PROJECT FINANCING

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1. INTRODUCTION

During the past few decades, Australia has witnessed the development of numerous large property and resources projects. The financing of these projects has exposed financiers, customers and their lawyers to considerable challenges. The intention of this paper is to briefly explore in the context of project financing some of the issues relating to the choice and effectiveness of the various forms of project structures and securities commonly taken by lenders.

Project financing traverses many areas of law, including the principles of the law of contract, property, securities, companies, equity, taxation and stamp duty. Frequently various aspects of international law also intrude. In addition, each project has to be assessed in its particular statutory context. The topic is immense and hence this paper does not purport to be exhaustive.

2. CHOICE OF FINANCING STRUCTURE

2.1 Commercial Considerations

Project financings are often extremely complicated; each finance package is different for it is usually tailored to meet the needs of the particular project. Various factors need to be considered in evaluating a project and how the finance package might best be structured. Commercial influences, which are usually assessed by the financier and its customer at the outset include:

2.1.1 The Project's Viability

The commercial viability of the project is obviously vital, as the lender will usually be looking to the project's cash flows and earnings to service the loan repayments. This analysis would require an evaluation and allocation of various risks. The nature and extent of these risks obviously varies from project to project. It is therefore suggested that, when approaching a project as a lawyer for lenders, it is more appropriate to assess risks, not on the basis of some pre-determined list, but from an independent examination of the likely requirements for the successful operation of the project. One should enquire who is bearing the risk of those requirements not being met and then determine the means by which the lender can reasonably satisfy itself that those requirements shall be met and the consequent risk minimised.

In this context, risks commonly considered include:[1]

(a) Completion Risk

The possibility that a particular project will not be completed within an acceptable time frame exists for a variety of reasons, eg, cost overruns, financial failure of the participants, labour difficulties or industrial disputes, physical destruction of project assets, or events of force majeure.

(b) Resource Risk

In the case of a mining project, there exists the risk that mineral reserves will prove to be less than those originally estimated.

(c) Operating Risk

The ability to operate the project on a continuing basis within acceptable economic and technical parameters demands a consideration of such factors as the secure availability of proven technology, a competent labour force, an expert operator and skilled management.

(d) Market Risk

Except where the project product is assured of a stable market, financiers would normally require evidence of appropriate sales contracts, which are sufficient to cover debt service, operating and other costs.

(e) Currency Risk

Fluctuations in currencies can undermine the viability of a project where, for example, project product sales are generated in a currency which differs from the currency of the financing.

(f) Political Risk

Political risk is an element present in all financings but is frequently unacknowledged. It encapsulates the myriad of possible forms of government interference in the project itself or the income or product generated by it, eg, forfeiture of project tenure, the imposition of new taxes, government imposts such as stamp duty, rail freight, royalties, harbour dues and the like, export prohibitions or price controls. Also included are any other approvals concerning the development and operation of the project, including, if necessary, foreign investment approval. In light of the relatively recent increase in environmental concerns in the community, lenders will also have to consider the implications of the project on the environment. The potential exposure of lenders (and receivers appointed by them) under various State environmental legislation will be an area of particular concern in most significant projects.

The above list is not exhaustive.[2]

2.1.2 Credit Status of the Relevant Parties

The extent to which recourse to the customer, as opposed to the project, is to be limited also falls for consideration. This will entail a credit appraisal of the customer and its associates which, even in the most attractive of projects, will be relevant to the "mix" of

full recourse and non-recourse elements, the reliance placed on security, completion covenants and other forms of support to be given by related companies.

2.1.3 Method of Financing

Project financing packages vary to meet the needs of the particular project. Project finance may be funded by various financing methods (for example, debentures, bonds, term debt, leasing, etc) as illustrated by MIM's Newlands and Collinsville coal projects in Queensland, the funding of which included:

(a) a Euronote facility;

(b) a commercial paper facility;

(c) Eurodollar and Japanese production loans; and

(d) an Australian bill facility.[3]

To permit borrowers to overcome borrowing limitations imposed in debenture trust deeds or other loan agreements, various methods have been developed to effect off balance sheet financings including:

(a) establishing a project vehicle to act as borrower which did not satisfy the subsidiary requirements under the companies legislation, thereby avoiding the necessity to disclose the project vehicle's borrowings as a liability in the sponsor's consolidated accounts;[4]

(b) financial leases;

(c) leveraged leases;

(d) forward sale and purchase agreements;

(e) production payments;

(f) take or pay agreements; and

(g) letters of comfort or awareness or Keep-Well Agreements.[5]

The attractiveness of some forms of off-balance sheet financing is diminishing as accounting standards become more stringent.

3. LEGAL CONSIDERATIONS - PROJECT STRUCTURE

The size and complexity of many projects demand the collaboration by a consortium of participants with sufficient financial strength and expertise to bring the project to fruition. This is normally achieved by the sponsors participating in some form of joint venture.

3.1 Categories of Joint Venture

Joint ventures fall into three basic categories:

(i) incorporated joint ventures;

(ii) unit trust joint ventures;

(iii) unincorporated joint ventures.

Much has been written in recent years on each of these categories of joint venture and hence only some brief observations shall be made in respect of them.[6]

3.1.1 Incorporated Joint Ventures

An incorporated joint venture (also known as equity joint venture, corporate joint venture, joint venture company) is one in which the joint venture parties arrange for the incorporation of a separate vehicle to undertake the project on their behalf. The joint venturers' interests are usually represented by their respective shareholdings in the joint venture company.

The principal advantage of this type of joint venture structure has usually been perceived to be the limited liability which attaches to the participants as shareholders. However, this advantage has been subjected to increasing attacks with the introduction of provisions in the Companies Code and the Corporations Law (ss556 and 592 respectively) which are aimed at piercing the corporate veil to extend liability in certain circumstances to directors personally. There are various recent examples where successful attacks have been waged on directors.[7] Notwithstanding the more tolerant judicial stance adopted in **Brosnan's Case**,[8] the stricter approach to directors' liability for company debts (as evidenced in **Morley's Case**[9] and **Eise's Case**[10]) is to be given statutory backing under the proposed Corporate Law Reform Bill 1992 so as to impose a positive duty on directors to prevent insolvent trading and to remove the possible current defence which "rewards" directors for being totally ignorant about the operations of their company.[11]

In the shareholder context, whilst earlier it appeared correct advice to state that a corporation gave limited liability and unincorporated structures did not, those two basic contentions are now also under some threat.

A shareholder can now in some circumstances have liability despite incorporation. Some such examples include:

(a) Section 60 of the Corporations Law

Section 60 defines "director" for the purposes of the Corporations Law.

This section defines a director to include "a person in accordance with whose directions or instructions the directors of the body are accustomed to act" (s60(1)(b)).

Clearly, if in an incorporated joint venture the board of directors is accustomed to act in accordance with the instructions of one of the shareholders, that shareholder may be liable for any failure of the joint venture as a director of that incorporated body.

(b) Section 186 of the Corporations Law

Section 186 renders members of a company severally liable for the payment of any debt of the company contracted at a time when the company has carried on business for more than six months while the number of members is reduced below the permitted statutory minimum number of members (which is two in the case of a proprietary company and five in the case of a public company).

(c) Directors' Indemnity

A number of companies quite properly seek to provide some indemnity to their representatives on joint venture boards. Indeed it has become usual for such indemnity to be granted.

The result, despite the limiting provisions of s241 of the Corporations Law, is that there will be situations where a director is liable and that indemnity effectively sheets the liability home to the shareholder even in an incorporated situation.

It is also no longer true that all unincorporated joint venture vehicles will not provide some limited liability.

Reference is made here primarily to limited partnerships, the establishment of which is now accommodated under separate legislation in various States.[12]

(d) Agency

Although it is normal for the joint venture documentation to deny an agency, the contents of the documents may not always be traced to a third party over the course of the management of a joint venture. The doctrine of ostensible authority may well introduce liability of the participants in a joint venture to third parties.

(e) Tortious Liability

Liabilities may be incurred arising out of tort where a court, in the event that a joint venture management vehicle cannot satisfy the judgment,will find it easier to attribute liability to the joint venturers directly.[13] Insurance cover should always be considered carefully in this context.

The principal disadvantage of an incorporated joint venture is that gains and losses are locked in at the joint venture vehicle level.

3.1.2 Unit Trust Joint Ventures

As is now well known, a unit trust is a variation of the ordinary trust, its principal distinguishing feature being that the beneficial interest in the trust property is divided into units which may be independently dealt with by their holders.

The concept of a trust does not mean that there is a separate legal entity at law but rather that certain property is impressed with the trust thereby creating beneficial interests in it. A unit trust joint venture necessitates the appointment of a trustee as the custodian of those interests, both to hold the property and to be bound by the interests impressed by the trust on that property. Usually the trustee is a company formed by the participants and often it has the dual role of trustee and manager of the joint venture. Generally, although not necessarily, its shareholding is constituted in the same manner as the unitholding in the trust.

The main advantage of this type of structure is that gains of the joint venture are dealt with in accordance with the respective unitholders' tax regimes and accordingly each unitholder may deal with those gains in the manner most advantageous to it. In the case of public trading trusts, legislative inroads have reduced the benefit of this advantage as public trading trusts are now liable to be treated as companies for taxation purposes under the Income Tax Assessment Act.

The principal disadvantage of unit trust joint ventures is that losses are trapped within the trust. This effectively means that gains of the trust may ordinarily be offset against losses of the trust, but where those losses exceed the gains, the respective beneficiaries' proportionate interests in those losses are not available to be offset against income of those beneficiaries from other sources.

Another disadvantage of the unit trust is that one cannot say unequivocally that the use of a unit trust will provide limited liability for the unitholders. Whilst significant strides have been made in terms of providing more definite provisions limiting unitholders' personal liability in unit trust deeds, no legislation has yet been promulgated to put to rest the argument which has raged for so long as to whether unitholders have any residual liability for the actions of their trustee.[14]

3.1.3 Unincorporated Joint Ventures

An unincorporated joint venture is an association of investors which lacks both corporate form and equity capital. It is frequently called a contractual joint venture. It is brought into existence by a contract under which investors undertake a joint commercial activity. The joint venturers will often hold their interests in the joint venture property directly (for example, as tenants in common) although to facilitate dealings with third parties and the administration of the joint venture itself, there is frequently interposed on the title to the property a nominee which holds the property as bare trustee and also sometimes serves as the manager of the joint venture.

Unincorporated joint ventures can be further categorised into:

- those which are partnerships; and
- those which are not.

The main advantage of this type of structure is that the primary taxation incidence occurs at the level of the respective joint venturers, as there is no intervening legal entity through which gains and losses must pass. It is also regarded as more flexible than incorporated and unit trust joint ventures.

