CIVIL LIABILITY FOR ERRORS AND OMISSIONS IN INFORMATION MEMORANDA IN THE WHOLESALE CAPITAL MARKETS

BRIAN SALTER

Partner
Clayton Utz, Solicitors, Sydney

INTRODUCTION

The domestic wholesale capital markets distribute securities known as commercial paper (or promissory notes), medium term notes and bonds. These are purchased by large institutions and professional fund managers seeking short to long term debt investments. The securities are principally issued through the mechanism of an information memorandum. The quality and quantity of the disclosures in these varies tremendously, but essentially an information memorandum plays a role analogous to that of a prospectus in the "public" equities market.

Whilst the origin of the capital markets in Australia is relatively recent, they play an important role in the economy. For example, Standard & Poor's estimates that the total outstandings for non-government commercial paper as at 29 February 1996 amounted to $16.5 billion.[1] The markets also fund the securitisation industry, which Standard & Poor's estimates had at least $8 billion of non-commercial paper securities on issue as at 31 December 1995.[2] The prospects for substantial growth in the capital markets are also encouraging, particularly as they are likely to become a major investment and distribution mechanism for superannuation savings, which are expected to rise from the present $214 billion to $784 billion by 2026.

In order to ensure the unfettered growth of the capital markets in Australia, there needs to be an appropriate regulatory balance between the interests of investors and the liability of those responsible for the preparation and distribution of an information memorandum. If one class is favoured over the other, the development of the capital markets may be impeded, by either jeopardising the integrity of the markets as an investment source or by making it too costly and burdensome for Australian businesses to source their debt funds from the markets.

The purpose of this paper is to review the statutory civil liability provisions where an information memorandum fails to meet the mandated legislative standards. The review highlights a number of substantial deficiencies in the regulatory scheme and queries whether the present approach achieves the balance necessary to promote the continued development of the wholesale capital markets in Australia.

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1 Standard & Poor's, "The Australian Commercial Paper Market", 1 April 1996, at 13.

2 Standard & Poor's, "Structured Finance - Australia and New Zealand", 1996, at 5-6.

LEGISLATIVE OVERVIEW

The principal statutory sources for civil liability in relation to a defective information memorandum are section 52 of the Trade Practices Act, 1974 (TPA) and section 995 of the Corporations Law (CL).[3]

Section 52(1) TPA provides as follows:

> "A corporation shall not, in trade or commerce, engage in conduct that is misleading or deceptive or is likely to mislead or deceive."

Section 995(2) CL uses the same language of "misleading or deceptive" conduct in the context of securities and prospectuses. The section provides as follows:

> "A person shall not, in or in connection with:
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> (a) any dealing in securities; or
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> (b) without limiting the generality of paragraph (a):
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> (i) the allotment or issue of securities;
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> (ii) any prospectus issued, or notice published, in relation to securities;
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> (iii) the making of takeover offers or a takeover announcement, or the making of an evaluation of, or of a recommendation in relation to, takeover offers or offers constituted by a takeover announcement; or
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> (iv) the carrying on of any negotiations, the making of any arrangements or the doing of any other act preparatory to or in any way related to any matter referred to in sub-paragraph (i), (ii) or (iii);
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> engage in conduct that is misleading or deceptive or is likely to mislead or deceive."

Section 995(2) applies to an information memorandum by virtue of the definitions of "securities" and "prospectus". The expression "securities" is defined in section 92(1) CL and embraces shares, debentures and prescribed interests. These in turn are defined in section 9 CL.[4] Without repeating the definitions, it is sufficient to say that almost every capital markets instrument is a "security", either because it is a "debenture" or is embraced by the catch-all "prescribed interest" notion. The only relevant exception relates to a promissory note having a face value of $50,000 or more. Such a promissory note is not a "debenture" by virtue of paragraph (e) of the definition of this term. In addition, a promissory note of any denomination is excluded by paragraph (h) from the definition of "participation interest" and hence is not a "prescribed interest". The face value of a promissory note issued into the capital markets usually exceeds $50,000. Accordingly, such promissory notes are not "securities" for the purposes of the CL and are not affected, amongst other things, by section 995(2). No significant practical advantage, however, flows from this as any misstatements or omissions in an information memorandum for a promissory note issue will still attract potential liability under section 52 TPA.

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3 See also the Fair Trading Acts of each State. The Corporations Law contains a number of other provisions which may also be relevant depending on the circumstances, eg sections 998(1), 999 and 1000(1).

4 See also section 78(4)CL which has some interesting implications, which are outside the scope of this paper, for the statutory definitions of "debenture" and "securities".

A "prospectus" is defined in section 9 CL to be:

> "... a written notice or other instrument:
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> (a) inviting applications or offers to subscribe for ... securities; or
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> (b) offering ... securities for subscription".

Given the function of an information memorandum, it will almost always be a "prospectus" for the purposes of the CL.

The inclusion of a section 52 standard in the CL stems from an apprehension that the "trade or commerce" constitutional requirement of section 52 would be narrowly construed by the courts, with the result that the section may not extend to all dealings in securities.[5] However, with the benefit of hindsight, this concern was probably unfounded.[6] Thus, in *Fraser v NRMA Holdings*, Gummow J made the following observation:

> "The first respondent... did not press a defence raising an issue as to whether some of the conduct complained of was not 'in trade or commerce' with the meaning of s.52 of the Act. This concession was no doubt wisely made. It would have required a restrictive view of trade and commerce and an exaggerated effect for the preposition 'in' to take the 'conduct' with which this case is concerned outside s.52".[7]

The similarity in language invites the courts to draw on the case law regarding section 52 for determining the meaning of "misleading or deceptive conduct" in the context of section 995. Indeed, the Explanatory Memorandum for the CL indicates that this was the original intention:

> "A guide to what type of conduct is misleading or deceptive [under section 995] can be gained from the many cases decided under TPA section 52."[8]

The relevance of the section 52 case law to section 995 was recognised by Gummow J in *Fraser v NRMA Holdings*. His Honour stated that "in the present case, a finding of contravention of section 52 would have been accompanied by a finding of contravention of section 995".[9] On appeal the Full Federal Court endorsed this view and said that "had the applicants sought to rely on section 995(2) the issues for determination would have been substantially the same".[10] The case law in relation to section 52 is, therefore, a guide to the application of section 995.

Whilst there are obvious similarities in the application of sections 52 and 995, there are also some important differences. The Full Federal Court in *Fraser v NRMA Holdings* felt that the remedies available for a breach of section 995 may be greater than for a breach of section 52.[11] However, as pointed out by Legg, if this is the case, then it is so not by much.[12] Perhaps more importantly, standing is not required to obtain an injunction under section 80 TPA for a breach of

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5 Explanatory Memorandum, Corporations Bill 1988, AGPS, paragraph 2961. See also G Golding, "Underwriters' Liability in Australian Securities Offerings", (1993) 11 *C&SLJ* 401, at 422.

