to the claim made by Mr Margaretic.'[7]

Implications

Not unsurprisingly, the High Court's decision in Sons of Gwalia created a lot of debate.

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2 The High Court of Australia followed Houldsworth's case in Webb Distributors v Victoria (1993) 179 CLR 15 (Webb Distributors). That case had concerned a claim for damages allegedly arising from misleading or deceptive conduct in a prospectus. The company itself was in liquidation at the time of the claim.

3 ASX Listing Rule 3.1. There are, of course, exceptions for matters such as incomplete business negotiations, but these are not relevant to Sons of Gwalia.

4 Sons of Gwalia Deed Administrators' Report Pursuant to section 445F of the Corporations Act, 14 June 2007.

5 *Sons of Gwalia Limited (Administrator Appointed) (ACN 008 994 287) v Margaretic* [2005] FCA 1305 ; *Sons of Gwalia Ltd v Margaretic* (2005) 149 FCR 227 at [51], [61] and [131].

6 *Sons of Gwalia Ltd v Margaretic; ING Investment Management LLC v Margaretic* [2007] HCA 1.

7 *Sons of Gwalia Ltd v Margaretic; ING Investment Management LLC v Margaretic* [2007] HCA 1 at [206].

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Bondholders and other traditional creditors argued that the ruling reversed longstanding principles underlying business incorporation and limited liability (as noted above, the incorporation 'bargain' – that, in return for effective immunity from liability for the company's debts, shareholders ranked behind creditors in the distribution of an insolvent company's assets).

It was argued that bondholders and other unsecured financiers would increase the cost of credit to cover the need to share the company's assets with a new class of creditors. Alternatively, they might simply withdraw from the Australian market completely:

> 'Connecticut lawyer Evan Flaschen acts for US bondholders, including institutions which are owed $450 million by Sons of Gwalia, ING among them.
>
> "The concern is that in any case shareholders will have the incentive to assert these claims," says Flaschen, from Hartford firm Bingham McCutchen.
>
> ...
>
> Flaschen says the response among US lenders is to put Australia in the too-hard basket. He says his clients are not interested in the finer points of the Federal Court decision or the lesson from the HIH decision that there is a real hurdle for shareholders to prove they relied on statements from the company when deciding to buy.
>
> "They can put their money anywhere they want. Why should they put it in Australia if this is how this issue is treated? What else can happen? The nuance about reliance or whatever, they don't care, it's not worth it to them."
>
> ...
>
> A pullback in the US would limit the ability of the big Australian banks to sell their debt if they prefer not to stick around to manage a floundering loan.
>
> Flaschen also predicts higher prices for Australian debt and, for some low-rated companies, difficulties issuing bonds at all.'[8]

Liquidators expressed concern about the delays caused by having to process large numbers of new and complex claims.

Shareholders, class action lawyers and litigation funders countered with the argument that the longstanding rule of 'shareholders come last' did not or should not apply where the shareholders had only become or remained shareholders because of misleading conduct by the company itself. They pointed out that such claims were unrelated to the rights and obligations of shareholders qua members of the company.

Some commentators also pointed out that Sons of Gwalia was something of a *'perfect storm'*:

- relatively unusually, it involved a failed company which had considerable valuable assets (ensuring a significant return for creditors and thereby holding out the hope of a return on investment for the litigation funders who would be running a class action for the shareholder-claimants);
- as a listed company, Sons of Gwalia was subject to the ASX continuous disclosure rules, thus creating a potential cause of action which would not be available for shareholders in the overwhelming majority of failed companies, which are unlisted.

Some comfort was also taken from the aftermath of Soden's case in England (or, more accurately, the lack of an aftermath).[9] The House of Lords decision is Soden did not appear to have resulted in a flood of shareholder claims against insolvent companies.[10]

What happened in Sons of Gwalia

The events that actually transpired after the High Court decision appear to show that, regardless of the merits of the competing theoretical positions, the decision did have real world impacts.

On 28 June 2007, the unsecured creditors of Sons of Gwalia – now including some of its shareholders – met to vote on two rival proposed transactions involving the company's tantalum assets.