The principal disadvantage is the apparent difficulty which the courts confront in distinguishing an unincorporated joint venture from a partnership. In the context of an unincorporated joint venture, the joint venturers would normally be endeavouring to establish that they are only severally liable for their respective interests in the joint venture. However, in the partnership context, the consequence would be that they would become jointly liable for all debts of the joint venture.

3.2 Joint Ventures and Partnerships

If the project to be funded has been structured in the form of a joint venture, it is an important question from a financing viewpoint whether the joint venture as a matter of law constitutes a partnership. The main considerations from a lender's viewpoint which flow from this distinction stem from various well established principles of partnership law which are as follows:

3.2.1 A partner generally has power to pledge the credit of his fellow partners within the scope of the partnership business. A joint venturer will usually be denied this power by the joint venture agreement.

3.2.2 Every partner has a right to have partnership property applied in payment of the debts and liabilities of the firm. The Partnership Acts recognise this right on the occasion of the dissolution of the partnership. This right is often described as a lien over partnership property. By way of contrast, joint venturers have no such lien as is enjoyed by partners. In practice in the joint venture agreement the rights of a chargee taking under security given by the joint venturer are subject to the rights of the other venturers, which rights may include a prior cross charge on at least some of the venturer's property.

3.2.3 A partner has no title to specific partnership assets. A partner's interest constitutes merely a right arising upon dissolution to a proportion of the surplus remaining after realisation of all assets and payment of partnership liabilities.[15]

In contrast to that of a partner, a joint venturer will generally have:

(i) a proprietary interest in each of the joint venture assets as a tenant in common; and

(ii) certain rights or *choses in action* represented by the joint venture agreement and related agreements.

3.2.4 The claims of partnership creditors against partnership assets have priority over the claims of creditors of each separate partner.[16] If the joint venture is in legal reality a partnership, it follows that the lenders cannot obtain a security over the borrower's interest in the property of the joint venture which will enjoy priority over other joint venture creditors.

It is important therefore that the distinction between joint ventures and partnerships be maintained. But just what are those critical distinguishing features?

The term "partnership" is defined in the Partnership Acts as being "the relation which subsists between persons carrying on a business in common with a view of profit".[17] There are accordingly three essential elements, all of which must be satisfied, if a particular relationship is to be classified as a partnership:

- a business must be carried on;
- it must be carried on by persons in common; and
- there must be a view of profit.

It has been contended that the first element contemplates a notion of continuity so that isolated transactions not intended to be repeated would not satisfy the partnership test. However, the High Court has afforded little weight to this aspect of the test of partnership. In **Canny Gabriel Castle Jackson Advertising Pty Ltd v Volume Sales (Finance) Pty Ltd,**[18] the High Court held the relationship there described as a "joint venture" to be a partnership notwithstanding that it was a "once only" relationship between the promoter and financier.

The High Court's stance in this regard is fortified by the provisions of some of the Partnership Acts which expressly contemplate that there might still be a partnership for a single adventure or undertaking.[19]

The second "in common" element is far more critical in differentiating unincorporated joint ventures from partnerships. Gerald L J Ryan observes, in the case of a typical mining joint venture:

> "... the parties own the joint venture assets as tenants-in-common; they jointly make decisions affecting the project; they jointly appoint a manager/operator to work the project on their behalf; they share the costs of developing and working the project; and they share in the production. These activities would constitute the activities of the business, and would appear to be carried out in common. However it might be argued that the business which is carried on is not carried on in common. The venturers sell product separately and not in common. The exploration, prospecting, development and production activities are not actually carried out by the venturers. There are no common activities (ie, the business) carried out by them. The activities are carried out by the manager/operator instead".[20]

R A Ladbury also contends forcefully that if the typical mining joint venturers are carrying on business they are not carrying on a common business by using common assets and contributing to common expenses:

> "The whole rationale of the joint venture supports this; for example, separate profit, separate accounting, separate tax treatment, the fact that the joint venturers cannot bind each other, the fact that each of them has severally and separately appointed the manager as its agent, the several extent of their liability to third parties and the separate taking of product. Each of these points to separate and several businesses".[21]

However, it is difficult to extrapolate this line of reasoning into the context of property development joint ventures. Neither in their structuring nor in their practical operation do property development joint ventures lend themselves to the type of analysis available to mining joint ventures. This difficulty also emerges in the third "view of profit" element of the definition of "partnership".

In the case of mining joint ventures, it is frequently contended that the common goal of each joint venturer is not joint profit but individual gain. Ladbury submits that:

> "a major difference between the mining joint venture and partnership is that in the joint venture the profit or gain will be derived by the venturers individually ... The mining joint venture is an expense sharing and production sharing agreement. Although each venturer may have the object of individual gain, there is no joint profit motive and no joint profit; thus even if it could be said that persons may be carrying out their business or undertaking in common, they are not carrying it out for joint profit. Indeed some venturers may sell the product while others may process it further before sale".[22]

This aspect was raised in the High Court in **United Dominions Corporation Ltd v Brian Pty Ltd**[23] where Dawson J stated:

> "Perhaps, in this country, the important distinction between a partnership and a joint venture is, for practical purposes, the distinction between an association of persons who engage in a common undertaking for profit and an association of those who do so in order to generate a product to be shared among the participants. Enterprises of the latter kind are common enough in the exploration for and exploitation of mineral resources and the feature which is most likely to distinguish them from partnerships is the sharing of product rather than profit".[24]

It would be difficult to adopt analogous reasoning for a typical property joint venture which is usually concluded by sale and distribution of profit, rather than the participants taking a share of the product. However it would not be impossible for the joint venture property to be transferred to the various joint venturers in their respective proportions for them to dispose as they see fit for individual gain (for example, in strata title commercial or residential property developments).

Because an unincorporated joint venture might be construed as a partnership, corporate and trust structures have been preferred in property joint ventures to date. However, where an unincorporated joint venture structure has been adopted, it is obviously important for the venturers and the financiers that the joint venture agreement excludes, as far as possible, any suggestion of partnership. To achieve this, the joint venture agreement should:

(i) provide for separate ownership and disposal of assets or product of the joint venture activity;

(ii) provide that joint venture assets are to be owned by the venturers in specified shares, as tenants in common;

(iii) disavow mutual agency between the joint venturers; and

(iv) for what it is worth, incorporate a provision confirming that a partnership is not intended. Of course, a mere disclaimer of partnership will be of no avail if the association is in fact properly characterised as a partnership.[25]

4. ESSENTIAL PROJECT FINANCE AGREEMENT PROVISIONS

The credit agreement, which will describe the facilities to be provided to the borrower, should incorporate special provisions dealing with:

(i) Permitted Use of Funding

There will need to be inserted restrictions on the purposes for which the funds may be used; obviously drawdowns will need to be restricted to the purposes of the project. The method of advancing funds will need to ensure this eventuates in practice.

(ii) Conditions Precedent

In addition to the usual conditions precedent which must be satisfied before the financier is committed to provide funding, other factors which may require special consideration include:

(a) the obtaining of all necessary Ministerial consents (including the granting of the project tenure and the creation of the proposed security interests);

(b) the necessity to obtain exchange control approval (which is now of diminished significance given the various exemptions which have been issued in recent years by the Reserve Bank pursuant to Regulation 38 of the Banking (Foreign Exchange) Regulations;

(c) the requirement to notify and obtain approvals under the Foreign Acquisition and Takeovers Act 1975 or any other applicable State legislation.[26] The ability of the Federal Treasurer to compel offending investors to disgorge any interests acquired in breach of the legislative requirements makes it essential for financiers to confirm that the necessary approvals have been obtained and all conditions have been complied with;[27]

(d) confirmation that all planning approvals have been obtained and all environmental protection legislation has been satisfied;

(e) whether any export approvals are required in respect of the project products;[28]

(f) whether there are any statutory controls which are likely to affect project production and therefore impact on project cash flows;[29]

(g) whether enforceable sales contracts, transportation and infrastructure agreements are in place;

(h) whether satisfactory legal opinions as to the efficacy of the project securities have been obtained.

(iii) <u>Representations and Warranties</u>

Additional representations and warranties will need to confirm that:

(a) the borrowers are entitled to all joint venture property free of any competing interests. The prospect of competing Aboriginal land rights claims must not be overlooked;[30]

(b) copies of all joint venture and other relevant project infrastructure documentation have been provided to the financier and that there are no breaches of those agreements;

(c) the entry into the project financing and the granting and enforcement of the project securities will not breach any provisions of the above agreements;

(d) the project is being undertaken within the boundaries of the project properties and all necessary consents have been obtained.

(iv) <u>Borrower's Covenants</u>

Careful thought will be required of particular special covenants which may have to be sought from the borrower. The nature of these covenants will be dictated largely by the nature of the project. However, the borrower will usually be required to covenant:

(a) to comply with the joint venture agreement and other project documentation;

(b) to report fully and regularly in respect of all salient aspects of the project; eg, project completion, cost projections, details of sales contracts;

(c) to notify all significant matters likely to affect the project (eg, joint venture or other project agreement defaults, events of force majeure, government or other political interference; proposed amendments to the joint venture or project documentation; any significant litigation);

(d) not to dispose of lease or grant other security interests in respect of project assets;

(e) to observe all financial ratios specified in the loan documentation;

(f) where the lender is looking to the project's cash flows and earnings to service the loan repayments, not to make any distributions by way of dividend or otherwise;

(g) not to amend or permit any amendment to any project documentation and not to act in any way which might result in a variation of the project specifications, a reduction in project production or a delay in project completion.

(v) Default Provisions

When drafting the credit agreement, the financier's lawyers will need to focus on any additional events of default which may be required by virtue of the particular nature of the project. The prospect and likely consequences of cross defaults under other borrowing arrangements will need to be considered. Examples of events of default particularly relevant to project financing include:

- project cost overruns;
- unauthorised delays in project completion;
- unauthorised variations or breaches of project documentation by not only the borrower but any other parties;
- threatened or purported forfeiture of project tenure;
- failure to obtain or comply with all governmental and other approvals necessary to ensure the successful completion and operation of the project;
- failure to obtain or to ensure completion of the requested number of project sales agreements.

5. SECURITY ASPECTS

5.1 Project Infrastructure Issues

In the project financing context, the financier's lawyers must recognise at the outset the importance of two distinct levels of documentation:

(i) project infrastructure agreements usually entered into by the project developer with third parties such as project tenure leases, constructions agreements, sales contracts, transport agreements to access rail and port facilities, any other agreements providing services to the venture (eg, roads, electricity, water) and joint venture agreements;

(ii) credit and security documents between the project developer and the financiers.