6 See for example Deane J, *Re Ku-Ring-Gai Co-operative Building Society (No 12) Ltd* 36 FLR 134, at 167. For a review of the "trade or commerce" requirement, see R S French, "A Lawyer's Guide to Misleading or Deceptive Conduct" (1989) 63 *ALJ* 250, at 253.

7 (1994) 12 ACLC 855, at 866.

8 Op cit n 5, at 2961.

9 Op cit n 7, at 867.

10 (1995) 13 ACLC 132, at 141.

11 Ibid, at 141.

12 M Legg, "Misleading and Deceptive Conduct in Prospectuses" (1996) 14 *C&SLJ* 47, at 48.

section 52, whilst this is still necessary under section 1324 CL in the case of section 995. Thus, the plaintiff directors in *Fraser v NRMA Holdings*, by bringing their action under section 52, did not need to establish that their interests were at risk to obtain an injunction. Also, although there are no defences for a breach of section 52, this is less clear in the case of section 995.

Generally, capital markets securities constitute an "excluded" issue, offer or invitation and, accordingly, the corresponding information memorandum is exempt from Part 7.12 CL (section 1017) and the related provisions governing Part 7.12 prospectuses (for example, section 996(2)). The grounds upon which a particular programme is an "excluded" issue, offer or invitation can vary, however, most are structured so as to qualify for the exemption applying where the amount subscribed by each offeree is at least $500,000.[13]

THE PROHIBITIONS IN DETAIL

Misleading or Deceptive Conduct

The touchstone for liability for a breach of sections 52 and 995 is that the effect of the misstatement in, or omission from, the information memorandum must be "misleading or deceptive". The meaning attributed to these words is to "lead into error".[14] A court will take a "practical, realistic view" of the effect of the relevant conduct.[15] Evidence that a particular person has been misled, whilst persuasive, is neither conclusive nor essential, as a court must determine the question for itself.[16]

Whilst the test is objective, the likely effect of the relevant conduct is not assessed in isolation. Instead, the court identifies the relevant section of the public exposed to the conduct in question and attributes to the audience a standard of sophistication against which the court decides whether the conduct was misleading or deceptive or was likely to mislead or deceive.[17] The audience may be as wide as the public at large or may be confined to a segment of it, such as the "investing public".[18] Thus, in *Fraser v NRMA Holdings*, the Full Federal Court identified the target audience of the demutualisation proposal in the following terms:

> "In the present case the membership of [the NRMA] to whom the prospectus and accompanying documents were addressed comprised some 1.8 million people, a large proportion of the adult population of New South Wales and the Australian Capital Territory. The common bond between them is that they are motorists. It is difficult to envisage a wider cross-section of the community... As the learned trial judge observed, the addressees of the prospectus may be expected to include significant numbers of people

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13 Sections 66(2)(a), (3)(a) and (3)(ba). Theoretically reliance could also be placed on Corporations Regulations 7.12.05(e) and 7.12.06(j) which provide for an exemption where the offeree or subscriber and its associates, including trusts under its management, controls not less than $10 million for the purposes of investment in securities. The difficulty with this exception is that if the offeree or subscriber represents that it qualifies, when in fact it does not, the consequences are borne by the corporation issuing the information memorandum, eg a failure to register it under Part 7.12 CL.

14 *Parkdale Custom Built Furniture Pty Limited v Puxu Pty Limited* (1982) 149 CLR 191, per Gibbs CJ at 198.

15 *Fraser v NRMA Holdings*, Full Federal Court, op cit n 10, at 153.

16 *Taco Company of Australia Inc v Taco Bell Pty Limited* (1982) ATPR 43,732, at 43,752; *Rhone-Poulenc Agrochimie SA v Chemical Services Pty Ltd* (1986) ATPR (Digest) 46-010, per Bowen CJ at 53,045 and Lockhart J at 53,049.

17 *Taco Bell*, ibid, at 43,751.

18 See, for example, *Burswood Management Limited v Burswood Casino View Motel/Hotel Pty Limited* (1987) ATPR 40-824, per Forster J at 48,918.

> who, whilst quite astute in dealing with their day to day financial affairs, have no experience in dealing with shares, with corporate reorganisations, or with a prospectus. ... It is also relevant to note that the addressees may be expected to include not only those who have no experience in dealing with shares or with corporate reorganisations, but also people in that category who are, as well, less astute, less intelligent or less well informed than the average member of the community ..."[19]

The effect of the $500,000 exemption is that usually only professional and institutional investors are able to participate in a capital markets issue.[20] It is likely that a court would attribute a relatively high level of sophistication to this audience. As a result, unlike where the recipients are ordinary members of the public or are relatively unsophisticated, a court probably would be less willing to construe "half truths" and ambiguities in an information memorandum as constituting misleading or deceptive conduct.

Omissions from an Information Memorandum

Normally great care will be taken during the preparation of an information memorandum to ensure that the statements in it can be verified by reference to external materials, such as the underlying transaction documents, the issuer's accounts etc. Traditionally the greatest concern of those involved in the preparation of an information memorandum is that despite all of the precautions that may be taken to ensure that all relevant information is disclosed, an omission may nevertheless occur which could be regarded by a court as constituting misleading or deceptive conduct.

The extent to which "silence" can constitute misleading or deceptive conduct has been, and continues to be, one of the more contentious areas of the case law in relation to section 52 TPA.

The current approach of the courts is to assess whether all the circumstances, such as the relationship between the parties, their knowledge and expertise, previous communications and any other relevant factors, are such as to give rise to a "reasonable expectation" of full disclosure. This was described by Black CJ in *Demagogue Pty Ltd v Ramensky* as follows:

> "Silence is to be assessed as a circumstance like any other ... the question is simply whether, having regard to all the relevant circumstances, there has been conduct that is misleading or deceptive or that is likely to mislead or deceive ... Although 'mere silence' is a convenient way of describing some fact situations, there is in truth no such thing as 'mere silence' because the significance of silence always falls to be considered in the context in which it occurs. That context may or may not include facts giving rise to a reasonable expectation, in the circumstances of the case, that if particular matters exist they will be disclosed."[21]

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19 Op cit n 10, at 144.

20 For example, the Joint Select Committee on Corporations Legislation agreed to the submission by the National Companies and Securities Commission that the $500,000 exemption covered institutional investors so the professional investor exemption originally contained in clause 66(1)(b) of the Corporations Bill could be excluded; Report of the Joint Select Committee on Corporations Legislation, AGPS, 1989, at 9.17.