In very general terms, one proposal was for a straight purchase of the tantalum assets; the other was a proposal to float a new company and to offer creditors the opportunity to take up shares in that company. A numerical majority of creditors opted for the straight sale proposal. A litigation funder who was supporting the shareholders was quoted in the media as saying:

> 'No-one's an expert in tantalum but everyone's an expert on the difference of having a dollar in your pocket and having it in someone else's pocket.'[11]

Notes

8 Elizabeth Sexton, 'Riff-raff slip into the creditors' queue', *Sydney Morning Herald*, 20 March 2006.

9 *Soden v British & Commonwealth Holdings plc* [1997] 4 All ER 353.

10 One theory is that this may have been, at least in part, to the fact that there was no litigation funding industry in the UK when Soden was decided.

11 *RCF wins battle for Sons of Gwalia asset* AAP, June 28 2007.

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An indication of the importance of the shareholders to the vote can be gained from the following figures: [12 13]

Type of creditor	*No. of creditors*	*Total value of claims*
Ordinary Creditor	922	USD 848.1 million
Shareholder Claimant	8,038	USD 577.0 million

As well as having a substantial impact on the administrators' disposal of the company's assets, the high number and complex nature of the shareholder claimants' claims required the administrators to adopt new procedures when conducting the administration.

Initial Government response

The Australian Government refrained from making any comment on the issues raised by Sons of Gwalia until the litigation had run its full course through the court system. Once the High Court had handed down its decision, the Government referred the matter to its specialist corporations law advisory body, the Corporations and Markets Advisory Committee (CAMAC).

The reality for CAMAC was that there were only two viable alternative conclusions: retention of the status quo (misled shareholders rank equally with unsecured creditors) or reversion to the status quo ante (shareholders come last). Despite this, CAMAC's December 2008 report, managed to canvass four options:

- 'maintain the current legal position, which treats aggrieved shareholders as ordinary unsecured creditor claims
- postpone those claims behind conventional unsecured creditor claims;
- maintain those claims as creditor claims but subject them to a monetary cap; or
- prohibit claims by aggrieved shareholders altogether.'

The reality, of course, is that the third and fourth options were not realistic. The suggested cap on shareholder claims was 10% of the net assets available for distribution to the unsecured creditors. Apart from the fact that this would not overcome one of the perceived problems with the High Court's decision – the complexity of handling shareholder claims – the cap would be a strong disincentive to litigation funders' assuming of shareholder-claimants' cases in Australia. A cap would therefore, in most cases, be a de facto prohibition on claims by shareholders.

CAMAC itself recognised that banning aggrieved shareholder claims altogether would be contrary to the current trend towards providing greater protection to investors.

In the end, therefore, CAMAC, faced with a choice between the status quo and the status quo ante, opted for the former:

> 'While members were not of the one view, the Advisory Committee as a whole is not persuaded of the need for change.'

The second Government response

The CAMAC report confirmed that there was no magic solution that would satisfy both sides of the debate.

In the face of this, it is perhaps not surprising that the Government did not respond to the report for over a year. What was surprising was that its response, announced on 19 January 2010, was to reject CAMAC's recommendations:

> '"Any direct benefits to aggrieved shareholders arising from non-subordination are outweighed by the negative impacts on shareholders generally as a result of restrictions on access to, and increases in, the cost of debt financing for companies,' Minister Bowen said.
>
> "The Government also remains concerned that the Sons of Gwalia decision has the potential to further increase uncertainty and costs of associated with external administration.
>
> "The decision has also been taken in light of the decision's potential negative impact on business rescue procedures."'[14]

Notes

12 Under the Corporations Regulations, a motion is only passed at a creditors' meeting if:
- it receives the support of the majority of creditors measured by *both* their numbers *and* the value of their claims;
- it receives the support of the majority of creditors measured by *either* their numbers *or* the value of their claims, *and* the chairman of the meeting votes for it.

