The conclusion to be drawn from this is that the Court is quite willing to accommodate the wishes of joint venturers who possess even the trappings of an argument where the joint venture agreement allows that the parties need only not act unreasonably.

CONCLUSION

Joint ventures are not partnerships. They are a set of contractual rights and obligations drawn up for a specific set of parties and circumstances. *Noranda*'s case is one of several recent decisions which reserve to venturers almost complete power to decide for themselves their relative rights and obligations.[27] The imposition of fiduciary duties as inherent to a joint venture would have reduced this freedom. Similarly, a restrictive approach to the simple contractual stipulation that one venturer not unreasonably refuse approval of an act by another would have also reduced the potential usefulness of joint ventures. The value of the joint venture is its wide adaptability to the wants and needs of the prospective venturers.

T. G. SEDDON*

[27] See, *e.g. Australian Oil & Gas Corp. Ltd v. Bridge Oil Ltd & Ors* (Ct. App. N.S.W., released 12 April 1989); *United Dominions Corp. Ltd v. Brian Pty Ltd* (1984-85) 157 C.L.R. 1, 10-1 (*per* Mason, Brennan and Deane JJ.): 'The most that can be said is that whether or not the relationship between joint venturers is fiduciary will depend upon the form which the particular joint venture takes and upon the content of the obligations which the parties to it have undertaken.'

* Thomas Garfield Seddon, B.A. (The Ohio State University), J.D. (University of Cincinnati). Arthur Robinson & Hedderwicks, Melbourne.

JEFFREE V. NATIONAL COMPANIES & SECURITIES COMMISSION[1]

INTRODUCTION

As a result of a decision of the Full Court of the Supreme Court of Western Australia this year, the duties of directors under Australian company law may be somewhat extended. This expansion consists of a duty towards not only shareholders and present creditors of the company, but also to prospective creditors of the business. The implications, both legal and economic, may be far reaching.

THE FACTS

Jeffree was charged by the N.C.S.C. under a breach of s. 229(4) of the Companies Code.[2] He was a director of Wanup Pty Ltd which was trustee of the Jeffree family trust. This company carried on business selling swimming pools. Wanup entered into a contract with Leighton Contracts Pty Ltd to construct a pool. There were serious defects in the pool and arbitration ensued to determine who was responsible for the defects.

Fearing an adverse award from the arbitration, the board of Wanup, acting on solicitor's advice, incorporated a new company, Cassidy Holdings Pty Ltd, with the same trustee structure, directors and shareholders as Wanup. Cassidy then purchased Wanup's assets. The trial judge had found that

> The transaction was designed to put Wanup in a position where any liquidation of the company consequent upon any substantial award in the pending arbitration would reap no benefit for Leighton.[3]

[1] (1989) 15 A.C.L.R. 217.

[2] 'An officer or employee of a corporation shall not make improper use of his position as such an officer or employee, to gain, directly or indirectly, an advantage for himself or for any other person or to cause detriment to the corporation.'

[3] (1989) 15 A.C.L.R. 217, 224.

Wanup became a 'dormant shell'[4] and its 'cupboard was virtually bare'.[5] Thus Wanup would have no assets against which Leighton could enforce any award.[6]

A large award was made against Wanup and Jeffree appealed against his conviction under s. 229(4).

THE PRE-EXISTING LAW

A number of authorities exist in support of the proposition that directors of a company owe a duty to creditors.

In *Walker v. Wimborne*,[7] it was accepted by the High Court that the duty of directors extends to creditors. As Mason J. said,

> the directors of a company in discharging their duty to the company must take account of the interest of its shareholders and its creditors. Any failure by the directors to take into account the interests of creditors will have adverse consequences for the company.[8]

According to *Kinsela v. Russell Kinsela Pty Ltd*[9] and *Nicholson v. Permakraft (N.Z.) Ltd*,[10] creditors may be said to be beneficially interested in the company's assets or contingently so where the company is in a state of insolvency or marginal insolvency. In the *Kinsela* case, Street C.J. said

> But where a company is insolvent the interests of the creditors intrude. They become prospectively entitled, through the mechanism of liquidation to displace the power of the shareholders and directors to deal with the company's assets. It is in a practical sense their assets and not the shareholders' assets that, through the medium of the company, are under the management of the directors pending either liquidation, return to solvency or the imposition of some alternative administration.[11]

THE JUDGMENTS

The court unanimously affirmed these previous decisions, and proceeded one step further by holding that the duty of directors extends to future or prospective creditors. In doing so, a statement of Lord Templeman in *Winkworth v. Edward Barron Development Co. Ltd*[12] was emphatically adopted:

> But a company owes a duty to its creditors, present and future. The company is not bound to pay off every debt as soon as it is incurred and the company is not obliged to avoid all ventures which involve an element of risk, but the company owes a duty to its creditors to keep its property inviolate and available for the payment of its debts. The conscience of the company, as well as its management, is confided to its directors. A duty is owed by the directors to the company and to the creditors of the company to ensure that the affairs of the company are properly administered and that its property is not dissipated or exploited for the benefit of directors themselves to the prejudice of the creditors.[13]

Wallace J. found that Jeffree knew the company faced liquidation and that the transaction that was instigated jeopardized Wanup's solvency and its pool of funds in the event of bankruptcy. Not only had he failed to act in the creditors' interests, but he had positively worked against them.