21 (1992) 39 FCR 31, at 32. The "reasonable expectation" test has been widely accepted. See for example, *Kimberley NZI Finance Limited v Torero Pty Limited* [1989] ATPR (Digest) 46-054; *Winterton Constructions Pty Ltd v Hambros Australia Limited* (1992) 39 FCR 97; *Warner v Elders Rural Finance Ltd* (1993) 41 FCR 399; *Fraser v NRMA Holdings*, Lower Court, op cit n 7; and Full Federal Court, op cit n 10.

Where there is a "reasonable expectation" that certain material will be disclosed, the failure to do so is misleading or deceptive as it implies that the material does not exist. In *Winterton Constructions Pty Ltd v Hambros Australia*, this was explained by Hill J as follows:

> "... if the circumstances are such that a person is entitled to believe that a relevant matter affecting him or her would, if it existed, be communicated, then the failure to communicate it may constitute conduct which is misleading or deceptive because the person who ultimately may act to his or her detriment is entitled to infer from the silence that no danger or detriment existed."[22]

It is reasonable to expect that a person will comply with their general law or statutory duties of disclosure. A failure to do so will almost certainly constitute a breach of sections 52 and 995. A recent example is the decision in *Fraser v NRMA Holdings*. There the Full Federal Court held that the members of the NRMA had a "reasonable expectation" that the directors would comply with their fiduciary duty to make a full and fair disclosure of all factors material to the members making a properly informed decision on the demutualisation proposal. The failure to do so therefore constituted misleading and deceptive conduct for the purposes of section 52. The Full Federal Court stated:

> "The prospectus asserts that under the proposed restructure members will be 'better off' and strongly recommends a 'yes' vote. In these circumstances the failure to identify and inform members about disadvantages of which the directors making the recommendation were aware was to leave the members in a half light which had the potential to lead them to think that the unidentified disadvantages, whatever they might be, must be ones that they would not treat as significant in relation to the rights being given up and the new rights to be acquired in a public listed company. This is more particularly so when it is remembered that, contrary to the notion engendered by the persistent use of the phrase 'Free Shares', the shares might be acquired without significant loss or outgoing, the rights that would be surrendered were significant ones which were material to the members of [the NRMA] in making a properly informed judgment."[23]

A finding of a "reasonable expectation" that certain material would be disclosed is not dependent, though, on whether there has been a breach of an underlying general law or statutory duty of disclosure. As stated by Samuels JA in *Commonwealth Bank of Australia v Mehta*:

> "Silence is not misleading only where there is a duty to disclose at common law or in equity. It may simply be the element in all the circumstances of a case which renders the conduct in question misleading or deceptive."[24]

The reason for this was stated by Bowen CJ in *Rhone-Poulenc Agrochimie SA v UIM Chemical Services Pty Limited*:

> "As in the case of other sections of the Trade Practices Act the Court may gain assistance from consideration of cases at common law and in equity dealing with related types of

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22 Ibid, at 114.

23 Op cit n 10, at 160. Interestingly, at page 143 the Full Federal Court indicated that the directors were under a duty to make full disclosure of relevant information not only pursuant to their fiduciary duties but also under section 1022 of the Corporations Law. This suggests that a failure to comply with section 1022 could, on the reasonable expectation test, constitute misleading or deceptive conduct. If this is correct, section 996 CL would become largely redundant. It also raises the issue of the continuing relevance of the defences in sections 1007-1011, as these would be inapplicable in an action based on section 52 TPA.

24 (1991) 23 NSWLR 84, at 88.

situations. However, the Court is not confined by such cases because it is concerned with the interpretation and application of the words of a particular statute ..."[25]

The test of whether an omission from an information memorandum constitutes a breach of sections 52 and 995 depends, therefore, upon whether an investor had a "reasonable expectation" that the omitted material would be disclosed. Although sections 52 and 995 do not create an independent duty of disclosure,[26] they have the practical result through the "reasonable expectation" test of setting a standard of disclosure in an information memorandum. If the standard is not met, then those responsible are exposed to potential liability for a breach of the sections. It is therefore important for those involved in the preparation of an information memorandum to be able to assess precisely the type of information that a court is likely to consider should be disclosed in a capital markets issue of securities.

The decision in *NatWest Australia Bank Limited v Tricontinental Corporation Ltd*[27] indicates some of the factors that a court may take into account in determining whether an omission from an information memorandum constitutes a breach of sections 52 and 995. There an information memorandum was prepared by Tricontinental to invite NatWest (and others) to participate in a syndicated loan to Pro Image. Tricontinental however failed to disclose the existence of certain guarantees by Pro Image, which were known to Tricontinental, of a compact disc maker, Disctronics.

The court considered that the following factors were relevant in determining whether there was a duty to disclose particular information in the information memorandum:

(i) the relationship between NatWest and Tricontinental;

(ii) the nature of the commercial enterprise;

(iii) the role of Tricontinental in the enterprise;

(iv) whether the information was "material and important" to the decision; and

(v) whether the author had knowledge of the facts.

The court concluded that the existence of the guarantees would have been material and important to NatWest. The NatWest executive who approved the loan did not want an exposure to the compact disc industry and therefore would have rejected the Tricontinental invitation had he known of Pro Image's guarantee of Disctronics. It was held, therefore, that Tricontinental had breached section 52 and was liable to compensate NatWest for its loss.

The relevance, though, of the court's approach in *Tricontinental* to a capital markets information memorandum is complicated by the uncertainty regarding whether, as syndicate promoter and manager, Tricontinental owed a fiduciary duty of disclosure to NatWest. This was alleged but was not specifically dealt with in the decision. Nevertheless it may have influenced the outcome.

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25 Op cit n 16, at 53,047.

26 *Demagogue Pty Ltd v Ramensky*, op cit n 21, per Gummow J at 40; *Fraser v NRMA Holdings*, Full Federal Court, op cit n 10, at 143. Cf *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd* (1988) 79 ALR 83, per Lockhart J at 95.