It is essential to bear in mind that the financiers shall be normally taking security over the whole array of project infrastructure documentation (comprising mainly intangible contractual rights) so that, in the event of default, the lenders can either operate or sell the project (preferably as a whole). In this context, financiers would normally prefer to structure the financing to the project participants on a joint, rather than several, basis because:

(i) all project assets and revenues can be more readily charged in favour of the lenders to secure repayment of the project loans;

(ii) the lenders' default powers (especially receivership and sale) are more readily exercisable as the securities will embrace the whole project; the prospect of confrontation with belligerent non-defaulting joint venturers is thereby avoided;

(iii) a joint financing removes many of the difficulties which would otherwise be confronted when structuring the joint venture agreement; and

(iv) in a several financing, a single joint venturer may not be able to effectively covenant to complete the project. It is not of much value to lenders to have a strong covenant from the borrowing venturer to use its voting power in favour of completion and against abandonment, unless in the joint venture agreement the other venturers commit to complete and not to abandon, in similar terms. The lenders are not ideally protected unless the other venturers also charge their interests in the joint venture to secure repayment of the borrowings, but this will of course be most difficult to negotiate where there are wholly independent joint venturers.

As part of preparing the financing structure, the lenders must satisfy themselves that the relevant project agreements are sufficiently comprehensive and enforceable, not only from the point of view of the parties to the project documents, but also in the context of security enforcement. It is also essential for security integrity to ensure that project infrastructure documents remain on foot and unaltered during the term of the financing.

5.2 Nature of Security

5.2.1 Fixed and Floating Charges

The lender will normally require, at least in a limited recourse financing, security over the project cash flow and assets.

Security would normally assume the form of a fixed and floating charge over the project assets (including insurance policies and proceeds thereof, project product and sales proceeds) and statutory registered mortgages over the project tenure.

The lenders will obviously be concerned that, as far as possible, the charge is fixed for as against other creditors, holders of floating charges are not in as secure a position as holders of fixed charges. A holder of a floating charge can be postponed to certain creditors[31] and a floating charge given within six months before the chargor company commences to wind up can be void.[32]

Floating charges are also vulnerable in other respects. If the floating charge is over debts due to the chargor, set-off can override the floating charge where the chargor's debt was one incurred in the carrying on of business in the ordinary course.[33] An

execution levied against assets of the chargor subject to a floating charge is now also seen as taking precedence over the chargee.[34]

Another right that overrides the present interest of a holder of an uncrystallised floating charge exists under s218 of the Income Tax Assessment Act 1936 (Cth) and s38 of the Sales Tax Assessment Act (No 1) 1930 (Cth) under which the Commissioner can serve a notice on a debtor of the chargor - taxpayer requiring that debtor to pay the Commissioner. It has been held that the Commissioner takes free of the floating charge.

From the borrower's perspective, the borrower will be anxious to ensure that the charge is floating as far as possible, at least in relation to some assets, so that the borrower has the ability to deal with them. Two possible compromises are:

(i) the floating charge can be strengthened by the inclusion of a provision prohibiting or restricting the creation of further encumbrances over any of the charged property. Under the Corporations Law system of priorities, where there is a restriction on the creation of further charges and the statement lodged with the charge provides to that effect, charges created in breach of the restriction will normally be postponed to the original chargee holding the floating charge.[35] However, it should not be overlooked that not all priority problems are thereby solved. The Corporations Law governs priorities only as between certain charges over certain property. Accordingly, for example, the lenders will need to consider in each case whether any of the interests charged constitute real or other property to which a specific system of registration may be applicable.[36] Problems also remain with the manner in which the Corporations Law purports to deal with priority of future advances. The Corporations Law will also not regulate, generally speaking, priorities between fixed securities over *choses in action* (except book debts). There also remains the difficulty of priorities as between securities over agreements. A subsequent security holder or assignee may take priority if it is the first in time to give notice of its interest to the other party to the agreement.[37] As the financier's lawyer, one should always therefore consider whether notice of the lenders' interests in any *choses in action* should be given to preserve the lenders' priority.

(ii) the floating charge can be drafted so as to automatically crystallise into a fixed charge on the occurrence of certain specified events which are of concern to the lender. Doubts have previously been expressed as to whether such clauses are effective. However, a New Zealand court has squarely held that a provision which calls unambiguously for automatic crystallisation is effective.[38] A similar view was obtained in England.[39] In Australia, Murphy J of the Supreme Court of Victoria has held that crystallisation may take place on any event stipulated as a matter of contract.[40] A similar stance has been adopted by Rogers CJ of the Supreme Court of New South Wales, where a provision in a charge which provided that the charge would crystallise if the company dealt with assets other than in "the ordinary course of its ordinary business" was held to be effective.[41] Walsh J of the Supreme Court of Western Australia arrived at a similar conclusion.[42] The High Court has also held that the appointment of a receiver under a prior ranking floating charge was effective under the terms of a later ranking floating charge to crystallise that later charge.[43]

Properly drafted, automatic crystallisation clauses can go a long way towards assuaging a lender's concerns. They can operate to prevent priority otherwise being afforded to judgment creditors and the Commissioner of Taxation in the circumstances adverted to above. However such clauses cannot be embraced with uncritical enthusiasm, especially from a borrower's point of view. If drafted so as to transform the floating

charge into a fixed charge too readily, their propensity to cause practical difficulties is obvious (especially if it results in a cross default under other borrowings).

It should also be noted that reform of the law regarding automatic crystallisation clauses may be imminent. The Australian Law Reform Commission has recommended that the companies legislation should provide for crystallisation to take place only:

(i) when a public act (entry into possession of the company's property by a receiver, an agent of the chargee or the chargee itself, or the liquidator or administrator) has occurred; or

(ii) a notice that the charge has become fixed has been lodged with the registering authority.[44]

This recommendation has not been dealt with in the Corporate Law Reform Bill 1992, as it is perceived to be relevant to the pending Australian Law Reform Commission review of personal property securities which are proposed to be the subject of separate amending legislation in the near future. However, s442B of the Corporate Law Reform Bill 1992 will, if enacted, affect the efficacy of floating charges in certain circumstances. Under that section, it is intended that an administrator appointed to take over the affairs of a company (pursuant to the proposed new Part 5.3A of the Corporations Law) may in certain circumstances deal with property that is the subject of a floating charge that has crystallised, as if the charge were still a floating charge.

In the context of automatically crystallising floating charges, a particular problem in respect of fixed charges should not be overlooked. The question whether any charge is fixed or floating is not decided by the label put on it by the parties. A charge the parties choose to describe as fixed will be treated as floating if it appears that they intend the company to be able to continue its business in relation to assets within the charge without reference to the chargee.[45]

If the courts were to hold a particular project joint venture to be in legal reality a partnership, it is worth noting that the High Court has held that a charge over a share in a partnership is a charge over "ascertained and definite" property in the shape of the chose in action (comprising the partner's share in the partnership consisting of a right to a proportion of the surplus after realisation of the assets and discharge of the liabilities of the partnership) and is therefore a fixed charge: **United Builders Pty Ltd v Mutual Acceptance Ltd.**[46] In that case a charge over a share in a partnership was held to be fixed with the result that it was not void for want of registration under the Companies Act 1961 (Qld).

5.2.2 Other Project Assets

There will be other significant project assets which can conveniently be subjected either to a fixed charge or to a specific registered mortgage as the borrower need not be able to dispose of them, without reference to the lenders, in the ordinary course of its business. Examples include mining and petroleum titles, land (both freehold and leasehold), major items of plant and equipment and sales contracts.

In this context, both present and future property needs to be considered. There is usually no reason why a charge of future property must operate as a floating charge.[47] In the case of charges over future property, however, each project must be considered in its particular statutory context, for legislative restrictions on this form of security may exist,[48] and the likely consequences of an intervening liquidation must not be overlooked.[49]

5.3 The Relationship Between the Lenders and the Co-Venturers

Where the project assumes the structure of an unincorporated joint venture, delay, expense and often unnecessary antagonism can be avoided if the lenders' interests and likely concerns are considered as early as possible. This observation is particularly apposite in circumstances where a joint financing is not contemplated; that is, where the lenders are lending only to some and not all of the joint venturers. In such a financing, a conflict exists between the interests of the lenders, who are anxious to ensure that they will be able to satisfactorily enforce their securities in the event of default, and the interests of the other venturers, who will be concerned that the lenders may exercise default powers to their detriment.

Lenders should therefore carefully consider the terms of the joint venture agreement and should concentrate on such matters of concern as:

(i) the joint venturer's interest in the joint venture assets and entitlement to project product;

(ii) the joint venturer's right to assign and charge its interest in the joint venture. These rights will need to be sufficiently comprehensive to permit the precise type of securities to be taken. A right to both assign and charge will usually be necessary to cover the possible types of security which may be required and to facilitate the lenders' or a receiver's powers of sale upon default;

(iii) the consequences of default by a joint venturer; these can vary to include any one or more of the following:

   (a) loss of information rights;

   (b) loss of voting rights;

   (c) the imposition of high interest rates on overdue payment;

   (d) the loss of entitlement to joint venture production or proceeds;

   (e) exercise of rights under joint venture cross charges to enforce the payment of outstanding contributions to the joint venture;

   (f) dilution of the defaulting joint venturer's interest in the joint venture - the defaulter's interest is often reduced in accordance with a formula based upon its relative financial status in the joint venture at the relevant time;

   (g) compulsory sale (sometimes effected by options to purchase) to the non-defaulters at a price determined by a formula or procedure set out in the joint venture agreement; or even

   (h) forfeiture of the defaulting joint venturer's entire interest.

   Usually a lender will require some delay in the exercise of any default powers and an ability to be able to cure the default itself;

(iv) whether the joint venture can continue to be carried on notwithstanding a default by a joint venturer;

(v) the lenders' rights, powers and obligations in an enforcement situation. The lenders would wish to exercise their power of sale free from restrictions on disposal (eg, rights of pre-emption or forced sale in favour of non-defaulting joint venturers). Such restrictions can unnecessarily complicate a mortgagee sale process and may be legally ineffective if the sale price for the defaulter's interest in the joint venture is for an amount less than its market value. Lenders would be proscribed from committing to sell as mortgagee for less than market value in some jurisdictions;[50]

(vi) the ranking of the lenders' security against the cross charges given to the other joint venturers. Often lenders will permit the cross charges to rank in priority, provided:

(a) the minimum sale price for the defaulter's interest is reasonable,

(b) enforcement by the non-defaulting joint venturers is delayed for a reasonable period after notice to the lenders to enable the lenders, if they so elect, to remedy the default or to exercise their default powers in priority;

(c) the obligations secured by the cross charge are limited to joint venture obligations;

(d) the extent of priority to be afforded to the cross chargee is agreed;

(e) the cross charge is limited to the joint venturer's interest in the joint venture;

(f) there is no obligation on the financiers to meet the borrower's liability for calls if they enforce their security;

(vii) whether there are adequate completion covenants;

(viii) whether the lenders are permitted to disclose confidential joint venture information in an enforcement situation;

(ix) whether default or termination powers of non-defaulting joint venturers are triggered upon enforcement of the lenders' securities;

(x) whether the joint venturers have covenanted not to partition, by order of a court or otherwise, any of the jointly owned joint venture assets. This would run counter to the concept of the binding legal continuity of a joint venture. Most joint venture agreements should therefore contain waiver clauses excluding the right to seek partition or to apply to the courts for a statutory trust for sale.[51]

5.4 Enforceability of Joint Venture Default Procedures

All of the abovementioned mechanisms for overcoming the inability or refusal of a party to meet its obligations, although set out in the joint venture agreement which is *prima facie* binding upon and definitive of the rights of the parties to it, may be set aside or modified by the courts in certain circumstances. It will be of common concern to both the lenders and the borrower that if another venturer defaults, the remedies available against it will be legally effective and will facilitate completion or continued operation of the project. In this context a number of legal issues arise including:

(i) Does the default provision, alone or in conjunction with other provisions -

(a) constitute a registrable charge;[52]

(b) constitute a voidable preference?[53]

(ii) Will the provision be subject to equitable intervention on the principles of forfeiture or penalties?