Brinsden J. concurred broadly with Wallace J., making particular reference to the meaning of the word 'improper' in the section. Referring to *Grove v. Flavel*,[14] he held 'improper' to be a flexible standard, understood in a commercial context, specifically referable to the duties and obligations of the company officer. Although the transfer of the assets was *prima facie* not improper, its motive, being to deny Leighton the benefit of its award, tainted it. Further, he held that s. 229(4) was to be

4 *Ibid*. 219.
5 *Ibid*. 220.
6 Thus, at the time of the transfer, Wanup could be said to be in a state of marginal or imminent insolvency (due to the pending arbitration claim).
7 (1977) 137 C.L.R. 1.
8 *Ibid*. 7.
9 (1986) 10 A.C.L.R. 395.
10 [1985] 1 N.Z.L.R. 242.
11 (1989) 15 A.C.L.R. 217, 222.
12 [1987] 1 All E.R. 114.
13 (1989) 15 A.C.L.R. 217, 221.
14 (1986) 43 S.A.S.R. 410; 11 A.C.L.R. 161.

construed strictly, and was directed against the improper purpose to *obtain* the gain, irrespective of whether any gain was actually made. Pidgeon J. concurred with his brethren.

RECENT DEVELOPMENTS

In *Hamilton v. Oades*,[15] the first ever order on behalf of creditors was made under s. 229(6)[16] of the Companies Act 1987 (Cth). The court there ordered the defendant, Oades to pay over $6,000,000 to the liquidators of two commodity trading companies of which he was a former director. The decision can therefore be seen as following up the lead provided in the *Jeffree* case. Directors now have solid grounds for fearing the loss of their personal assets when the company's assets are unable to meet creditors' claims.

CONCLUSION

The decision in this case makes good business sense, by striking a balance between the need for companies to pursue their necessarily risky business objectives and protection of creditors. Creditors will often be the providers of capital or stock-in-trade, both of which are essential to commercial viability, so this decision gives them added protection. It may however increase the burden on directors by widening the classes to which directors owe their duties.

A number of issues do however remain unresolved. In particular, this case provides that as a company moves towards insolvency, the greater the risk will be that certain transactions will prejudice creditors. How is a company to know when it is marginally insolvent, narrowing the scope for such transactions? This line will have to be drawn very carefully in the future. Furthermore, who is a 'prospective' creditor and what time limit will bring a creditor into this class?

There may well be some economic impact also, since directors may concentrate more heavily on preservation of share capital rather than profit generation. However, it seems unlikely that the current state of the law in this area would dramatically alter the behaviour of the nation's boardrooms.

Finally, whether directors should owe a duty to creditors *per se* is a matter of contention. Are creditors not already consequentially protected through the duties owed to shareholders? Perhaps a duty should extend only as far as 'quasi-creditors' such as convertible-note holders, or holders of redeemable preference shares. A duty owed to creditors may not accord with the bulk of company law principles (such as not being bound by the articles and memorandum of association).

APPENDIX: PROSPECTS FOR REFORM

The law reform commission in its 1987 August discussion paper[17] has recommended the imposition of a new civil liability attaching to the directors for failing to prevent the company engaging in insolvent trading. Insolvent trading would be defined to relate to obscure accounting records, balance sheet insolvency (*i.e.* where liabilities exceed assets) and 'continuing' insolvency (once a situation of insolvency is established, this continues until proven otherwise). Defences of reasonable belief of the ability to pay debts or non-participation in management due to supervening causes would be available and liability would only attach once a company was being wound up. Thus the liquidator could bring an action for an amount just with respect to creditors. In this situation, a court has a wide discretion.

MICHAEL L. EDELSTEIN* AND MARCO BINI**

15 (1989) 15 A.C.L.R. 123.

16 'Where —

(a) a person is convicted of an offence under this section; and

(b) the court is satisfied that the corporation has suffered loss or damage as a result of the act or omission that constituted the offence,

the court by which he is convicted may, in addition to imposing a penalty, order the convicted person to pay compensation to the corporation of such amount as that court specifies, and any such order may be enforced as if it were a judgment of that court.'

17 Commonwealth Law Reform Commission, Discussion Paper No. 32, August 1987.

* Student of Law at the University of Melbourne.

** B.Com. (Hons) (Melb.), Student of Law at the University of Melbourne.