27 Unreported, Supreme Court of Victoria, No 2493 of 1990.

The approach of the court in *Tricontinental* involved, amongst other things, an assessment of whether the relevant omitted information was material. This was also adopted by the Full Federal Court in *Fraser v NRMA Holdings*. There the court stated:

> "The need for an applicant to establish materiality is of particular importance in a case like the present one where the proposal is complex, and involves difficult questions of commercial judgment and matters of degree and conjecture as to the future about which there is room for a range of honestly and reasonably held opinions ... In the circumstances the Court should not be quick to conclude that a contravention of section 52 has occurred because other information could have been provided that was not. The need for the applicants to establish the materiality of errors and omissions is an important step in the proof of their claims."[28]

The emphasis on materiality in *Tricontinental* and *NRMA* suggests that this may be a touchstone for whether an omission will give rise to a breach of sections 52 and 995. Strictly speaking, though, this is a secondary issue. The initial question is not whether the relevant omission was material but whether in all the circumstances an investor had a "reasonable expectation" that all material information would be disclosed. Where there is no such expectation, the materiality or otherwise of the omission cannot affect the outcome. Materiality only becomes relevant if the audience, as in *Tricontinental* and *NRMA*, had a "reasonable expectation" that all relevant information would be disclosed.

The decisions in *Tricontinental* and *NRMA*, whilst dealing with analogous circumstances, in light of the foregoing, probably only have limited value in terms of giving an insight into the likely approach of the courts as to the "reasonable expectations" of a capital markets investor.

The approach of a court probably will turn on its assessment of the function and role of an information memorandum in the investment process. Unfortunately there does not appear to be any consensus on this subject. There are two opposite views:

(i) The first is that investors typically do not have access, nor are privy, to all information relating to the particular capital markets securities. An information memorandum, therefore, performs a function similar to that of a prospectus by providing an intending investor with all material information necessary to make an investment decision. Accordingly, the information that an investor would expect to be disclosed in an information memorandum is similar to the standard set out in section 1022 CL for a Part 7.12 prospectus - ie all information that an investor would reasonably require and reasonably expect for the purpose of making an informed assessment of the issuer and the relevant securities.

(ii) The contrary view is that those who prepare an information memorandum are not investors. They cannot predict all the information that would be relevant to an investment decision. Whilst all due care may be taken to prepare an information memorandum, there is no guarantee that it contains all relevant information. It is the duty of each prospective investor to satisfy themselves on this front. If a prospective investor fails to adequately protect its interests, this should not lead to liability for those who prepare an information memorandum.

There is some merit in both views. On one hand, investors are largely dependent on the disclosures in an information memorandum in making their investment decisions. On the other, to require disclosures equivalent to a section 1022 standard would be to equate capital markets

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28 Op cit n 10, at 132-133.

investors to members of the public, yet the present legislative scheme is founded on the assumption that sophisticated investors do not need the protection of prospectus legislation.[29]

The doubt regarding the appropriate standard of disclosure in an information memorandum represents a major deficiency with the present situation. It creates a substantial uncertainty for those involved in the preparation of an information memorandum regarding the disclosures necessary to avoid liability for a breach of sections 52 and 995. It also places an unfair burden on issuers. The reason for this is that, in an effort to minimise their potential liability under sections 52 and 995, many issuers measure the adequacy of their disclosures by reference to section 1022 and also engage in due diligence (to varying levels of sophistication). These issuers, therefore, adopt the higher disclosure levels for Part 7.12 prospectuses and incur the costs of a due diligence program, but without enjoying the corresponding benefits that accompany this such as access to the defence in section 1011(1) CL.

Inadvertent Omissions

Another area of uncertainty in relation to omissions regards whether an inadvertent (as opposed to deliberate) failure to make a disclosure in an information memorandum can breach sections 52 and 995.

The expression "conduct" is defined in section 4(2) TPA as, amongst other things, "doing or refusing to do an act" and a reference to "refusing to do an act" is defined therein as including "refraining (otherwise than inadvertently) from doing that act". An identical definition of "conduct" appears in section 762 CL.

The exception in sections 4(2) TPA and 762 CL that conduct does not include an inadvertent failure to do an act suggests that an innocent omission from an information memorandum will not lead to a breach of sections 52 and 995. This view was taken by Bowen CJ in *Rhone-Poulenc Agrochimie SA v UIM Chemical Services Pty Limited* where he stated:

> "The appellants submit that UIM's failure to warn customers of the risks of seizure and forfeiture constituted 'engaging in conduct' within the special definition in section 4(2). I do not agree. Although section 4(2) recognises that an omission to do an act may constitute 'engaging in conduct', that will only be so where there has been a refusal to do, or a deliberate refraining from doing, an act. The words 'refuse' and 'refrain' clearly connote that the omission to do an act must be deliberate."[30]

Similarly, in *Spedley Securities Ltd v Bank of New Zealand*, Cole J stated:

> "One cannot fail to inform of matter of which one was not aware. Conduct proscribed by section 52 which may be constituted by refusing to do an act includes refraining from doing an act (otherwise than inadvertently ...). Concepts of 'refusal' or 'refraining' involve some mental process of decision-making, or at least, the existence of circumstances where a body may be reasonably taken to be required to make a decision. There can be no such actual or deemed decision-making in the absence of knowledge of facts in respect of which such decision is to be taken."[31]

However, although this approach gleans support from the wording of section 4(2) TPA, and protects those responsible for an information memorandum from liability for innocent omissions, it is in tension with the well established principle that knowledge is not a necessary ingredient for

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29 See the discussion in the section "'Excluded' Issue, Offer and Invitation" below and the references cited therein.

30 Op cit n 16, at 53,046.

31 (1991) 13 ATPR 41-143, at 53,065.

a breach of section 52 (and presumably section 995). In *Parkdale Custom Built Furniture Pty Limited v Puxu Pty Limited*, Gibbs CJ said:

> "There is nothing in the section that would confine it to conduct which was engaged in as a result of a failure to take reasonable care. A corporation which has acted honestly and reasonably may therefore nevertheless be rendered liable to be restrained by injunction and to pay damages if its conduct has in fact misled or deceived or is likely to mislead or deceive."[32]

The relationship between silence and section 4(2) was specifically dealt with by Gummow J in *Demagogue Pty Ltd v Ramensky*:

> "'Conduct' within the meaning of section 52 includes refusing to do an act and refusal to do an act includes a reference to 'refraining (otherwise than inadvertently) from doing that act': section 4(2). But in any case where a failure to speak is relied upon the question must be whether in the particular circumstances the silence contributes or is part of misleading or deceptive conduct. The expanded meaning given by section 4(2) to 'conduct' should not distract attention from the fundamental issue in the case at hand."[33]

This approach was endorsed by the Full Federal Court in *Fraser v NRMA Holdings*:

> "... for the purposes of section 52, if by reason of what was said and what was left unsaid the conduct of the corporation is misleading or deceptive or likely to mislead or deceive, a contravention would occur even if the corporation through its directors and officers did not have knowledge of the undisclosed facts which rendered the conduct in breach of section 52."[34]

The implication of this approach is that if the "reasonable expectation" test carries with it a standard of disclosure, as seems likely, and an issuer innocently fails to meet that standard, even after say "due diligence", then a breach of sections 52 and 995 could occur. This imposes a very exacting, if not unfair, requirement on issuers and is to be compared to the more favourable treatment in relation to Part 7.12 prospectuses where a liability for a breach of section 996(2) can be met by the due diligence defence of section 1011(1).