13 Sources: Ferrier Hodgson, Deed Administrators' Report Pursuant to Section 445F of the Corporations Act, 2001, Sons of Gwalia Ltd ACN 008 994 287 (Subject to Deed of Company Arrangement) and certain of its subsidiaries as set out in the Schedule (All Subject to Deed of Company Arrangement), 7 December 2007, p. 6; Ferrier Hodgson, Circular to Creditors, June 2008.

14 The reaction to the Government's announcement was not overly enthusiastic, to put it mildly. Australia's leading financial newspaper, the Australian Financial Review was neutral-to-positive, with two stories headlined: 'Bowen says shareholders win' and 'Gwalia reversal gains industry approval'. Other major newspapers were less positive: 'Shareholders lose, banks win in new law' (*Sydney Morning Herald*); 'A slap in the face for shareholders as High Court judgment is reversed' (*The Australian*); 'Chris Bowen's decision will deny mistreated shareholders any recourse against the company' (*The Australian*); 'Shareholder rights eroded' (*Herald Sun*).

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Draft legislation was released for comment two months after this announcement and the resulting amendment Bill was introduced into Parliament just over a month later. The calling of a general election then delayed the passage of the Bill, which was not finally passed and operative until 18 December 2010.

Overview of the amendment Act

The amendment Act aims to address three issues raised or highlighted by the Sons of Gwalia situation.

The first issue was the finding of the High Court that shareholder-claimants' claims were not postponed by s 563A. The Act effectively reversed this decision by replacing s 563A with a new provision which provides that the payment of all claims in relation to the buying, selling or holding of shares is deferred to the payment of all other creditors' claims.

The Act then moved to address an issue highlighted by Sons of Gwalia, even though it was not a matter raised in the litigation: the voting rights of shareholder-claimants. The Sons of Gwalia litigation and the subsequent events (detailed above) showed that, no matter what their ranking vis-à-vis more conventional creditors, shareholder-claimants were undoubtedly creditors of their company (at least insofar as they had a claim against the company for misleading conduct in relation to their shares). The Act contained provisions aimed at curtailing shareholder-claimants' voting rights.[15]

Finally, the Act overturns the principle in Houldsworth, by removing any restriction on the ability of a shareholder to recover damages against a company based on how they acquired the shares or whether they still hold the shares.

The amendment Act in detail

As noted above, the key provision in the Act is a new s 563A:

> '563A Postponing subordinate claims
>
> (1) The payment of a subordinate claim made against a company is to be postponed until all other claims made against the company are satisfied.
>
> (2) In this section, subordinate claim means:
>
> (a) a claim for a debt owed by the company to a person in the person's capacity as a member of the company (whether by way of dividends, profits or otherwise); or
>
> (b) any other claim that arises from a person buying, holding, selling or otherwise dealing in shares in the company.'

The title of this new section is somewhat misleading: it postpones the payment of claims, rather than the claims themselves. As a result, therefore, the new s 563A does not address one of the major practical considerations arising out of Sons of Gwalia: the ability of claimant shareholders to use their votes as creditors in creditors' meetings. That issue is addressed by a new s 600H:

> 'A person whose claim against a company is postponed under section 563A is entitled:
>
> (a) to receive a copy of any notice, report or statement to creditors only if the person asks the administrator or liquidator of the company, in writing, for a copy of the notice, report or statement; and
>
> (b) to vote in their capacity as a creditor of the company, during the external administration of the company, only if the Court so orders.'

That these provisions aim to prevent shareholder-claimants' swamping creditors' meeting is made very clear by the Government's Explanatory Memorandum which accompanied the Act:

> '[T]here could be 5,000 aggrieved shareholders, all of whom would be entitled to be provided with information by the liquidator and to attend and vote as creditors at meetings, notwithstanding that upon subordination they may have no real interests in the outcome of the liquidation. Given their numbers and the limited funds available, their votes could significantly affect the efficacy of the liquidation and reduce the returns to other creditors. The amendments provide that such shareholders would now receive reports to creditors only after making a written request, and would now not be entitled to vote as creditors unless the Court grants leave.'