(iii) Will the provision be set aside by a liquidator?[54]

(iv) Will the provision, where it incorporates an option to purchase juxtaposed with a cross charge, be treated as ineffective in equity as its exercise would in substance amount to a foreclosure out of court or an unlawful fettering of the mortgagor's equity of redemption?[55]

In the context of equitable relief against penalties and forfeiture, the High Court in **Legione v Hately**[56] has held that a party having a legal right shall not be permitted to exercise it in such a way that the exercise amounts to unconscionable conduct.[57]

5.5 Project Agreements - Restrictions on Assignment

As many of the project assets will comprise contractual rights (under documents such as the joint venture agreement, sale agreements, agreements with governments (State Agreements) transportation and other infrastructure agreements) lenders will wish to ensure that the borrower's interest under those agreements are adequately charged to enable the lenders to complete or continue the project in an enforcement situation.

An immediate issue to consider when taking security over a project agreement is whether the rights of the borrower under that document can be mortgaged or charged. The document will need to be reviewed to determine whether its terms permit the charging of the borrower's rights. A concomitant of this question is whether such rights can be assigned.

In the absence of any clause restricting assignment, it would seem that contractual rights and benefits may be freely assigned, absolutely or by way of security,[58] unless they are too personal to be capable of assignment. A project joint venture agreement, involving elements of mutual confidence, fiduciary relationships and long term association for the development of the project, would normally be a contract incapable of assignment without the consent of the other joint venture parties.

Frequently, however, project agreements will prohibit or restrict assignments or charging of rights by the borrower. It can become problematic interpreting a clause which only restricts "assignments" - does such a clause preclude a mortgage or charge by way of security which does not contemplate a complete assignment or transfer of rights?

Although the consequences of taking a charge in breach of a contractual prohibition are uncertain, some authorities indicate that a charge given in breach of the clause may be totally ineffective.[59] Meagher Gummow and Lehane proffer the view that a breach may confer on the third party contractor a claim for damages against the borrower if, in the traditional analysis, the clause requiring consent is a warranty. However, if the clause can properly be construed as a fundamental term or condition, the third party contractor may elect to treat the breach as a repudiation and rescind.[60]

It is axiomatic that this is an area where both borrower and lender should proceed cautiously and seek prior consents from all other parties to the agreement. As far as the lenders are concerned, advance consents to two transactions should be sought - the first being the granting of the mortgage or charge, and the second a sale of the mortgaged property upon default by the lenders or receivers appointed by them under the security.

5.6 Security over Project Cash Flows

It is customary for lenders to insist that the borrower's rights under sales contracts be subject to an assignment by way of mortgage or a fixed or floating charge. Unlike most other project documents, a sales contract may be governed by a law other than the domestic law of the place of the project. This often gives rise to complex issues of private international law and the lenders' risks may thereby be increased.

Conflicts of laws principles relating to the assignment of contractual rights will need to be considered. Whether rights under a sales contract may be assigned will depend upon the proper law of the sales contract, which will normally be specified in the contract. However, on occasions no governing law is expressed. In any event, the need to take proceedings against a foreign buyer in his own country (and the likely consequences of taking such proceedings) may have to be addressed. The foreign law rules governing the formalities which must be completed in order that a purported assignment will be valid, and matters going to priorities between competing interests in the assigned rights will necessitate advice from lawyers practising in the foreign Jurisdiction.[61]

If a charge over the sales contract is contemplated, a specific fixed charge (if effective) is preferable to a floating charge because a specific charge confers an immediate equitable interest in the present and future debts the subject of the sales contracts thereby entitling the chargee to preserve its priority by giving notice of its interest to, and compelling payment of sales proceeds by, the debtor, pursuant to the rule in **Dearle v Hall**.[62] A chargee under a floating charge is disqualified, whilst the charge remains floating, from giving notice under the above rule.[63]

However, because a fixed charge disentitles the chargor from dealing with the charged assets without the specific consent of the chargee (the strict compliance with which, in a practical sense, may render a fixed charge over project cash flows unworkable where the borrower needed to access some or all of the sales proceeds to continue to carry on business), a practice emerged in recent years which involves incorporating in the charge provisions which permit the chargor to collect and utilise sale proceeds in the course of its business without the consent of the lenders. Lenders could still elect in these circumstances to give notice of its "fixed" charge to the buyer under the sales contract (to preserve priority), but to prevent diversion of project cash flow which would otherwise occur, the buyer was informed that until further notice (to be given after default by the borrower), the buyer may continue to make payments to the chargor.

It would appear that such a practice would preclude the charge from being properly construed as a fixed charge. In light of the authorities mentioned previously, a court would look to the substance and not the form of the transaction and regard the security as a disguised floating charge.[64]

If a lender wishes to obtain an enforceable specific charge over all present and future book debts the subject of the project sale contracts, there would need to be some real, and not illusory, consent and control provisions and defined procedures which regulate the use of the sale proceeds by the chargor. Ideally, the charge should require that sale

proceeds be credited to a nominated account under which the chargee lender is a signatory, either alone or at least jointly with the chargor. The account should be opened with a third party (eg, a related entity of the lender) for where sale proceeds are paid into a bank account with the lender itself, any purported charge would not confer a security interest in favour of the lender, but the lender may rely on rights of combination and set-off.[65]

To be effective, the fixed charge would also need to incorporate a provision restricting the granting of any subsequent charges or absolute assignments. It would also be imprudent for lenders to agree to limit the ordinary effect of the specific charge in any circumstances (by, for example, allowing the chargor to use sale proceeds for the purpose of its business prior to default) and the charge should be drafted to extend to the current credit balance of the nominated account, and the sales proceeds themselves until they are deposited in that account.[66] If the borrower chargor is to be permitted access to any of the funds deposited in the account, there must be a requirement that the lenders firstly consent and even then, the extent of such access must be carefully regulated.

If, as foreshadowed previously, the above restrictions are practically too inconvenient, the lenders may consider resorting to a registered floating charge, which includes a covenant restricting subsequent charges or assignments, and which also automatically crystallises into a fixed charge in the event of any creation, or attempted creation, of subsequent charges or assignments.

Before finalising any securities over sales contracts, the lenders would need to review the contracts in question to satisfy themselves as to such matters as:

(i) price escalation and review provisions;

(ii) method, security for and currency of payment;

(iii) the duration of each contract;

(iv) force majeure and frustration;

(v) the nature and extent of warranties required of the seller;

(vi) default provisions;

(vii) methods of resolving disputes between the parties;

(viii) whether assignment or charging by the seller of its interest in the contract and the proceeds is permitted;

(ix) governing law.

5.7 Security over Land Subject to Instalment Contracts

Project lenders should be made aware that, in the case of Queensland property development projects, a vendor under an instalment contract[67] is not permitted to mortgage the land the subject of the contract without the consent of the purchaser.[68] Where the land is mortgaged in contravention of the section, the instalment contract is voidable by the purchaser at any time before completion of the contract.[69] Section 4(1) of the Property Law Act 1974 (Qld) defines "mortgage" to include a charge on any property for securing money or money's worth. Thus, a variation of a mortgage which is

existing at the date of the contract of sale, which variation increases the amount for which the land is a security by providing for further advances, has been held to be mortgaging the land within the meaning of s73(1) of the Property Law Act.[70] It has been held that the effect of the legislation is that such a further advance requires the purchaser's consent.[71]

An exception to this would be where the mortgage is securing the operation of a current account of the vendor within an agreed overdraft limit, the agreement for that limit having been established at the time of the contract of sale. In such an instance, further drawing against the overdraft up to that limit, beyond the amount drawn at the date of the contract of sale, will not amount to a variation of mortgage nor create a charge upon the land merely being an application of an existing contractual arrangement by way of mortgage or charge in respect of a specific advance.[72] Each separate advance under such a mortgage securing a current account will not amount to a fresh charge for the purposes of s73 of the Property Law Act and the principles of tacking in relation to future advances upon such bank mortgages covering an overdraft have no application in the interpretation of the section.[73]

Similar provisions apply in some other States.[74]

5.8 Completion Covenants and Letters of Comfort

In a limited recourse financing, lenders will require assurance that the project will in fact be completed. In a several financing, a single joint venturer may not be able to covenant to complete the project, in which case the financing should be structured so as to encourage the venturer to ensure completion (eg, covenants to use its voting power in a manner consistent with the lenders' interests and which will not prejudice completion). If the borrower is an insubstantial subsidiary of a project sponsor, recourse to the parent sponsor will not be available, if the project is not completed for any reason, unless the sponsor assumes some enforceable legal commitment. The form of commitment that lenders should seek before completion, is a guarantee of the debt. If given, no particular difficulty arises.

However, parent company guarantees are sometimes not procurable. Instead, lesser commitments in the form of letters of comfort or keep-well agreements are offered in substitution. Not surprisingly, if default occurs, lenders will sometimes seek to enforce letters of comfort. It was in this context that the first instance judgment of Hirst J in **Kleinwort Benson Ltd v Malaysia Mining Co Berhad**[75] focussed the attention of lenders and borrowers generally on the possibility that such letters may be construed to be enforceable in the nature of guarantees in some circumstances.

Although Hirst J's judgment was reversed on appeal,[76] Rogers CJ in the Commercial Division of the New South Wales Supreme Court has recently echoed the same warnings when His Honour held that a letter of comfort given by Australian National Industries Ltd gave rise to contractual obligations.[77]

Rogers CJ agreed with the Court of Appeal in **Kleinwort** that there exists no general legal rule concerning comfort letters which would indicate or determine the scope of the legal obligations which the writer of the letter had assumed. His Honour noted that comfort letters had developed, first in the United States in the 1960s, as an alternative to a guarantee or surety, where the writer (usually the parent company) was unable or unwilling to issue one of those more traditional securities. This reluctance was often due to the accounting fact that a guarantee had to be disclosed as a contingent liability in the parent's accounts, which could affect its credit rating.