An alternative approach is for the courts to incorporate within the "reasonable expectation" test a standard of diligence in relation to an information memorandum. For example, they may consider that capital markets investors would reasonably expect an information memorandum to only state material known to the issuer or that the information memorandum would only be issued after due diligence by those responsible for its preparation. This would deal with the problem of the potential liability that an issuer has for omissions not known to it, and would also be consistent with the likely expectation of capital markets investors. However, until the issue is considered by the courts, those responsible for the preparation of an information memorandum face the prospect of potential liability for failing to disclose information which was not known to them.

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32 Op cit n 14, at 197. See also *Hornsby Building Information Centre Pty Ltd v Sydney Building Information Centre Ltd* (1978) 140 CLR 216, at 228; and *Yorke v Lucas* (1985) 158 CLR 661, at 666.

33 Op cit n 21, at 40.

34 Op cit n 10, at 144.

LIABILITY FOR A BREACH OF SECTIONS 52 AND 995

The Consequences of a Contravention

A breach of section 52 does not constitute an offence (section 79(1) TPA). An injured person can claim for their loss by way of a civil action pursuant to section 82 TPA. In addition, an injunction (section 80), a disclosure order (section 80A) or remedial orders (section 87) may also be available. The regime for a breach of section 995(2) CL is similar. Section 995(3) CL provides that a breach of section 995(2) is not an offence. Instead, a person who suffers loss or damage by conduct in breach of section 995(2) may recover the amount of this under section 1005 CL which is modelled on section 80 TPA. In addition, an order prohibiting payment or transfer of money, securities or other property (section 1323), an injunction (section 1324) and other orders (section 1325) may also be available.

Two Classes of Persons Exposed to Civil Liability

Sections 82 TPA and 1005 CL impose civil liability on the person who engaged in the conduct constituting the contravention and on any other person involved in the contravention.

Engaged in a Contravention

Normally, an information memorandum will identify the party that takes responsibility for its contents. It is that person who engages in the relevant conduct for the purposes of sections 52 and 995. Usually this will be the issuer of the relevant securities or, in the case of a securitisation, the manager or sponsor of the program. Sometimes, where a number of parties have prepared an information memorandum, they will take responsibility for their individual portions. A single information memorandum in these circumstances can, therefore, comprise a series of separate instances of conduct by different parties.

Section 764 CL provides, among other things, that a reference to doing an act for the purposes of section 762(1) CL includes a "reference to causing, permitting or authorising the act ... to be done". Interestingly, there is no equivalent to section 764 in the TPA. The effect of section 764 is to widen the class of individuals that could be liable for a breach of section 995, than would be the case in relation to section 52. As a result, the directors who formally authorise the issue of a defective information memorandum are probably deemed to engage in a contravention of section 995. However if the relevant action was brought under section 52, their liability would depend on whether they satisfied the statutory requirement of being "involved" in a contravention (see below).

A phrase analogous to that appearing in section 762(1) CL has also been criticised as being too imprecise, and that there is little precedent as to its meaning, so as to give guidance as to the classes of persons embraced by it.[35] For example, external parties who assist in the preparation of an information memorandum are concerned that they could fall within the phrase and hence be liable if the information memorandum is defective. This uncertainty is inappropriate, particularly in a situation as here, where enormous potential liability depends on the outcome. Instead, those who could be liable for a defective information memorandum should be precisely identified so that they can take any necessary action to avoid, or mitigate, the risks of being associated with it. This has been one of the concerns in relation to the equivalent civil liability provisions for a Part 7.12 prospectus and applies with equal merit in relation to an information memorandum.

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35 Report of the Prospectus Law Reform Sub-Committee (the "Lonergan Committee"), March 1992, at 92, in relation to the equivalent phrase "authorise or cause the issue of a prospectus" in section 996.

Involved in a Contravention

Both the TPA and the CL contain provisions which define exhaustively the phrase "involved in a contravention". For example, section 79 CL provides as follows:

> "Subject to section 1006, a person is involved in a contravention if, and only if, the person:
>
> (a) has aided, abetted, counselled or procured the contravention;
>
> (b) has induced, whether by threats or promises or otherwise, the contravention;
>
> (c) has been in any way, by act or omission, directly or indirectly, knowingly concerned in, or party to the contravention; or
>
> (d) has conspired with others to effect the contravention."

Section 75B TPA is in substantially the same terms.

The case law under the TPA indicates that in order for a person to satisfy section 75B TPA (and, because of the similarity of the language, presumably also section 79 CL), knowledge of the actual contravention on the part of the person "involved" is required, or, as a minimum, that the person's participation was in the context of knowledge of the essential facts constituting the particular contravention in question.[36]

The Possible Extended Scope of Section 1006

As can be seen from above, section 79 CL leaves room for the operation of section 1006.

That section in turn, when it applies, removes the requirement of a mental element (that is knowledge) to establish a person's involvement in a contravention. This is achieved by deeming certain classes of persons to be involved in a contravention for the purposes of liability under section 1005. These include the issuer, the directors of the issuer, experts who have consented to statements in a prospectus, underwriters, auditors, bankers and solicitors named with consent in the prospectus and any other person named with consent in the prospectus as having performed any function in a professional, advisory or other capacity for the issuer or in relation to the issue of the securities (section 1006(2)).

In order for this extended class to avoid liability, sections 1007 to 1011 provide for a number of defences which vary depending upon the category of the individual concerned. The most widely known of these is the "due diligence" defence of section 1011(1).

There is considerable uncertainty whether or not section 1006 and the defences following it, apply in relation to an action brought under section 1005 for breach of section 995. The application of section 1006 to a defective information memorandum has, though, mixed results. On the one hand, section 1006(2) extends the class of persons that could be liable for a defective information memorandum, but at the same time the defences provide a shield against potential liability for a breach of section 995. For example, if an issuer of an information memorandum undertakes "due diligence", then it, any underwriter named in the information memorandum and any person who authorised or caused the issue of the information memorandum would have the benefit of the defence in section 1011(1).

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36 *Yorke v Lucas*, op cit n 32, at 666-669.

The scope of section 1006 is set out in subsection (1) as follows:

> "This section applies for the purposes of an action under section 1005 in respect of conduct being the issue of a prospectus in relation to securities of a corporation:
>
> (a) in which there is a material statement that is false or misleading; or
>
> (b) from which there is a material omission."