Finally, the abrogation of Houldsworth is achieved by the insertion of a new 247E:

> '247E Shareholding does not prevent compensation claim
>
> A person is not prevented from obtaining damages or other compensation from a company only because the person:
>
> (a) holds, or has held, shares in the company; or
>
> (b) has subscribed for shares in the company; or

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15 Of course, the Sons of Gwalia matter merely drew attention to the fact that, under the already-existing law, shareholder-claimants could vote with other creditors. The litigation did not create any new law in that regard.

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(c) has a right to be included in the register that the company maintains under section 169.'

This wording is very similar to s 111A of the Companies Act (Eng), introduced after Soden.

Problems with the amendment Act

Despite the time taken for its drafting, the amendment Act contains a number of problems.

The first of these is that the Parliament refrained from an outright ban on voting by shareholder-claimants. Instead, it opted to allow them to apply to a Court to be allowed to vote. The new s 600H does not provide the Court with any guidance on how it is to exercise its power. Faced with a new statutorily-unrestrained discretion, Australian Courts will normally have recourse to the official explanatory materials accompanying the amending statute and to the underlying history of the legal issues which prompted the amendment.

Unfortunately, they will not find much guidance in the case of s 600H. The Explanatory Memorandum to the Bill (quoted above) does not give any indication of the circumstances in which the Court might grant voting rights to shareholder-claimants. The only relevant comment is that allowing 5,000 shareholder-claimants to vote and to receive reports from liquidators 'could significantly affect the efficacy of the liquidation and reduce the returns to other creditors'.

This is not, presumably, intended to indicate that 5,000 is some kind of threshold figure, below which shareholder-claimants might be allowed to vote. The only policy objective discernible from the Explanatory Memorandum, therefore, is the more general one that shareholder-claimants' voting rights should be restricted because of their potential effect on unsecured creditors. This suggests that courts should only grant voting rights where the exercise of those rights would not affect the returns to other creditors – which rather begs the question of granting voting rights at all.

The issue of voting rights also lies at the heart of two other problems with the Act.

Application to voluntary administration

Sons of Gwalia was in voluntary administration. Voluntary administration is an insolvency regime established by Pt 5.3A of the Corporations Act. It allows a financially-troubled company to appoint an external administrator to take control of the company and, within a short timeframe, report to creditors on whether the company should be wound up or whether it should enter into a DOCA (as noted above, a binding debt arrangement between the company and its creditors). A DOCA becomes binding upon the company and its creditors when a majority of creditors vote to adopt it and the company executes it.

While the company is under the control of the voluntary administrator (i.e., before the vote by the creditors), there are no statutory rules for the payment of creditors or the order in which creditors are to be paid. The voluntary administrator will identify creditors for the purpose of voting on a DOCA, but has no power to pay those claims. A DOCA may (and usually does) set up a regime for the payment of claims (including which claims will be paid and the order in which they are paid). With only a few exceptions, the rules for the payment of creditors and the order of payment are set by the DOCA itself (the contents of which, in theory at least, are determined by the creditors, rather than by the Corporations Act).[16]

Both voluntary administration and DOCA therefore differ from liquidation: when a company is in liquidation, the Corporations Act requires the payment of creditors and provides a statutory order in which they are to be paid. That statutory order of payment for companies in liquidation now includes s 563A.

As noted above, the new s 600H purports to restrict the voting rights of shareholder claimants. It applies to a 'person whose claim against a company is postponed under section 563A.' However, as discussed, s 563A does not affect the payment of claims in voluntary administration or under a DOCA (unless the creditors vote to incorporate it into the DOCA). Does this mean that the new s 600H does not apply to creditors' voting rights in voluntary administration or under a DOCA?

It appears that the intention of the legislature was to prevent shareholder-claimants' voting without court approval in a voluntary administration or under a DOCA:

> 'The Bill inserts a definition of external administration clarifying that the reforms to voting rights and the right of creditors to receive reports, as contained in the Bill, apply to voluntary administrations, deeds of company arrangement, voluntary and involuntary liquidations, provisional liquidations and schemes of arrangement.'[17]

Despite this intention, it is more than arguable that the wording of s 600H does not achieve the intended effect. In order to give effect to the section, a court would have to read it as applying to 'a person *the payment of* whose

Notes

16 It will be recalled that the Sons of Gwalia litigation was triggered by a DOCA which, by incorporating the then-section 563A, purported to postpone the payment of claims by shareholder-claimants.