In determining whether a letter of comfort gives rise to contractual obligations, Rogers CJ held that:

(a) the ordinary rules of construction and interpretation relating to contracts apply;

(b) the overriding test is that of the intentions of the parties as deduced from the document as a whole seen against the background of the practices of the particular trade or industry and in the events surrounding its inception;

(c) the *prima facie* presumption that in respect of commercial transactions there is an intention to create legal relations applies and the onus of proving the absence of such intention rests with the party who asserts that no legal effect is intended.[78]

Taking into account the negotiations leading to the final version of the ANI Ltd letter of comfort and a close textual analysis of its terms, Rogers CJ held that the letter of comfort contained enforceable contractual promises which had been breached by ANI Ltd thereby exposing ANI Ltd to a liability in damages.[79]

Even if an enforceable liability in contract cannot be established, lenders and borrowers should not overlook other possible areas of exposure that letters of comfort may generate, including:

(i) an action for misleading or deceptive conduct under s52 of the Trade Practices Act;

(ii) an action in damages for deceit, negligent misstatement or breach of warranty;

(iii) s592 of the Corporations Law has to be considered in connection with letters of comfort or keep-well agreements which take the form of an agreement by a parent company to keep its subsidiary in funds so as to maintain liquidity. If the agreement contemplates that the directors of the subsidiary may cause the subsidiary to incur a debt to the parent when the subsidiary is in a liquidity crisis, it could be taken to contemplate a breach of s592.

5.9 State Agreements

Many of the major capital-intensive projects undertaken in Australia are operating under the terms of an agreement between the project sponsors/developers and the government of the State where the project is located. Most State agreements focus on the following:

(a) the project - the developers' basic obligation is to design, build and operate the project;

(b) infrastructure commitments - the respective obligations of the developers and the State to provide a range of project and social infrastructure (eg, railways, roads, towns, schools, essential services) will be specified;

(c) revenue aspects - the developers' obligation to contribute to royalties, base rentals, freight payments and the like will be specified;

(d) State's obligations - such as providing tenure for the project site, power generation, access to water resources and rail transport, will be specified together with the price to be paid for such services;

(e) other contractual provisions - dealing with such matters as force majeure, termination, arbitration, assignment, mortgaging and charging, variation, governing law and so on.

From the point of view of project financiers, any such agreement will be of considerable importance and it is essential that the borrower's rights under the agreement are included in the lenders' security.

The project lenders would need to consider and confirm the legal status of any relevant State agreement and would have to investigate:

(i) whether the agreement has provided sufficiently for the initial requirements of the project, such as the grant of title over the project lands and the grant or waiver of all necessary planning or other consents;

(ii) whether and in what circumstances the title, consents or the agreement itself can be terminated, varied or revoked;

(iii) whether the State government has agreed not to discriminate against the developers;

(iv) whether government charges or taxes are afforded priority ahead of the project lenders;

(v) whether assignment, mortgaging or charging of the developer's interest in the agreement and in the project lands in the manner contemplated by the lenders are expressly permitted;[80]

(vi) whether the lenders will have adequate opportunity to implement protective measures should a default occur under the State agreement;

(vii) whether the lenders (or receivers appointed by them) are free to assign the borrower's rights and interest under the agreement and in the project assets in the event of default.

In those Australian States which do not favour State agreements, project sponsors (and financiers) of major projects may have to rely on letters of undertaking or comfort from the government. There are, however, problems associated with the securing of an enforceable agreement with a State over a long period of time. There is clear authority that a State cannot by contract fetter or limit the future use of its discretionary powers,[81] or its future legislative or discretionary action.[82] Therefore such letters often provide only political, not legal, support.

Most State agreements are approved and ratified by separate legislation to remove any doubt of the State to make the agreement or of the authority of the person signing on behalf of the Crown.[83]

5.10 Limitation on Recourse

The underlying principle of project financing is that there is usually only limited recourse to the assets of the borrower other than the cash flow of the project and the project assets. The extent of the recourse is a matter for negotiation between the lenders and the borrower in each transaction.

Limitation on recourse can be achieved simply if the project is to be operated by a specially incorporated company which is to hold no other assets. If the project sponsors have not guaranteed the borrower's obligations, the lenders would only have recourse to the assets of the project as their only rights would be exercisable against the borrower.

However, if the sponsor is developing the project, or the project company owns other significant assets or intends to acquire further assets in the future, how does one ensure that there is no recourse beyond that which the parties have agreed? The following suggestions are tentatively proffered:

(i) the lender should not be entitled to have resort, for the payment or recovery of moneys owing to it by the borrower, to any asset or property of the borrower, except project assets the subject of the lender's security;

(ii) the borrower's personal covenant to pay must be limited so as to extend (except to the extent of any additional recourse which may be agreed, examples of which follow) to project revenues and, on default, project assets subject to the lender's security. The borrower's obligations are sometimes expressed to be entered into, not as personal obligations with the intent of binding it personally, but for the purpose only of binding the secured project assets. It is obviously important that the limitation on recourse clause is drafted to limit the rights of recovery of the lenders rather than to deny (by exclusion or release) the existence of an obligation. If there is no personal obligation to repay, there may be inadvertently excluded any claim which may be made against the borrower;

(iii) for similar reasons, and again except to the extent that additional recourse is agreed upon, recourse for damages or other liability arising under or in relation to the project loan agreements must also be restricted;

(iv) to perfect the desired limitation on recourse, a borrower would normally require the lender to agree that, notwithstanding any default by the borrower, the lender will not, in relation to any indebtedness or liability arising in respect of the project loan agreements:

    (a) apply or seek to wind up the borrower or prove in any winding up;

    (b) levy or enforce any execution against any assets or property of the borrower (other than project assets);

    (c) seek to have the borrower placed under official management;

    (d) seek to have a receiver appointed by a court or appoint a receiver under the lender's securities (other than in respect of project assets - and even then, the receiver's authority as agent of the borrower to incur debts or obligations binding upon the general assets of the borrower would need to be restricted. Similarly, the authority or powers of any attorney or agent of the borrower, which the lender may be empowered to appoint under its project securities, must also be restricted);

    (e) exercise any rights of indemnity, combination or set off (except in the case of project sales proceeds accounts);

    (f) obtain a judgment for the payment of money or damages.

True "non-recourse" financing is, however, rare as lenders will wish to have general recourse to the assets of the borrower in certain circumstances, including:

(i) if the borrower or sponsor fails to complete the project. Completion guarantees will normally be sought to ensure that everything necessary is done to achieve completion by a specified date;

(ii) if there have been breaches of fundamental warranties or covenants, eg, as to title to or security over project assets, or if the borrower improperly disposes of project assets without the lenders' consent. The lenders' rationale is simple - whilst they are prepared to limit their recourse to the security, the security must at all times remain intact, valid and effective;

(iii) where project revenues have been paid into a security or escrow account but the borrower has been permitted to access some of the proceeds in that account in successful years, the lenders may insist on the right to recapture or claw back those funds previously paid out to the borrower.

Where borrowers are able to negotiate financing on a limited recourse basis, the extent of the protection thereby afforded may be negated unless cross-default provisions in their other borrowing arrangements are restricted so as not to operate simply because of a default under the limited recourse facility or enforcement of a project security.[84]

5.11 Difficulties Flowing from a Liquidation of the Borrower

Limited recourse financiers rely, for security purposes, upon the continuing operation of the project. Irrespective of the priority of their securities, unless the lenders' position is carefully considered and provided for, liquidation of the borrower can place the project lenders in an invidious position in an enforcement situation, if a receiver has been or is to be appointed, or if the project has not been completed.

Notwithstanding the appointment of a liquidator, a receiver may still exercise his powers to hold and dispose of the project property of the borrower without the concurrence of the liquidator for such powers are given by the disposition of the borrower's property which it made in equity when the charge was given.[85] However, the making of a winding up order does affect a receiver in various ways. For instance:

(i) if he was appointed under a mortgage which provided that he was to hold his position as agent for the borrower (as is usually the case), that agency will diminish when the borrower goes into liquidation;[86]

(ii) in consequence, the receiver will no longer be able to look to the borrower for indemnity, or to make it liable, in contract or otherwise create debts provable in the borrower's liquidation against its unmortgaged assets;[87]

(iii) it has been previously considered by others to be inconsistent with the notion of a winding up that the company's business should continue to be carried on beyond the extent necessary for its beneficial winding up. However, as a consequence of the decision in **Atkins v Mercantile Credits Ltd**[88] the position may not be as stringent as had been previously believed. Although winding up terminates authority of the receiver to act as agent for the borrower, it does not affect his power to hold and dispose of property of the borrower that is subject to the lenders' security, nor does it extinguish the receiver's power to carry on the borrower's business except that he may not thereby create debts which are provable in the borrower's liquidation.[89]

As a receiver's right to custody of charged assets overcomes the statutory right and duty of the liquidator to take possession of those assets, then if the right to carry on business was part of the lenders' security, it would seem logical to conclude that the right to carry on business was not a company asset that the liquidator was entitled to control. Furthermore, the cessation of the receiver's agency for the company does not put an end to the powers of a receiver conferred by the security under which he was appointed and the Corporations Law.[90]

Although it is assumed in the various authorities that the receiver's agency is terminated by the winding up order or the passing of the winding up resolution, the effect of the usual power of attorney conferred on the mortgagee and his substitutes by most mortgage debentures is often overlooked. The power of attorney, if properly drafted, is expressed to be irrevocable, comprises part of the security, and is granted for valuable consideration; that is, the advances or other financial accommodation which the lenders provide.

Under the general law such a power of attorney is not revoked by the liquidation of the borrower company.[91] Most States entrench this principle statutorily in provisions stating that an irrevocable power of attorney granted by a company to secure a proprietary interest survives the winding up of the grantor company.[92]

Accordingly, the fact that the receiver's special agency is terminated by the winding up should not preclude a receiver and manager acting as the company's substitute attorney under the power of attorney conferred on the mortgagee and his substitutes by the mortgage debenture.

Further difficulties will also emerge for project lenders, if liquidation intervenes before the project is concluded, in respect of further advances necessary to complete the project.

Prior to liquidation, a receiver and manager is personally liable under s419(1) of the Corporations Law for debts he incurs in the course of the receivership for services rendered, goods purchased or property hired, leased, used or occupied. But such personal liability is expressed to be "without prejudice to the [receiver's] rights against the corporation or any other person", thereby preserving the receiver's right to an indemnity from the company and the mortgagee.

When the company goes into liquidation the receiver and manager's personal liability for these debts remains but he loses his right to claim the indemnity out of the unsecured assets of the company. Such debts are not provable against the company in liquidation.

