Client Newsletter

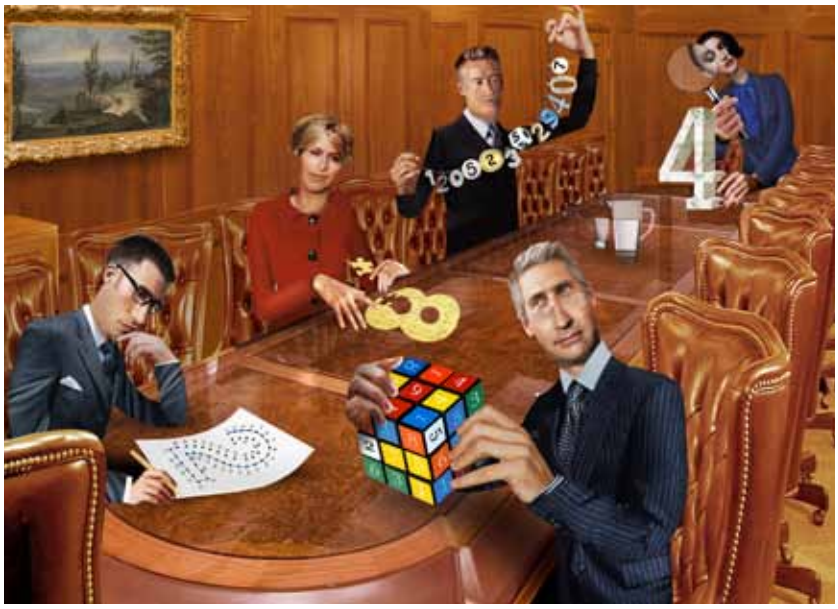
No. 4, 2011

In touch with the law

The law is constantly changing and this newsletter describes developments which may be relevant to you. If you are in any doubt about these or any other aspects of the law, please make an appointment to see your solicitor.

DIRECTORS' DUTIES

Approving financial statements a serious matter



A recent court decision against the directors of a major company demonstrates how demanding are a director's duties when approving financial statements.

To meet those demands, boards may seek to change the way in which financial information is presented to directors and how they review it. Information overload is not an excuse for failing to read, understand and focus on material provided to the board, especially material relating to the approval of financial statements.

The decision identifies limits on the extent to which directors can rely on management and external advisers. The law imposes a special responsibility on directors for approving financial statements. They cannot simply delegate that responsibility. Where directors know enough to spot a possible error in draft financial statements, they must question management and their external advisers.

It means that directors must have a degree of financial literacy. This knowledge should extend at least as far as basic accounting concepts and conventional accounting practices. However, the decision leaves unclear the question whether a director's knowledge should extend beyond this and, if so, how far.

The court ruled that current and former directors of Centro, a debt-laden shopping centre owner, had broken the law by approving incorrect financial accounts which classified more than $2 billion in short-term loans as long-term loans.

The company's former chief financial officer admitted to having broken the law but, in their defence, the directors said they had employed a major accounting firm to make sure the accounts were correct.

The judge decided that eight men had contravened the Corporations Act because they did not check that the accounts were correct.

"The directors are intelligent, experienced and conscientious people," he said. "There has been no suggestion that each director did not honestly carry out his responsibilities as a director ... However, I have found ... that the directors failed to take all reasonable steps required of them, and acted in the performance of their duties as directors without exercising the degree of care and diligence the law requires of them." ❑

PLANNING AHEAD

What is an enduring guardian?

An enduring guardian is someone you appoint, at a time when you have capacity, to make personal, health or lifestyle decisions on your behalf should you lose the capacity to make them for yourself.

When you appoint an enduring guardian you should choose which decision-making areas you want your enduring guardian to have. For example, you can authorise your enduring guardian to decide such things as where you may need to live or what medical treatment you should receive.

Your enduring guardian must act in your best interest and within guardianship laws. You cannot give your guardian a function that would involve them in an unlawful act, such as euthanasia. ❑

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PERSONAL INFORMATION

Lessons from recent privacy violations

News of data security breaches at major organisations that reveal thousands of individuals' personal information is not uncommon these days. Privacy impact assessments can be an important method of lowering the risk.

Inadequate security may be a breach of Australia's privacy laws, but the actions of customers and the media may create more havoc and opportunities for economic loss than government intervention, as recent cases involving Telstra, Vodafone and Google illustrate.

Many companies seem to consider the privacy laws have no teeth, but the commercial ramifications of media reports regarding breaches of customer privacy can be significant and do great damage to a company's reputation. For example, some reports suggested that Vodafone lost several hundred thousand customers as a result of its recent breach.

Prevention is always better than a disaster recovery cure. The ability to conduct a privacy impact assessment and establish a legal due diligence defence for the treatment of personal information may also uncover weaknesses in systems that can be remedied before any breaches occur.