In many cases "misleading or deceptive conduct" in the context of an information memorandum will spring from a "material statement that is false or misleading" or from a "material omission". This suggests that section 1006 could apply in such circumstances to a breach of section 995.

On the other hand, the substantive language of section 1006(1) is an exact repetition of section 996(1)(b), which does not apply, by virtue of section 996(1)(a), to an information memorandum. The Explanatory Memorandum for the Corporations Law suggests that it was intended that section 1006 would only apply in connection with a contravention of section 996.[37] Also, it would seem illogical for some contraventions of section 995 to require the plaintiff to prove an accessory's state of mind (that is under section 79), yet for other contraventions under the same section to place no such burden on the plaintiff in relation to the same persons (that is under section 1006). Also, many of the defences in sections 1007 to 1011 assume that liability under section 1006 can only arise for a Part 7.12 prospectus (see, for example, sections 1008A(2) where it refers to a consent under section 1032, and also sections 1009(3)(a), 1009(3)(b) and 1009(4)(a)).

Unfortunately, it is difficult to come to any firm conclusion on this point. On the one hand, there are good arguments for saying that section 1006 does not apply in relation to an action based on a breach of section 995. Yet, on the other hand, as the legislation is currently drafted, there appears to be clear overlap leading to potential liability, and defences, for the wider class of persons referred to in section 1006(2).[38] To the extent to which a defendant may seek to rely on the defences, the debate though is very much academic if that person would, in the absence of section 1006(2), be liable under section 52 TPA. It is clear in relation to the latter that there are no defences.

The Position of Dealers

Capital markets securities are normally issued through a dealer panel. The name of each dealer often appears on the front page and in the body of the information memorandum as performing this role. The dealers also distribute the information memorandum to potential investors, sometimes accompanied by supplementary materials prepared by them regarding the securities on offer. Normally an information memorandum will indicate that the contents are the responsibility of the issuer or sponsor and that the dealers have not prepared, and do not accept liability, for the information memorandum (except, perhaps, in relation to nominated sections prepared by a particular dealer).

A dealer, though, can be exposed to potential liability on a defective information memorandum in a variety of ways. It will, for example, be liable for those sections in respect of which it has specifically accepted responsibility. In addition, depending on the extent to which it has assisted

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37 Op cit n 5, at paragraph 2993. The Explanatory Memorandum refers to section 107 of the former Companies Act 1981, which in turn related to the former section 108 which was the basis for section 996.

38 A number of commentators believe that the better view is that section 1006(2), and the subsequent defences, apply to a breach of section 995. See for example, Golding, op cit n 5, at 423-424; J Azzi, "Disclosure in Prospectuses" (1991) 9 *C&SLJ* 205, at 231; and the Corporations Law Simplification Task Force, Report on Fundraising, Attorney-General's Department, 1995, at 18 n 2.

in the preparation of the information memorandum, it may be liable on the basis that it has "caused" its issue for the purposes of section 762(1) CL. Also, if section 1006(2) applies to an information memorandum, a dealer may be an "expert", "underwriter" or other person performing a "function in a professional, advisory or other capacity" for the purposes of sections 1006(2)(e), (f) and (h) respectively.

Another area of risk for dealers is that by innocently distributing a defective information memorandum, notwithstanding the disclaimer referred to above, they will incur liability for a contravention of sections 52 and 995.

The position of intermediaries, who pass on information prepared by another, is still being developed by the courts.

In *Yorke v Lucas* the High Court stated:

> "That does not, however, mean that a corporation which purports to do no more than pass on information supplied by another must nevertheless be engaged in misleading or deceptive conduct if the information turns out to be false. If the circumstances are such as to make it apparent that the corporation is not the source of the information and that it expressly or impliedly disclaims any belief in its truth or falsity, merely passing it on for what it is worth, we very much doubt that the corporation can properly be said to be itself engaging in conduct that is misleading or deceptive."[39]

However, in *Gardam v George Wills and Co Ltd*, French J said:

> "When, however, a representation is conveyed in circumstances in which the carrier would be regarded by the relevant section of the public as adopting it, then he makes that representation."[40]

The dividing line between the two situations considered in *Yorke v Lucas* and *Gardam v George Wills* is obviously very fine. The difficulty for dealers in this area is highlighted by the decision in *John G Glass Real Estate Pty Limited v Karawi Constructions Pty Limited.*[41] There, a real estate agent, acting for the vendor in the sale of an office building, passed on an incorrect figure for the net lettable area of the building. The figure was included in a brochure indicating that the source was a consultant acting for the vendor. The front page of the brochure contained the name of the real estate agent. The brochure also contained a disclaimer stating, amongst other things, that the information in the brochure had been prepared with care by the real estate agent or had been supplied to it by apparently reliable sources and that the real estate agent had no reason to doubt its completeness or accuracy. The disclaimer went on to state that the real estate agent did not guarantee the information and that all interested parties should make their own inquiries to verify the information and that it was the responsibility of interested parties to satisfy themselves in all respects regarding the property.

The Full Federal Court held that the real estate agent was liable under section 52 for damages to the purchaser for the incorrect figure. The court stated:

> "In our opinion an estate agent which holds itself out as, amongst other things, 'consultants to institutional investors and to developers of major properties' would not be regarded by potential purchasers of properties as merely passing on information about the property 'for what it is worth and without any belief in its truth or falsity' ... In the present case the [real estate agent] adopted the information in question and incorporated it as an essential and prominent feature of their selling effort on behalf of the vendor. There was certainly no

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39 Op cit n 32, at 666.

40 (1988) 82 ALR 415, at 427.

41 (1993) ATPR 41-249.

expressed disclaimer of the [real estate agent's] belief in the truth of the information in the brochure - indeed there was an express assertion of such belief. As part of its ordinary business the agent was providing the information in a persuasive form with a view to achieving a sale of its principal's property and of course earning commission. It was this conduct which the learned trial judge, correctly in our opinion, held to be misleading and deceptive. Once the falsity of the figure was demonstrated, it seems to us that no other conclusion could follow."[42]

The decision in *John G Glass Real Estate* highlights the risk that a dealer assumes under sections 52 and 995 by innocently distributing a defective information memorandum, as well as the ineffectiveness of any warning that may accompany or be included in the information memorandum that the dealer has not verified the accuracy of the information contained therein and that potential investors should undertake this task themselves.

Another area of risk for dealers is that by merely being associated with the issue of the relevant securities, an erroneous implication may be drawn by investors regarding the veracity of the material contained in the information memorandum. An example of this is the Dutch decision of *Association of Bondholders Coopag Finance BV v ABN AMRO Bank NV*.[43] There, ABN AMRO, who was the lead manager in a euro-bond issue, was held liable under the Dutch Civil Code (which is analogous in its relevant terms to sections 52 and 995) in relation to a defective information memorandum. This was on the basis that its participation implied that it had engaged in due diligence of certain materials contained in the information memorandum, when in fact it had not undertaken this.