If the security documents confer upon the lenders appropriate powers of preservation and improvement, any additional moneys expended by the lenders, as mortgagees in possession, or by a receiver appointed by them, to complete the project can be added to the principal component of the secured moneys and would be covered by the project securities. However, such moneys would not be regarded as borrowings of the chargor company or by the receiver as its agent, for the reasons mentioned above. Accordingly, although pre-liquidation advances will continue to accrue interest until repayment at the rate specified in the loan documentation, the question whether moneys expended by the lenders or a receiver after liquidation also accrue interest at that rate is more problematic. Unless the indebtedness was incurred at the request of the liquidator and possibly also with the approval of the court,[93] or the loan or security documentation clearly empowered the lenders to advance (or a receiver to borrow) funds in these circumstances at the rate of interest sought, and such moneys and interest formed part of the moneys covered by the project securities, interest at the desired contractual rate may not be recoverable.

It is suggested that the revocation of the receiver's powers to pledge credit and incur debts which are provable against the company in liquidation neither prevents the receiver from invoking his express indemnity from the mortgagee nor stops the mortgagee recouping himself out of the secured assets. However, the security documents will require careful drafting to achieve the lenders' expectations in this regard.

In light of the above complications, lenders will often prefer a single or special purpose company as borrower (whose memorandum may entrench a prohibition against carrying on any other business) and will specify strict financial ratios to be observed by the borrower. To further minimise the possibility of the borrower's liquidation, project lenders may also insist upon covenants by the borrower, its shareholders and other joint venturers not to attempt to resolve to wind up the borrower voluntarily, or borrow or raise money from other parties without the prior concurrence of the project lenders.

Reform of the law in this area is also proposed. Proposed sub-s420C(1) of the Corporate Law Reform Bill provides that a receiver of a company that is being wound up may carry on the company's business where the receiver obtains the written approval of the liquidator or the approval of the Court.

Section 420C(2)(a) makes it clear that the power conferred by sub-s(1) is additional to any other power which the receiver may have. An example of such a power would be a power of attorney granted under the mortgage security under which the receiver was appointed, enabling the receiver to act as agent of the company in order to realise assets of the company.

Section 420C(3) of the Bill is intended to make it clear that where the receiver carries on business with the approval of the liquidator or the Court, he does so as agent of the company, and thus has a right of indemnity from the company assets for expenses and liabilities incurred in carrying on the business.

Section 420C(4)(a) goes on to impose on the receiver statutory personal liability for debts incurred in carrying on the business, although that personal liability is without prejudice to the rights of the receiver against the company or any other person. Thus it is without prejudice to the receiver's rights as an agent of the company to be indemnified from the company's assets.

Section 420C(4) provides that liabilities incurred by the receiver in carrying on the business are liabilities incurred in the receivership and not in the liquidation. Thus, the liabilities do not attract the special payment priority available under proposed s556(1)(a) of the draft Bill. The receiver would need therefore, as at present, to satisfy himself before incurring liabilities that there are sufficient company assets available, or that a reliable indemnity is available from another source, to cover those liabilities.

6. THE INTRUSION OF FIDUCIARY OBLIGATIONS

Essentially, a "fiduciary" may be defined as a person who has "bound himself in some way to protect and/or to advance the interests of another."[94]

The lender-borrower relationship does not seem to fit easily with other established categories of fiduciary relationships, such as that of trustee and beneficiary, promoter and investor, partner and partner, principal and agent and director and company where accepted rules govern the behaviour within such relationships. However, when these more traditional and established relationships are examined, it becomes apparent, having regard to the typical roles of the various parties in project financing transactions,

that a court will hold that a number of the fiduciary duties governing those relationships are also present in most project financing transactions.

Furthermore, the categories of fiduciary relationships are constantly being extended by the courts. In other jurisdictions, fiduciary duties have recently been extended to a mortgagee's power of sale,[95] and to a bank providing advice, information and assistance in a takeover.[96] In **Catt v Marac Australia Ltd**[97] Rogers J of the New South Wales Supreme Court held that a financier, who for technical reasons calculated to enhance the plaintiffs' position acted as both purchaser and vendor of an aircraft, the property the subject of the financing, had put itself in a position akin to that of a promoter and was liable to the various investors on the basis that it knowingly participated in the breach of duty owed to the investors by the promoters of the scheme.

It would also seem that lead managers of project loan syndications have particular duties to their fellow participants; for example, they should not place themselves in a position where their interests conflict with their participants, nor should they receive monetary consideration not generally available or disclosed to all participants. Lead managers would also need to ensure full disclosure of all information relevant to a particular decision to participate in a syndicated facility to all intending participants. If a lead bank owed fiduciary duties to participants, it would not be allowed to use its position to make secret profits,[98] nor use confidential information for its own benefit.[99]

Agents for participants in syndicated credit facilities also have clear fiduciary obligations to the participants on whose behalf they act as a consequence of the agency relationship. Where the agent is acting for more than one banking syndicate providing different funding facilities to the same borrower under the one credit document, difficult problems can arise for the agent, particularly where the agent is a participant in one or more of the facilities. The only solution to these problems is sometimes resignation by the agent; for example, where a default occurs under such a facility, it may well transpire that the interests of one facility group will be drastically different to the interests of another. An agent's duty to exercise its powers for the benefit of all of its principals may prove to be incapable of fulfilment in these circumstances, and the permissions usually afforded to agents in most syndicated facility documents to wear different hats may be insufficient to displace that duty.[100]

Unless there are express contractual limits to an agent's obligations with respect to information received, it would seem that the duty of confidence may also have to be observed by an agent towards a borrower in terms of particular information which the agent receives about the borrower and the borrower's business affairs.

The extent to which fiduciary obligations exist between joint venturers is also of great concern in the situation where the financier is or becomes a participant. Some project financings have utilised structures where the financier has taken an equity participation in the project. In this context, **Brian's Case**[101] confirms that a financier who becomes a partner must accept the liabilities flowing from that role and cannot use its position as financier to alter that. Similarly, a financier who becomes a non-partner joint venturer must accept the obligations arising from the joint venture relationship, which may include fiduciary obligations owed to the other participants.[102]

Despite an earlier reluctance to impose fiduciary obligations in a commercial context,[103] the reasoning of the various members of the High Court in **Brian's Case** indicates that fiduciary obligations are not confined, in the commercial context, to relationships classified as partnerships. Where the relationship falls outside that classification, the court will examine the joint venture agreement and structure to determine the actual

obligations undertaken by the parties. In light of **Brian's Case**, the following additional matters should also be taken into consideration:

(i) parties who enter into negotiations for a joint venture agreement should be aware of the duty which prospective joint venturers may owe to each other. Fiduciary obligations can arise even in pre-contractual negotiations. These fiduciary obligations include:

(a) joint venturers must not mislead each other and must positively make full disclosure;

(b) joint venturers are accountable for secret profits made without their joint venturer's knowledge and consent, and also for profits made as a result of information gained in the course of the joint venture business;

(ii) full disclosure by one joint venturer and express consent by the others will usually prevent the disclosing party from incurring liability for breach of any fiduciary duties owed;

(iii) whether a joint venture attracts fiduciary obligations will depend on the form and content of the joint venture agreement - if there is a de-emphasis of any relationship based on trust and confidence and a stressing of the contractual relationship (ie, the commercial and arm's length nature of the arrangement), fiduciary duties and obligations may be negated.

Noranda Australia Limited v Lachlan Resources NL and Others[104] suggests that joint venturers in an unincorporated joint venture can limit the extent of their fiduciary obligations by carefully drafted express terms to that effect in the joint venture agreement.

7. CORPORATION LAW REFORM

Brief preliminary mention should be made of some other provisions of the Corporate Law Reform Bill 1992, an exposure draft of which has just been released for public scrutiny and comment. It is anticipated that the draft legislation will (or, at least, should) be subject to a number of amendments before its enactment.

7.1 Insolvency Reform

The centrepiece of the Bill is the long awaited implementation of the Harmer Report on corporate insolvency. The Bill proposes a new form of insolvency administration, under which a company that is in financial difficulties would be able to appoint an independent administrator.

This would have the consequence of imposing a moratorium on actions against the company, to allow the administrator to prepare a scheme of administration to place the company back on its feet.

The new regime is found in proposed Part 5.3A which involves the following elements:

(i) allowing directors to appoint an independent administrator;

(ii) allowing the administrator up to thirty-five days to develop a proposed scheme of arrangement for consideration by the company and its creditors;

(iii) giving force to the arrangement if the company and its creditors support it;

(iv) giving protection to the rights of secured creditors by:

(a) allowing them to challenge the appointment of an administrator where the appointment is being used by company management merely to delay an inevitable winding up;

(b) allowing a creditor secured over the whole or substantially the whole of the company's assets a short period during which the creditor may elect to enforce the security, notwithstanding the appointment of an administrator; and

(c) requiring the court to ensure the adequate protection of any creditor who opposes certain action by an administrator or who votes against a scheme of arrangement; and

(v) where the administrator or the meeting of creditors concludes that the company should be wound up, provide for a smooth transition to a winding up process.

7.2 Recovery of Insolvent Trade Debts

As mentioned previously, a stricter approach to directors' liability for company debts is to be given statutory backing.[105]

The right to sue a director to recover insolvent trading debts will initially be the province of the liquidator and all unsecured creditors will participate in any successful recovery action by the liquidator. Creditors will only be able to launch their own actions if the liquidator fails to do so.

Of greater significance in the project financing context is that the insolvent trading net is also to be extended to holding companies. A subsidiary's liquidator will be able to sue a holding company if it allowed the subsidiary to trade when the holding company knew or should have known that the subsidiary was insolvent.[106]

7.3 Receivers and Mortgagees in Possession

Part H of the draft Bill implements Harmer Report recommendations that:

(i) most of the Corporation Law's receivership provisions be extended to mortgagees and their agents (the provisions in question relate largely to reporting to shareholders and the ASC, some of which are potentially onerous);

(ii) receivers, chargees in possession and their agents have a duty to take reasonable care in exercise of their powers including, in particular, the sale of company assets;

(iii) a receiver appointed under a subsequent charge be empowered in some circumstances to dispose of property of the company, notwithstanding a prior charge, provided the rights of the prior chargeholder are adequately protected.[107]

7.4 Loans to Directors and Related Companies

The object of proposed Part 3.2A of the draft Bill is to tighten up the existing s234 of the Corporations Law, and extend the scope of regulation to other corporate financial transactions, by:

(a) broadening the class of regulated transactions (presently only loans, guarantees and security relating to loans and guarantees), to encompass all types of financial assistance;

(b) subject to certain exemptions, such as for approved employee share acquisition schemes and housing assistance schemes, prohibiting a company from entering into loans (and other transactions) with its directors (and certain persons, companies and trusts associated with directors);

(c) subject to analogous exemptions (which will cover most group treasury operations), prohibiting a company from entering into transactions such as loans to related bodies corporate, or bodies corporate to which it is "linked" - that is, in which one body corporate has a significant influence over the other - unless a strict members' approval procedure is followed and approval obtained; and

(d) subject also to certain exemptions, prohibiting a company from entering into assets transfer transactions with associates of the company (the potential application of these provisions has presumably been overlooked for they are couched in the widest of terms), except in accordance with a strict members' approval procedure.