The privacy laws regulate how businesses in Australia deal with personal information and they affect all organisations collecting it. Personal information is defined as being "information or an opinion about an individual whose identity is apparent or can reasonably be ascertained from the information or opinion".

For businesses that operate in the credit reporting, credit provision or health space, are additional rules apply. For other organisations, whose annual turnover is in excess of $3 million, the main application of the law is the requirement to comply with a set of national principles.

The Office of the Privacy Commissioner has a guide to privacy impact assessments on its website, and your solicitor can help you in ensuring your business is in compliance with the law and not exposed to prosecution. ❑

HANDLING A TAX DEBT

Identifying technical issues is key

Unless you are a taxpayer who is self-assessing and subject to pay-as-you-go instalments, the general rule is that tax has to be paid within 21 days of receiving a notice of assessment.

The tax office doesn't have to prove its assessments are correct. It is up to the taxpayer to prove one is wrong and they will have to pay at least part of any disputed tax before the authorities decide whether it needs to be paid or not.

The tax office set out the principles underlying its approach in guidelines earlier this year: "If a tax debtor does not pay by the due date and does not contact us, we assume they are not going to pay and take whatever action is necessary to recover the debt."

If a taxpayer believes a debt should not be paid or they can't pay it within 21 days, they should contact the tax office at once, and apply to pay by instalments if need be.

The fact that a taxpayer disputes a debt does not prevent the tax office from collecting the tax. The basic rule is that it will only agree to defer recovery action when it considers a genuine dispute exists and the taxpayer has arranged to pay half the disputed amount. However, it will not grant a deferral if it considers the revenue at risk, or the objection is frivolous or without merit.

Litigating the tax office can be a lengthy and emotionally costly business. As a key to settlement negotiation your solicitor will identify discrete technical issues and try to convince the tax office that it is not going to win them. The tax office doesn't approve of commercial settlements or 'horse trading', unless there is a benefit in doing so over and above the returns that would flow from taking bankruptcy or insolvency action.

> "As a key to settlement negotiation your solicitor will identify discrete technical issues."

With respect to a company, directors may avoid incurring tax debts by initiating its liquidation. As an alternative, a company might simply be deregistered. But this could be false economy. The law provides for reinstatement of a deregistered company where a person has been aggrieved by deregistration.

Further, unsuccessful deregistering or liquidation of a company might in the end cause it to be subject to extra tax penalties and even cause a director to be subject to prosecution. ❑

STRATA LAW

Court puts limit on insurer taking it to excess

The amount of the excess payable by an owners corporation when a claim is made on a home owner's warranty insurance policy in relation to common property building defects has now been determined by the courts in NSW.

A recent court case establishes that when a claim is made by the owners corporation on the home owners warranty insurance policy for a breach of the statutory warranty affecting the common property, only one excess is payable.

The case is important, particularly for those who live in residential units, because it means it is not necessary for lot proprietors to make individual claims under the insurance policy in order for the insurer's indemnity to be enforced. Similarly, it is not necessary for the owners corporation to claim indemnity on behalf of the individual lot proprietors.

> "Lot proprietors will not be required to pay an excess in respect of defects to common property."

Lot proprietors will now be able to breathe a sigh of relief as they will not be required to pay an excess in respect of defects to common property.

In the case, the insurer argued that the policy had been taken out on behalf of each of 201 lot proprietors and that the owners corporation had made a claim for indemnity on behalf of each of the lot proprietors. The excess payable, the insurer argued, was to be determined by multiplying the number of lots insured (201) by the $500 excess. It contended the excess payable was $100,500 – an amount that exceeded the owners corporation's claim.

The Court of Appeal's decision to strike down the insurer's argument removes the absurdity that would permit a claim by a lot proprietor for $700 for minor defects to a bathroom cupboard in a lot, while a claim in respect of a $100,000 defect in common property would not be met. ❑

OH&S

When is it safe to dismiss employees?

A string of recent unfair dismissal cases has seen employees reinstated to their former positions following dismissal for breaches of safety regulations and practices.

In recent occupational health and safety cases, the Fair Work Australia authority has considered various factors that lessen the severity of actions taken against employees.

To avoid costly court cases, employers considering disciplinary action would be well advised to think about the terms of the safety policy that has been breached and the consequences envisaged by the policy. Breaches should be assessed in light of any relevant subjective factors that might suggest a more moderate penalty.

As a guide, some of the factors that have been considered by Fair Work Australia are the personal and economic situation of the employee, including age, education, employment prospects, possible financial hardship and adverse impact on the employee's marriage.

Other factors that have been taken into account are the employee's unblemished record, practice by other staff, the length of time since training was last provided and the obligation to indicate whether additional training is required being placed on the employee rather than the employer.