DISCLAIMERS

Their Use in an Information Memorandum

An information memorandum almost always contains a detailed disclaimer or exclusion of liability. This is usually found in the Important Notice section at the front of the information memorandum.

Disclaimers vary in their language, but usually fall into one of two classes:

(i) Often, but not always, the information memorandum contains an express denial of liability in respect of representations or statements contained in it.

(ii) Usually investors will be directed to make and rely upon their own enquiries in relation to the securities on offer.

Disclaimers as a Means of Avoiding a Contravention

It is clear that a disclaimer cannot oust section 52 TPA (and presumably section 995 CL).[44] Section 52 "embraces public rather than private rights and, as an expression of public policy, is

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42 At 41,359.

43 For a description of the decision, see F G B Graaf and R F Bertrams, "Prospectus Liability of Lead Managers in the Netherlands", IBA Section on Business Law, Issues and Trading in Securities, July 1995, at 5; and H E M Velthuyse and F M Schlingmann, "Prospectus Liability in the Netherlands" [1995] 6 *JIBL* 229.

44 *Petera Pty Ltd v EAJ Pty Ltd* (1984) 7 FCR 375; *M K Hutchence and Ors (Trading as "INXS") v South Sea Bubble Co Pty Ltd (trading as "Bootleg T-Shirts")* (1986) 8 ATPR 40-667; *Clark Equipment Australia v Covcat* (1986) 71 ALR 367.

incapable of being affected by the will of the parties."[45] It cannot, therefore, be contracted out, irrespective of the sophistication or desire of the parties. Where, therefore, a person engages in misleading or deceptive conduct through a defective information memorandum, a disclaimer to avoid statutory liability will be ineffective.

This, though, should not be confused with a provision, also often found in the Important Notice, which allocates responsibility for the contents of the information memorandum amongst various parties and states that a party is not liable for the other sections of the information memorandum. Such a provision makes it clear which portion of the information memorandum constitutes a given party's conduct for the purposes of sections 52 and 995. The denial of liability in this circumstance in relation to the balance of the information memorandum should be effective; unless the party engages, or is concerned, in other "conduct" attracting sections 52 and 995.

Using Disclaimers to Eliminate Reliance

Sections 82 TPA and 1005 CL each require that the plaintiff establish a causal connection between the misleading and deceptive conduct and the loss claimed ("loss or damage *by* conduct of another person"). In *Pappas v Soulac Pty Ltd*, this was stated by Fisher J as follows:

> "The applicants will only be entitled to an award of damages under section 82 of the Act if they establish that they were induced by the representation ... to enter into the ... contract ... The question in each instance is whether they acted upon the statements ... in the sense of placing reliance upon the conduct in entering into the contract. There must be a causal connection between the conduct and the loss for which they seek to be compensated."[46]

The second class of disclaimer referred to above seeks to eliminate the causal connection between the misleading or deceptive conduct represented by a defective information memorandum and the alleged damage, by advising intending investors that they must not rely on the information memorandum.

Whilst the courts have unhesitatingly rejected the first class of disclaimer, they have been more sympathetic with the second and have been prepared to entertain its efficacy in some circumstances. As stated by French J in *Kewside Pty Ltd v Warman International Limited*:

> "A disclaimer or exclusion clause will affect liability for misleading or deceptive conduct only if it or breaks the causal connection between conduct and loss. Whether it has the effect in a given case is a question of evidence and not a question of law."[47]

Although these are some authorities in support of the second class of disclaimer, a consistent and uniform judicial approach has yet to emerge on this issue.[48] It is likely that the courts would be more prepared to uphold such a disclaimer where the recipient, as with a capital markets issue, is sophisticated. However, it is equally likely that a court's approach would also be influenced by its assessment of how practical it would have been for an investor to rely on its own

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45 A Terry, "Disclaimers and Deceptive Conduct", [1986] *ABLR* 478, at 479.

46 (1983) 50 ALR 231, at 238.

47 (1990) 12 ATPR (Digest) 46-059 at 53,222. For examples where such a disclaimer has been held to be effective, see *Keen Mar Corporation Pty Limited v Labrador Park Shopping Centre Pty Limited* (1989) ATPR (Digest) 46-048; and *Khalaf Agaiby v Darlington Commodities Limited* (1985) ATPR 40-535.

48 For examples where a disclaimer was ineffective, see *NatWest Australia Bank Limited v Tricontinental Corporation Ltd*, op cit n 27; and *John G Glass Real Estate Pty Limited v Karawi Constructions Pty Limited*, op cit n 42.

inquiries. If the court takes the view that an investor could not have reasonably implemented the direction in the disclaimer, then it probably will not give effect to its terms.

The Need for Disclaimers

The reasons, and hence the legitimacy, for using a disclaimer obviously vary depending upon the circumstances. In many cases its presence reflects a perception by those responsible for the preparation of an information memorandum that sections 52 and 995 unduly favour the interests of investors at their expense. Disclaimers in their various forms, because of their uncertain status, also cloud any legal analysis of the impact of sections 52 and 995. If the causal connection can be broken by an appropriately worded disclaimer, or if a provision that the maker believes a statement is true to the best of its knowledge can oust the objective element of sections 52 and 995, then the results of an assessment of the risks posed by the sections would be radically different from where one assumes these would be ineffective. Also from a policy perspective a disclaimer is an unsatisfactory means for addressing the problem. It is a legal device that is targeted at one of the essential elements of a plaintiff's case - ie reliance. A disclaimer does not introduce a new element which might achieve a more satisfactory balance in the relationship between those responsible for the preparation of an information memorandum and investors. A preferable approach would be to eliminate the need for disclaimers through regulatory intervention to establish this balance by, for example, providing defences equivalent to those in the CL for Part 7.12 prospectuses.

REVIEW OF SOME OF THE ASSUMPTIONS UNDERLYING THE PRESENT REGULATORY SCHEME

"Excluded" Issue, Offer and Invitation

The policy underlying denying the recipients of "excluded" issues, offers and invitations specific legislative protection is that they can independently obtain the necessary information to properly assess the proposed investment. The policy assumes that investors in this category can - and importantly will - actively seek out the necessary information.[49]

Although this may be a reasonable assumption for most recipients of an "excluded" issue, offer or invitation, arguably it is not applicable to the majority of capital market investors. They are largely passive and by and large rely on an information memorandum as the basis of making their investment decision. The divergence between their behaviour and that expected of other recipients of an "excluded" offer, issue or invitation, raises the question of whether the current regime is appropriate in their case. Their dependence on material contained in an information memorandum perhaps suggests that they warrant a greater level - or at least a different form - of legislative protection than afforded at present. Also, the present legislative scheme predates the emergence of the capital markets as a significant area of investment activity and since then there has been no serious examination of whether investors in this market should be encompassed by the "excluded" issue, offer or invitation concept.