17 Revised Explanatory Memorandum to the Corporations Amendment (Sons of Gwalia) Bill 2010.

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claim against a company *would be postponed* under s 563A *if the company were being wound up under this Act* and *if the claim were being made in that winding up*'.

It is not beyond the bounds of possibility that a court would baulk at such a major rewrite of a statutory provision.

Schemes of arrangement

Like many other jurisdictions with roots in English company law, Australia has a court-supervised statutory corporate reconstruction regime called 'scheme of arrangement'.

This is considerably older than the voluntary administration regime, although it shares some of the same policy objectives (e.g., allowing a financially-troubled company to enter into a binding arrangement with its creditors). Two key elements of a scheme of arrangement under s 411 of the Corporations Act are:

- a separate scheme is required for each class of creditor;
- a scheme will only be binding on a class of creditor if the Court orders that a meeting of that class be held and the meeting ordered votes in favour of the scheme.[18]

During the passage through Parliament of the Sons of Gwalia Bill, the Bill was examined by a Parliamentary Committee. The Committee appears to have concluded that shareholder-claimants would not be bound by a scheme of arrangement if they were not able to vote on it. The Committee's reasons for reaching this conclusion were somewhat confused. It is unclear whether it believed that:

- non-voting shareholder-claimants would not be bound by a scheme because their inability to vote would mean that they would constitute a separate class of creditor and, since the class could not vote on the scheme, would not be bound by the scheme; or
- non-voting shareholder-claimants would not be bound by a scheme because, even though they might belong to the same class as other unsecured creditors, a scheme would only be binding on creditors who had an entitlement to vote on it.

The second proposition does not appear to be supported by the wording of s 411. In fact, when one looks at the evidence presented to the Committee by the Government Department responsible for the Bill, it appears that the first proposition is the correct one:

> 'It is Treasury's understanding that [these] concerns may be addressed by amendments that would have the effect of providing that a [scheme of arrangement] would be binding on [shareholder-claimants] who had not been given leave to vote, despite the fact that a meeting of *that class of creditors* had not been ordered by the Court … .'[19] (emphasis added)

As a result, amendments were made to the Bill to address this issue. Those amendments took the form of a new s 411(5A):

> '(5A) If the compromise or arrangement:
>
> (a) involves creditors of the Part 5.1 body with subordinate claims (within the meaning of subsection 563A(2)) [i.e., shareholder claimants]; and
>
> (b) is approved by the Court;
>
> those creditors are also bound by the compromise or arrangement despite the fact that a meeting of those creditors has not been ordered by the Court under subsection (1) or (1A).'

The reference to 'the fact that a meeting of those creditors has not been ordered by the Court' supports the view that shareholder-creditors constitute a separate class of creditor. However, if this is correct, the necessary condition required by the opening words of the new provision is a nullity. As already pointed out, a scheme will only bind a single class of creditors. If it is correct that shareholder-claimants are a separate class and if the court has not ordered a meeting of that class, then there is no scheme that 'involves' those creditors within the meaning of s 411(5A)(a).

Conclusion

The Sons of Gwalia situation was never going to be a simple one. It highlighted the fact that you cannot incorporate two apparently contradictory policy objectives in the same piece of legislation. At the end of the day, if there is only a limited pool of funds available for distribution to the victims of a corporate collapse, some difficult policy decisions have to be made.

In the end, the Australian legislature decided that investor protection had to take second place to ensuring the ready availability of credit to Australian companies. Whether the result will be good for companies, creditors and investors in the long term remains to be seen.

That said, it is difficult to reconcile the five year timeframe within which this issue played out with the deficiencies in the drafting of the legislative response.

Notes

18 These are necessary, but not sufficient, conditions: see s 411 for further details.
19 Australian Government, The Treasury, Letter to Senate Standing Committee on Legal and Constitutional Affairs, 12 November 2010.

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International Corporate Rescue

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