Companies involved in joint venture operations will be able to seek exemption from the main regulatory provisions of the Bill for internal transactions within the joint venture structure, although the ASC is to enjoy a monitoring role.[108]

The draft Bill will also require greater disclosure to the company by directors of matters which may give rise to a conflict of interest. A company will also be required to keep a register of any such interests which have been declared which shall be available for inspection by any member or director of the company.[109]

7.5 Priority Among Creditors - Debt Subordination

The Harmer Report recommended that the operation of ss555 and 556 of the Corporations Law (which established general rules for priority among creditors) should not prevent a creditor agreeing that the creditor's particular debt should be deferred until another creditor's debt is paid in full or in part.

Section 555 of the Corporations Law provides that all debts proved in a winding up rank equally, and if the property of the company is insufficient to meet them in full they should be paid proportionately. Conflict with this provision may arise if a creditor of a company has agreed to subordinate payment of a debt due to the creditor to the claims of one or more other creditors. Subordinated debt often forms a part of the package proposed for a project financing. However, since the decision of **British Eagle International Air Lines Ltd v Compagnie Nationale Air France**,[110] an unresolved issue has been whether the terms of a contract providing subordination should prevail over the clear mandate of s555, particularly as it might affect the duty of an insolvency administrator to apply that provision.

Proposed s563C(1) of the draft Bill provides that a debt subordination by a creditor of a company shall not be unlawful or unenforceable except to the extent that debt subordination would disadvantage any creditor of the company who was not a party to or otherwise concerned in the debt subordination.

Proposed sub-s563C(2) defines "debt subordination" to mean an agreement or declaration by a creditor of the company, however expressed, to the effect that, in specified circumstances, the debt owed by the company to the creditor will not be repaid until debts owed by the company to another creditor or creditors have been repaid in full.

However, it seems that the amendments do not yet go far enough for the Bill does not provide that a liquidator shall be bound by the debt subordination arrangements and may adhere to them notwithstanding the priority provisions of s555 of the Corporations Law.

7.6 Some Reforms Still Outstanding

7.6.1 Problems Relating to Registration of Charges

The Corporations Law imposes a separate obligation upon companies to give notice of charges they create so that a public register of charges may be maintained by the Australian Securities Commission.

All bills of sale, stock mortgages, liens on crops, liens on wool and the like created by companies are "charges" and thus are required to be registered pursuant to the Corporations Law.[111] In addition, the bills of sale legislation in the various States requires such instruments to be registered.

Registration pursuant to two statutory systems as regards the same document seems unnecessary. For this reason, s273(1)(a) of the Corporations Law provides that where notice in relation to a company charge is required to be lodged under the Corporations Law (to enable registration) the charge "need not be registered under a specified law of this jurisdiction", and "a failure to register the charge under a specified law of this jurisdiction does not affect the validity, or limit the effect, of the charge".[112]

In Queensland, for example, the laws which have been specified are the Bills of Sale & Other Instruments Act 1955 and The Liens on Crops of Sugar Cane Act 1931.[113] This is not new. A similar position applied under the Companies (Queensland) Code[114] and the Companies Act 1961.[115] However, what the previous companies legislation also achieved (and in respect of which the Corporations Law is defective) was preservation of the efficacy of a charge if it infringed other provisions of the Bills of Sale legislation (eg, compliance with formal requirements), besides a failure to register.

It has recently been held by the Queensland Supreme Court that whilst the Companies (Queensland) Code provided that a charge registrable under the Companies Code did not have to be registered under the Bills of Sale legislation, nothing in the Code excused the charge from having to comply with the formal requirements of the Bills of Sale legislation.

In **Re Bauer Securities Pty Ltd & Anor: Austral Mining Construction Pty Ltd v NZI Capital Corporation Ltd & Anor,**[116] McPherson J held that:

(a) failure to comply with the formal requirements of the Bills of Sale legislation renders company charges invalid against third parties;

(b) registration under the Bills of Sale legislation does not cure the invalidity; and

(c) registration under the Companies Code does not cure the invalidity.

The matter went on appeal to the Full Court of the Supreme Court,[117] but the correctness of these conclusions were not disputed on appeal and the Full Court upheld McPherson J's decision.

The practical effect of the decision is widespread and does not appear restricted to Queensland. The security for most significant project financings will include valuable chattels. It would be surprising if many of the numerous company charges potentially affected would have complied in every respect with the formal requirements of the Bills of Sale legislation. If the decision in **Re Bauer Securities** is followed, these company charges, if they also constitute bills of sale within the meaning of the relevant Bills of Sale legislation, would be held to be invalid as securities, notwithstanding the company charges are properly registered under the Corporations Law, at least in so far as they relate to chattels.

The Federal Attorney-General's Department has agreed to amend the Corporations Law (such amendments to be retrospective to January 1, 1991) to circumvent this problem, but as yet the amendments have not been legislated.

7.6.2 Section 241 of the Corporations Law

The Companies and Securities Law Review Committee has previously recommended important amendments to what is now s241 of the Corporations Law.[118]

By s241(1), a company cannot by provision in its articles or in any contract or otherwise exempt any officer (which term is defined in s241(4) to include a receiver of property of the company) or auditor of the company from, or indemnify him against, any liability which by law would otherwise attach to him in respect of "any negligence, default, breach of duty or breach of trust" of which he may be guilty in relation to the company. Any such provision is void.

The extent to which articles of association of the borrower company may reduce the scope of directors' duties in light of s241 remains unclear, although recent English authority construing the UK equivalent of s241, suggests that the section should not preclude the articles removing a disability affecting an officer (eg, under the conflict of interest doctrine).[119]

Does the section catch provisions in contracts to which the company is not a party? The section applies to "any provision, whether contained in the articles or in a contract or otherwise". The words "or otherwise" could still refer to an arrangement within the company, such as a resolution of a general meeting. Unless the section is limited to arrangements within the company, the possible ramifications are far reaching for the section would invalidate an indemnity given by a third person to an officer against liability arising from activity as an officer of the company. The section could therefore conceivably affect:

(i) an indemnity given to a receiver by the lender appointing him;

(ii) an indemnity given by a parent company of a person appointed as a director of a wholly owned subsidiary;

(iii) an indemnity given by a lender to a person properly appointed to the board of the borrower company to represent the lender's interests;

(iv) directors' and officers' liability insurances.

It appears from its English predecessor that s241 was intended to cover only indemnities given by the company, but the meaning of this unsatisfactorily drafted section still awaits legislative clarification.

FOOTNOTES

1. The stated list of project risks appears in Wood, **Law and Practice of International Finance**, Vol 2, 1981 at p313.

2. See Ladbury, "Financing Resources Projects" (1988) 62 *ALJ* 937 for additional risks that fall for consideration.

3. See generally J Martin, "Project Finance", in Bruce and others (Eds), **Handbook of Australian Corporate Finance** (3rd Ed, 1989), p329.

4. For further discussion of this method, refer to M Markovic, "Off Balance Sheet Financing: The Legal Implications" (1992) 10 *CSLJ*, pp41-44.

5. See R A Ladbury, "Recent Trends in Limited Recourse Financing with particular reference to Limited Recourse Loans, Production Payments and Forward Sale and Purchase Agreements" (1979) *AMPLJ* 68 and R S McCormick, "Legal Issues in Project Finance" (1983) 1 *JERL* 21 for an elaboration on these methods.

6. See, for example, the various articles published in the Australian Mining and Petroleum Law Journals.

7. Some of these include **Hussein v Good** (1990) 8 ACLC 390; **Heide Pty Ltd v Lester** (1990) 8 ACLC 958; **Statewide Tobacco Services Ltd v Morley** (1990) 8 ACLC 827; **Commonwealth Bank of Australia v Friedrich** (1991) 9 ACLC 946.

8. **Group Four Industries Pty Ltd v Brosnan** (1991) 5 ACSR 649.

9. *Supra*, note 7 (1990) 8 ACLC 827.

10. *Supra*, note 7 (1991) 9 ACLC 946.

11. See Part D of the Corporate Law Reform Bill 1992.

12. Partnership (Limited Liability) Act, 1988 (Qld); Limited Partnership Act, 1909 (WA); Limited Partnership Act, 1908 (Tas); Partnership Act, 1892 (NSW) ss49-81.

13. See, for example, **Heys & Barrow v CSR and Midalco** (Rowland J Nos 1148 and 1161 of 1987, Supreme Court of Western Australia).

14. As to the nature of this argument, see A M Millhouse, "Trading Trusts" (1988) *QLSJ* 443.

15. **Federal Commissioner of Taxation v Everett** (1980) 143 CLR 440.

16. Section 110 of the Bankruptcy Act 1966.

17. Partnership Act, 1891 (Qld) s5(1); Partnership Act, 1892 (NSW) s1(1); Partnership Act, 1958 (Vic) s5(1); Partnership Act, 1895 (WA) s7(1); Partnership Act, 1891 (SA) s1; Partnership Act, 1891 (Tas) s6.

18. (1974) 131 CLR 321. See also **United Builders Pty Ltd v Mutual Acceptance Ltd** (1980) 33 ALR 1.

19. For example, s35(2) of the Partnership Act, 1891 (Qld); s32(b) of the Partnership Act, 1892 (NSW); s36(b) of the Partnership Act, 1958 (Vic); s43(b) of the Partnership Act, 1895 (WA); s37(b) of the Partnership Act, 1891 (Tas).

20. "Joint Venture Agreements" (1982) 4 *AMPLJ* 101 at 135.

21. "Mining Joint Ventures" (1984) 12 *ABLR* 312 at 320.

22. Ladbury, *op cit* at 321.

23. (1985) 157 CLR 1.

24. *Op cit* at 15.

25. **Adam v Newbigging** (1888) 13 App Cas 308 at 315; **Stekel v Ellice** [1973] 1 WLR 191 at 199; **Ex parte Coral Investments Pty Ltd** (1979) Qd R 292.

26. For example, Queensland's Foreign Ownership of Land Register Act 1988.

27. See s35 of the Foreign Acquisitions and Takeovers Act which provides that the Supreme Court of a State or Territory may on the application of the Treasurer, make orders to enforce, for example, any divestiture orders by the Treasurer. Such orders could conceivably extend to mortgagees directing them to deliver up title documents notwithstanding that the mortgage debts may still be outstanding. Compare the more favourable treatment afforded to mortgagees by Part V of the Foreign Ownership of Land Register Act 1988 (Qld).

28. For example, lenders will wish to be satisfied that any export permits under the Customs (Prohibited Exports) Regulations have been obtained where applicable.

29. For example, under s58 of the Petroleum (Submerged Lands) Act 1982, a licensee is subject to directions from the designated authority as to the rate of recovery of petroleum.

30. Many project participants and their financiers may be potentially affected by the High Court's pending judgment in **Mabo and Others v State of Queensland** in this regard.

31. For example, certain employees' entitlements which enjoy priority by virtue of s433 of the Corporations Law.

32. See s566 of the Corporations Law.

33. **Biggerstaff v Rowatt's Wharf Ltd** [1896] 2 Ch 93.

34. **Evans v Rival Granite Quarries Ltd** [1910] 2 KB 979.

35. See s279(3) of the Corporations Law.

36. For example, the relevant State mining legislation.

37. Pursuant to the rule in **Dearle v Hall** (1828) 38 ER 475.

38. **Re Manurewa Transport Ltd** [1971] NZLR 909.

39. **Re Permanent Houses (Holdings) Ltd** (1989) 5 BCC 151.

40. **Deputy Commissioner of Taxation v Horsburgh** [1983] 2 VR 591.

41. **Fire Nymph Products Ltd v The Heating Centre Pty Ltd** (1988) 14 ACLR 274.

42. **Re Wrights Hardware Pty Ltd** (31 October 1988, unreported).

43. **Stein v Saywell** (1969) 121 CLR 529.

44. ALRC Report No 45 para 196.

45. **Hart v Barnes** (1982) 7 ACLR 310; **National Provincial Bank of England Ltd v United Electric Theatres** [1916] 1 Ch 132; **Siebe Gorman & Co Ltd v Barclays Bank Ltd** (1979) 2 Lloyds L Rep 142; **Re Armagh Shoes Ltd** [1984] BCLC 405; **Re Wallyn Industries Pty Ltd** (1983) 7 ACLR 661; **Waters v Widdows** [1984] VR 503; **DFCT v Horsburgh** [1984] VR 773; **Norgard v DFCT** (1986) 5 ACLC 527; **Re Brightlife Ltd** [1986] BCLC 418; **Re Keenan Brothers Ltd** [1986] BCLC 242; **FCT v Lai Corporation Pty Ltd** [1987] WAR 15, 83 FLR 63; **Perrins v State Bank of Victoria** [1991] 1 VR 749.

46. (1980) 33 ALR 1.

47. **Holroyd v Marshall** (1862) HL C 191; **Tailby v Official Receiver** (1888) 13 App Cas 523.

48. See, for example, **Re Anroma Pty Ltd** (1987) 2 Qd R 134.

49. The charge, when "attaching" to future property when that property comes into existence, may be challenged by a liquidator as a void disposition of property under s468 of the Corporations Law, as occurred in **Re Anroma Pty Ltd** (*supra*, note 48).

50. For example, in Queensland any agreement is void to the extent that it purports to relieve, or might have the effect of relieving, a mortgagee from the duty imposed by s85 of the Property Law Act to take reasonable care to ensure that the property is sold for its market value.

51. For example, pursuant to s38 of the Property Law Act 1975 (Qld).

52. Cross charges, for example, would normally be registrable as charges pursuant to s262 of the Corporations Law.

53. By virtue of the application of ss120 or 122 of the Bankruptcy Act, as applied to a company in liquidation by s565 of the Corporations Law.

54. See, for example, s468 of the Corporations Law. See generally Roberts, "Default Clauses in Joint Venture Agreements in the Context of Sections 368, 451 and 200 of the Companies Code" (1987) AMPLA Yearbook 318.

55. As to the possible conclusions a court may reach in respect of these questions, see J R F Lehane, "Joint Venture Finance and Some Aspects of Security and Recourse" in **The Law of Public Company Finance** (1986) pp521-526; K D MacDonald "Joint Ventures - Breakdowns and Repairs Rights Upon Default" (1983) AMPLA Yearbook 209; Roberts, *supra* note 54.

56. (1983) 152 CLR 406.

57. See also **AMEV-UDC Finance Ltd v Austin** (1986) 162 CLR 170; **Stern v McArthur** (1988) 81 ALR 463; **Esanda Finance Corporation v Plessnig** (1989) 84 ALR 1; **AMEV Finance Ltd v Artes Studios Thoroughbreds Pty Ltd** (1989) 15 NSWLR 564; **CRA Limited v NZ Goldfields Investments** [1989] VR 873; **David Securities Pty Ltd v The Commonwealth Bank of Australia** (1990) 23 FCR 1; Justice M J R Clarke, **Penalties Forfeiture and Dilution** (1989) AMPLA Yearbook 1.

58. **Tolhurst v Associated Portland Cement Manufacturers (1900) Ltd** [1902] 2 KB 660.

59. **Helstan Securities Ltd v Hertfordshire County Council** [1978] 3 All ER 262.

60. See Meagher Gummow and Lehane, **Equity: Doctrines and Remedies**, (2nd Edition), pp192-195.

61. As to some of the complex conflict of laws issues which can arise, see Lehane, *supra* note 55, pp530-531.

62. *Supra*, note 37. See also W J Gough, **Company Charges** (1978) p371.

63. **English and Scottish Mercantile Investment Co Ltd v Brunton** (1892) 2 QB 700; W J Gough, **Company Charges**, at p143.

64. *Supra*, note 45.

65. See **Broad v Commissioner of Stamp Duties (NSW)** (1980) 2 NSWLR 40; **Re Charge Card Services Ltd** [1986] 3 WLR 697 and **Estate Planning Associates (Australia) Pty Ltd v Commissioner of Stamp Duties (NSW)** (1985) 2 NSWLR 495.

66. **Re Keenan Bros Ltd** [1985] BCLC 302.

67. Section 71(2)(b), Property Law Act 1974 (Qld) defines "instalment contract" as an executory contract for the sale of land in terms of which the purchaser is bound to make a payment or payments (other than a deposit) without becoming entitled to receive a conveyance in exchange therefor; it includes contracts for the sale of unregistered lots in a building units or group titles plan: **Chan v Dainford Ltd** (1985) 155 CLR 533.

68. *Ibid*, s73(1). Similar provisions apply in some other jurisdictions: *Infra*, note 74.

69. *Ibid*, s73(2)(a).

70. **Landers v Schmidt** [1983] 1 Qd R 188 at 195 per Connolly J.

71. **Coast Securities No 9 Pty Ltd v Bondoukou Pty Ltd** (1986) 61 ALJR 285 at 288 (PC) per Lord Oliver.

72. **Highfern Pty Ltd v Sibbles** [1987] 2 Qd R 667 at 686 per Andrews CJ.

73. **Sibbles v Highfern Pty Ltd** (1987) 62 ALJR 55 at 57-58.

74. See, for example, ss7(1) and (4) of the Sale of Land Act, 1962 (Vic) and s14 of the Land Sales Act, 1964 (NSW).

75. [1988] 1 WLR 799.

76. [1989] 1 WLR 379.

77. **Banque Brussells Lambert SA v Australian National Industries Ltd** (1989) 21 NSWLR 502 (presently on appeal to the Court of Appeal of New South Wales but at the time of writing of this article, the appeal had not been heard).

78. Following the English authority of **Edwards v Skyways Ltd** [1964] 1 WLR 349 at 355.

79. For other Australian authorities concerning letters of comfort, see **Commonwealth Bank of Australia v TLI Management Pty Ltd** [1990] VR 510; **Esanda Finance Corporation Ltd v Wordplex Information Systems Ltd** (1990) 99 FLR 40; and **Helco Pty Ltd and Ors v O'Haire and Anor** (1991) 109 ANZ Conv R 8.

80. Such provisions are important notwithstanding that, as a matter of law, an agreement with the Crown is capable of assignment: **R v Brown** (1912) 14 CLR 17.

81. **South Australia v The Commonwealth** (1962) 108 CLR 130.

82. **Rederiaktiebolaget Amphitrite v The King** [1921] 3 KB 500; see also K D MacDonald, "The Negotiation and Enforcement of Agreements with State Governments Relating to the Development of Mineral Ventures" (1977) *AMPLJ* 29.

83. See generally L Warnick, "State Agreements" (1988) 62 *ALJ* 878.

84. See J R F Lehane, **Project Securities** (1983) AMPLA Yearbook 183 at pp190-192.

85. **Sowman v David Samuel Trust Ltd** [1978] 1 WLR 22 at 30.

86. **Gosling v Gaskell** [1897] AC 575; **Re Obie Pty Ltd (No 2)** (1984) 8 ACLR 574.

87. **Atkins v Mercantile Credits Ltd** (1986) 4 ACLC 125.

88. *Supra*, note 86.

89. J O'Donovan, (ed), McPherson, **The Law of Company Liquidation**, (3rd ed) (1987) at pp201-202.

90. Section 420(2)(h).

91. **Griffin v Clark** (1940) 40 SR (NSW) 409; **Frith v Frith** [1906] AC 254.

92. See Property Law Act 1974-1986 (Qld), s173; Conveyancing Act, 1919 (NSW), s164; Property Law Act 1969-1979 (WA), s86(1); Powers of Attorney Act 1934 (Tas), s10; Instruments Act 1958 (Vic), s124.

93. See s477 of the Corporations Law.

94. Finn, **Fiduciary Obligations** (1987), at p9.

95. **Murphy v Financial Development Corporation** (1985) 495 A 2d 1245.

96. **Standard Investments Ltd v CIBC** (1985) 52 OR (2d) 473.

97. (1986) 9 NSWLR 639.

98. **Parker v McKenna** [1874] 10 Ch App 96.

99. **Boardman v Phipps** [1967] 2 AC 46.

100. See generally Wood, *supra* note 1 pp256-270.

101. *Supra*, note 23.

102. For recent examples, see **Crusader Resources NL v Santos Ltd** (Unreported No 2635/89 SA Supreme Court (Full Court), 18 June, 1991), and **Pacific Coal Pty Ltd v Idemitsu Queensland Pty Ltd and Ors** (Unreported judgment of Ryan J of the Supreme Court of Queensland dated 21 February, 1992).

103. **Hospital Products Ltd v United States Surgical Corporation** (1984) 156 CLR 41.

104. (1988) 14 NSWLR 1.

105. See paragraph 3.1.1 of this paper and Part D of the Corporate Law Reform Bill 1992.

106. See proposed ss588X and 588Y of the Corporate Law Reform Bill 1992.

107. Proposed ss420A and 420B of the draft Bill.

108. Proposed s243GA.

109. Proposed s243MA.

110. [1975] 1 WLR 758.

111. Sections 262(1)(d), 262(1)(h) and 262(5).

112. Section 273(1)(c) of the Corporations Law.

113. Corporations Law Application Order No 2 of 1990.

114. Section 211(1).

115. Section 100(9).

116. (1991) 4 ACSR 328.

117. (1991) 4 ACSR 57.

118. Companies and Securities Law Review Committee Report No 10.

119. **Motivex Ltd v Bulfield** (1986) 2 BCC 99, 403.