On the other hand, it could also be said that capital markets investors have the capacity to make the necessary enquiries, perhaps as inconvenient and time-consuming as these would be. If they choose instead to be passive, this does not of itself justify a change of law and they should bear the consequences of their decision. Interestingly, it is not so clear that this would be the outcome under sections 52 and 995. If the courts conclude that capital markets investors have a "reasonable expectation" that all material information would be disclosed in an information

[49] Interim Report of the Securities Information Review Committee, National Companies and Securities Commission, 1988, at 3.2; Report of the Joint Select Committee on Corporations Legislation, 1989, at 9.17; Lonergan Committee; op cit n 35, at 92.

memorandum, then sections 52 and 995 could afford such sophisticated investors, whether they are passive or active, substantially greater protection than was originally intended to be the case.

The Appropriateness of Sections 52 and 995 to the Securities Industry

A threshold issue which needs to be examined is whether sections 52 and 995 are appropriate to the securities industry as a whole. As mentioned above, traditionally the goal of securities regulation has been to seek a balance between the interests of investors and those responsible for the preparation of a prospectus. Thus, for Part 7.12 prospectuses, civil liability is imposed on those who are responsible for the preparation of the prospectus for any material misstatements and omissions (sections 996, 1005 and 1006 CL). However, the balance is achieved by extending to the class of section 1006 persons the benefit of the defences in sections 1007-1011. Section 52, on the other hand, is essentially a consumer protection device. It is not concerned with balancing the interest of the parties nor with ensuring that the raising of capital is not unduly impeded. Instead it favours the consumer at the expense of the corporation.

At the time of the introduction of section 995, there does not appear to have been any consideration of its relevance to the securities industry nor whether the securities industry has special qualities warranting differential legislative treatment. In the context of Part 7.12 prospectuses, there now seems to be widespread recognition of the difficulties posed by sections 52 and 995.[50] To the extent that there is an overlap between sections 52 and 995 (on the one hand) and section 996 (on the other), the application of the former undoes the balance referred to above by imposing strict liability for a breach.

The Corporations Law Simplification Task Force (CLSTF) recommends resolving the problem by exempting Part 7.12 prospectuses from sections 52 and 995.[51] This is quite a controversial proposal and is likely to be strongly resisted on the basis that section 52 (and section 995) have become a minimum standard of commercial conduct in Australia. If it is implemented, a significant portion of commercial activity will then be exempt from this standard. If a special case can be made out for Part 7.12 prospectuses, then it leaves the way open for other industries to also seek an exemption, thus watering down the universal operation of section 52. This perhaps indicates how ingrained section 52 is in our legal system and the difficulty in resolving a situation, as here, where it conflicts with another regime that has a different origin and goals. Nevertheless, ultimately the two regimes are incompatible and a solution needs to be found.

The debate regarding the application of sections 52 and 995 to a Part 7.12 prospectus raises a broader issue of whether the sections ought to apply at all to the securities industry and more particularly to an information memorandum. The CLSTF justifies exempting Part 7.12 prospectuses from the operation of sections 52 and 995 on, amongst other things, the following grounds:

> "Despite taking every possible precaution to comply with the requirements of the Corporations Law, business is likely to remain exposed to liability because it is not able to rely on the Corporations Law defences. The result is to increase the cost of fund raising by Australian business."[52]

These words could just as equally apply to the capital markets. It is hard to escape the conclusion that if sections 52 and 995 are inappropriate for the public equity markets, because they disturb the balance between the interests of investors and issuers, and so impede the raising of capital, then this must also be the case for the capital markets.

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50 Lonergan Committee, op cit n 35, at 91; Golding, op cit n 5, at 432; R Austin, "NRMA Float opens a Can of Worms", [1995] *ABM* 55; M Legg, op cit n 12; and the Corporations Law Simplification Task Force, op cit n 38, at 18-20.

51 Op cit n 38.

52 Op cit n 38, at 20.

The CLSTF proposal, if implemented, could also lead to an inconsistency of treatment between an information memorandum and a Part 7.12 prospectus. The CLSTF recognises that there is a substantial overlap between sections 52 and 995 (on the one hand) and section 996 (on the other). If the proposal is implemented, an omission of certain material from a Part 7.12 prospectus that constitutes a breach of section 996 will be subject to defences, however, the omission of the same material in an information memorandum could lead to strict liability under section 52. One of the possible consequences of this is that the intended legislative scheme for civil liability for a defective information memorandum and a Part 7.12 prospectus could be reversed where sections 52 and 995 overlap with section 996. If a member of the "public" were to sue on a defective Part 7.12 prospectus their recourse for loss could be defeated by the defences, whilst a sophisticated investor could obtain compensation for loss on a defective information memorandum without being frustrated by the defences.

CONCLUSION

There are clearly many shortcomings in relation to the application of sections 52 and 995 to an information memorandum. These include:

(i) the present, and probably foreseeable, uncertainty posed by the "reasonable expectation" test which sets the standard of disclosure in an information memorandum;

(ii) the strict liability of sections 52 and 995. Whilst defences such as "due diligence" are applicable for Part 7.12 prospectuses, those who prepare an information memorandum do not have the benefit of these;

(iii) the uncertainty regarding whether the extended class of persons in section 1006(2) could be liable on a defective information memorandum and, if so, whether they have the benefit of the defences in section 1007-1011;

(iv) the uncertain position of dealers regarding whether they engage in a contravention of sections 52 and 995 when distributing a defective information memorandum; and

(v) the doubts surrounding the efficacy of disclaimer clauses in an information memorandum.

Apart from the above deficiencies, sections 52 and 995 also appear to be inappropriate to the securities industry. The sections are essentially consumer remedies and lack the balance needed between the interests of investors and those responsible for the preparation of an information memorandum. It would seem to follow that if the sections are undesirable in their application to a Part 7.12 prospectus, then this must also be the case for a capital markets information memorandum. As such, their continued application to an information memorandum may impede the otherwise natural evolution of the capital markets in Australia. There is a growing list of amendments necessary to Parts 7.11 and 7.12 CL, but rather than implementing these in a piecemeal fashion, it would be preferable for a complete review to be undertaken with a view to achieving a consistent and comprehensive regime for information memoranda, as well as for Part 7.12 prospectuses, free of the restrictions and present shortcomings of sections 52 and 995.