FEDERAL COURT OF AUSTRALIA

Australian Securities and Investments Commission v Healey [2011] FCA 717

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| Citation: | | Australian Securities and Investments Commission v Healey [2011] FCA 717 |
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| Parties: | | **AUSTRALIAN SECURITIES AND INVESTMENTS COMMISSION v BRIAN HEALEY, ANDREW THOMAS SCOTT, SAMUEL KAVOURAKIS, JAMES WILLIAM HALL, PAUL ASHLEY COOPER, PETER GRAHAM GOLDIE, LOUIS PETER WILKINSON and ROMANO GEORGE NENNA** |
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| File number: | |  |
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| Judge: | |  |
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| