Pro Image Shares 46342199 April 1991

Pro Image shares issues 1991

Pro Image bankrupt share issue 1991

92,684,398 Shares @ 0-50 cents each $46,342,199

Pro Image bankrupt share issue 1991

March – April 1991 Supreme Court of Victoria Judgment CTB BNZ v Pro-Image Studios debt http://law.ato.gov.au/atolaw/view.htm?DocID=JUD%2F4ACSR586%2F00002

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Pro Image bankrupt share issue 1991

ASIC letter March 2015

Page 1

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Page 2

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Pro-Image v Comm Bank 1991

http://law.ato.gov.au/atolaw/view.htm?DocID=JUD%2F4ACSR586%2F00002

Pro-Image Studios v. Commonwealth Bank of Australia

(1991) 4 ACSR 586

(1991) 9 ACLC 671

(Judgment by: Fullagar J.)

Pro-Image Studios

v. Commonwealth Bank of Australia

Court:

Supreme Court of Victoria

Judge:

Fullagar J

Hearing date: 26 March 1991

Judgment date: 24 April 1991

Melbourne

Judgment by:

Fullagar J.

The plaintiff company applies by summons on originating motion for the following relief:

A declaration pursuant to s 36 of the Supreme Court Act 1986 (Vic) that an issue to the defendants of 92,684,398 fully paid ordinary shares of 50c each in the capital of the plaintiff, for a consideration consisting of the release of debts amounting to $46,342,199 due by the plaintiff to the defendants, is not an issue of shares at a discount within the meaning of s 190 of the Corporations Law.

Both Mrs Campbell for the defendant banking companies and Mr Nettle for the Australian Securities Commission supported the making of the declaration.

They supported, and indeed Mr Nettle added to, the arguments in favour of the declaration which were put by Mr Beaumont QC, who with Mr Strong appeared for the plaintiff company. As to declaratory relief per se, Mr Nettle referred me to the useful compendious summary appearing in Aronson and Franklin's work entitled Review of Administrative Action at pp 465-6.

The company is insolvent. If it were now wound up its shareholders and unsecured creditors would receive nothing while the 2 secured banks would receive something like 91c in the dollar. The 2 secured banks--that is to say the defendant banks--are effectively owed by the company one debt of $46,342,199 which is now due and payable.

The company's share capital consists of shares of a nominal value of 50c each. The company and the banks have in effect agreed in the events which have happened that the company shall issue to the banks 92,684,398 shares fully paid up to 50c and that the banks shall pay for the allotment of shares by releasing their debt of $46,342,199.

About 2800 shares in the company have so far been issued and they have been trading on the stock exchange at prices around 5c per share up to the time of the hearing in the Practice Court. If the proposed conversion of debt to equity is carried out, it will bring about a surplus of assets over liabilities arising from the elimination from the liabilities of the debt of $46m-odd and an increase of the same amount in shareholders' equity, having the effect of creating a real net asset value for all of the issued shares.

It therefore appears that the proposed issue of shares to the 2 defendant banks will be greatly to the benefit of shareholders and unsecured creditors. Section 190 of the Corporation Law provides, as have the Companies Acts for many years, that except in stated circumstances a company may not issue shares at a discount. All parties concerned in the present case have some fear that if the proposed transaction is carried through it may subsequently be set at nought or worse by being held by a court to have involved the issue of shares at a discount. This fear arises by reason of the decision and reasoning of Young J in the Supreme Court of New South Wales in Re Jarass Pty Ltd (1988) 3 ACLR 728 .

In that case a scheme of arrangement was proposed whereby most creditors of a company would accept about 12c in the dollar in full satisfaction of their debts whilst other "internal" creditors would not be paid the 12c but would each be allotted one redeemable cumulative preference share of $1 for each dollar of indebtedness. No money was tendered or to be paid for these shares but the company's liability to the internal creditors would be fully satisfied by the allotment of the shares.

Young J held that the scheme did involve the issue of shares at a discount. It seems that his Honour took the view that, since upon a distribution on winding up the internal creditors would have received only 12c in the dollar, the company would really receive from the internal creditors the release of 12c in the dollar or at all events a release of very much less than 100c in the dollar. It seems that his Honour relied in part upon the reasoning of the House of Lords in Ooregum Gold Mining Co of India Ltd v Roper [1892] AC 125 .