Genuine remorse and contrition shown by the employee over past conduct and undertakings to improve in the future have also been considered. ❑

DISPUTED DEBT

Company not saved from insolvency

The courts have found a company can be wound up for insolvency even though its debt is in dispute.

In a recent case, a receiver and manager had been appointed by Westpoint over a company's assets, claiming a debt of over $6 million.

The Australian Security and Investments Commission applied to wind up the company alleging it was insolvent.

Company law states that the courts must presume a company is insolvent if, during or after three months after application, a receiver has been appointed under a legal agreement relating to securities.

The company had other debts of $1.7 million and assets of $5.7 million. It disputed the Westpoint debt, arguing that the debt owed was $5 million less than claimed, an argument the judge did not accept. He then wound up the company.

On appeal, the High Court found that the principle that the court would not order a winding-up on the basis of a disputed debt did not apply in the case brought by ASIC. It stated that "the principle was based upon the potential abuse, by creditors, of the winding up process to compel a solvent company to pay a genuinely disputed debt".

That could not apply to ASIC in this case, as it did not claim the status of creditor and did not seek winding up on the basis of a debt owed. ❑

ASTROTURFING

Misleading advertising on social media

Astroturfing refers to an orchestrated expression of support for a cause, product, service or policy designed to give the impression of a grassroots movement.

Under Australian law, if a business engages in this type of practice and misleads consumers, it breaches both the law and the advertising code of ethics.

There have been a few publicised instances of astroturfing in Australia, including the most recent revelation that opponents of plain cigarette packaging, the Alliance of Australian Retailers, was a front for Big Tobacco.

In 2004, Westfield paid $3.5m to Kirela to settle a law suit alleging the former had hired a PR company to set up the North Strathfield Residents' Action Group to oppose Kirela's development of a new retail centre in Strathfield, which would have competed with Westfield's Burwood centre.

Most of the cases have been in the political activism space, but now the rapid rise in the use of a variety of social media platforms by businesses to promote their brands and products online has created an environment ripe for the phenomenon of astroturfing.

What is designed to appear to be a genuine grassroots movement or groundswell of support is in fact a sophisticated and carefully targeted PR campaign. The term is derived from the brand of synthetic carpeting designed to look like real grass: AstroTurf.

While it is understandable that a business may be tempted to engage in astroturfing to fashion a groundswell of support for its products or services, it is worth remembering that such activity carries a double risk. Not only could it expose the company to legal action for misleading consumers – the other gamble is that once the artificial nature of the support movement has been revealed, the ruse will completely backfire and destroy any goodwill which has been created. ❑

CARBON PRICE GOUGING

Prevention is better than cure

The government has announced that the ACCC, the Australian Competition and Consumer Commission, will be given responsibility to police how businesses pass on the carbon price and for ensuring they do not engage in price gouging by using the carbon price as an excuse to increase prices beyond its actual effect.

The best way to avoid such unwanted attention from the national regulator is to make an early start on preparing for the implementation of the carbon price.

For example, businesses should be asking the following questions:

❑ Is my business going to absorb the impact of the carbon price or is it proposing to pass the cost on to customers?

❑ Has my business prepared estimates of the likely impact of the carbon price on its prices?

❑ How do these estimates compare to the estimates prepared by the goverment?

❑ Does my company wish to advise customers that price increases are due to the effect of the carbon price or does it wish to remain silent on this point?

❑ Will forward estimates of the likely impact of the carbon price on my prices stand up to ACCC scrutiny?

❑ Have all frontline staff been briefed on what to say if asked about the impact of the carbon price on prices?

While the simplest ways of avoiding unwanted attention is either to absorb the effect of the carbon price or to make no mention of it in relation to price rises, these approaches do not make good business sense. Businesses have a right to pass on the impact of the carbon price in the form of higher prices and should do so.

The most sensible approach is to take the time now to calculate the likely effect of the carbon price on the price of your goods and services and then advise customers in clear and unambiguous terms what that effect is. ❑

ROAD RULES

Heavy vehicle signage found to be outside the rules

The NSW Supreme Court has questioned the legality of heavy vehicle signage, which may render unsafe past convictions for contravention of these signs.

Heavy vehicles are compelled by signage to enter heavy vehicle checking stations for assessment of their suitability to carry loads.

In defending their prosecution for failing to comply, the lawyers for two truck drivers argued that signage in the terms "Heavy Vehicle Checking Station 300m. Vehicles over 8t GVM must enter" did not strictly comply with the Road Rules and was confusing.

The judge agreed. He noted the definitions of vehicle, motor vehicle and truck under the rules had the combined effect that all trucks are vehicles, but only some vehicles are trucks (the rules define trucks as a motor vehicle over 4.5t GVM). The judge also said that, by reason of those definitions, a sign requiring vehicles over 8t GVM to do something would necessarily include all trucks over 8t GVM but would not include all trucks. ❑