Of course, I cannot be sure of all the facts which were before Young J in Re Jarass Pty Ltd but, upon the facts only which are disclosed in the report, I am respectfully of the view that his Honour was in error in holding that there was an issue of shares at a discount and that his decision on that question should not be followed in this court.

What had occurred in the Ooregum case was an issue of shares, as fully paid up, for a consideration less than the nominal value of the shares issued, and the remarks of the Law Lords cited by Young J were, I think, directed to that situation alone. When Lord Macnaghten spoke of "payment in full" he meant payment of a sum equal to the nominal value of the shares. In argument at 128-9 Mr Rigby QC said, correctly in my opinion, that the "consolidated appeals raise the same question, viz, whether a limited company registered under the Companies Acts of 1862 and 1867 can issue shares as fully paid up upon which a less sum than the nominal value has been paid". In that case the court did not consider whether any released debt was equal to the nominal value, because what was paid was 15 shillings actual cas h for shares of P1 nominal value.

In my respectful opinion Young J was in error in Jarass in countenancing the proposition that one could value the debt released by the subscribers--that is to say the internal creditors--as something less than the full amount of the debt which was at law immediately due and payable, and in error--at least under Victorian law--in holding that there could be no set off of the amount of that debt against what was due as the full nominal value of the shares issued. It is the debt which is released that counts, not some assessed value to the creditor of the debt owed to him based upon prospects of realisation or execution of or upon the debt.

Provided that the debt was genuinely created in the course of the company's business--a matter which in my opinion distinguishes the case of Mosely v Koffyfontein Mines Ltd later referred to--and provided that it is immediately payable, as is the liability to pay for the shares proposed to be allotted to the creditor, the issue of shares in consideration of the extinguishment of a debt of a sum equal to the nominal value of the shares issued is not an issue at a discount but in an issue for a payment in cash equal to the nominal value of the shares: see Re Harmony and Montague Tin and Copper Mining Co (Spargo's case) (1873) 8 Ch App 407 . In that case James LJ said this, at 412-3:

But if a transaction resulted in this, that there was on the one side a bona fide debt payable in money at once for the purchase of property and on the other side a bona fide liability to pay money at once on shares, so that if bank notes had been handed from one side of the table to the other in payment of calls they might legitimately have been handed back in payment for the property, it did appear to me in Fothergill's case and does appear to me now that this Act of Parliament did not make it necessary that the formality should be gone through of the money being handed over and taken back again; but that if the two demands are set off against each other the shares have been paid for in cash.

If it came to this, that there was a debt in money payable immediately by the company to the shareholders and an equal debt payable immediately by the shareholders to the company and that each was accepted in full payment of the other, the company could have pleaded payment in an action brought against them, and the shareholder could have pleaded payment in cash in a corresponding action brought by the company against him for calls.

Supposing the transaction to be an honest transaction, it would in a court of law be sufficient evidence in support of a plea of payment in cash, and it appears to me that it is sufficient for this court sitting in a winding up matter. Of course, one can easily conceive that the thing might have been a mere sham, or evasion, or trick, to get rid of the effect of the Act of Parliament, but any suggestion of sham, or fraud, or deceit seems to be entirely out of the question in this case, because everybody in the company knew of the transaction; every shareholder of the company was present, and was a party to the resolution. There was no deceit practised on any creditor, nor was there any registration of these shares except as shares paid up. This seems to me to dispose of the case.

It seems to me that this last part of the passage from the judgment of James LJ reads directly on to the present case. In this case every shareholder of the company knows of and is in a sense a "party" to the transaction by reason of resolutions that have been passed.

It seems to me that no deceit has been practised on any creditor in any way. Reference might also be made to the case of Arsene A Laroque v Beauchemin [1897] AC 358 .

In FCT v Steeves, Agnew and Co (Vic) Pty Ltd (1951) 2 CLR 408 at 420-1, Dixon J said this:

If cross-liabilities in sums certain of equal amounts immediately payable are mutually extinguished by an agreed set-off, that amounts to payment for most common law and statutory purposes: 'Nothing is clearer than that if parties account with each other and sums are stated to be due on one side, and sums to an equal amount due on the other side on that account, and those accounts are settled by both parties, it is exactly the same thing as if the sums due on both sides had been paid. Indeed, it is a general rule of law, that in every case where a transaction resolves itself into paying money by A to B and then handing it back again by B to A, if the parties meet together and agree to set one demand against the other, they need not go through the form and ceremony of handing money backwards and forwards' (per Mellish LJ in Spargo's case)... But for the application of these principles there must be cross-liabilities and agreement, express, tacit or implied, and the cross- liabilities must be equal.

It is true that Sir Owen Dixon added that the cross-liabilities must be equal but the point made, in my opinion, is that it is the 2 liabilities that must be equal, the 2 causes of action immediately payable, not some assessed value of the prospects which one or each side respectively has of executing for a judgment upon the cause of action once obtained. It is to be observe d too that his Honour emphasised

that there must be an agreement, express or implied, to set one liability off against the other.
In my opinion there is no authority for making the inquiry, opened up by the reasoning of Young J in Jarass, into the financial capacity of the issuing company to pay the creditor-allottee the amount of the latter's presently payable debt, that is to say in the absence of some fraud or deceit.
In Fadden v FCT (1945) 70 CLR 555 it was unsuccessfully argued that a transfer of shares in consideration of an immediately enforceable promise to pay for them was a gift. At 559 of the report Latham CJ said:
"In my opinion it is impossible to say that such a promise is an inadequate consideration and it has not hitherto been suggested that a distinction should be drawn between such promises as consideration by reference to the financial capacity of the promisor to pay. Entry into such matters to determine the 'real consideration' or the 'adequacy' of the consideration under such provisions as those now under consideration would open up an entirely new field of inquiry, an inquiry for which there appears to be no authority for making."
In my opinion, the same applies to the present case. The value of a debt for all purposes of the present case is the face value of the legally and immediately enforceable obligation constituted by the debt itself. If this were not so the long established principle above stated by Dixon J could not be correct. As Gibbs J said in Bray v FCT (1971) 123 CLR 348 at 360, Fadden's case "shows that, in valuing a promise to repay, it is not right to consider the financial capacity of the promisor to repay".
On the facts before me there is no suggestion of deceit or fraud and no suggestion 0that the proposed transaction is other than bona fide. In Jarass, Young J at 730 of the report is reported to have said that there were "at least three answers" to the unsuccessful arguments of counsel in that case. The first was that: "Set off does not exist in New South Wales any more except as some procedural device under the Rules of Court. Accordingly, an obligation to pay $1 is not extinguished by the mere fact that there is an obligation on the obligee to pay the obligor $1 also."
To this I would say, with respect, that of course statutory set-off may be viewed as a procedural device irrelevant to that case and to the present case: see In Re K L Tractors Ltd [1954] VLR 505 especially per O'Bryan J at 507 in the passage commencing "Set-off is the creature of statute". But what is referred to by Dixon J, and what is relevant to the present case, is an agreement to set off 2 cross-obligations.
It is not the "mere fact" of the obligation upon the obligee that matters but the bipartite agreement to set off the 2 obligations. I have found no authority upon the second of his Honour's answers and the

third has no application on the facts to the present case. The case of Mosely v Koffyfontein Mines Ltd [1904] 2 Ch 108 is in my opinion distinguishable on the ground that there the debt to the proposed subscriber was contrived to enable an issue to be later made against it.

The only anxiety I have felt about the present case, in addition to that occasioned by my differing from another judge, is upon the question whether all the relevant facts are before me with sufficient precision to justify a declaration in the form sought. The original court file has been "lost" but all the parties appearing before me, including the Australian Securities Commission, have assured me that the substitute file of documents put before me is accurate and adequate. All are agreed that the debt is owed by the company to the defendants, Commonwealth Bank of Australia and BNZ Securities Australia Ltd and is debitum in praesenti, immediately enforceable against the company. I understand that BNZ Securities succeeded to the debt as assignee of the Bank of New Zealand.

In these circumstances I am of the opinion that it is proper to make a declaration in the following terms, which are only slightly different from those proposed.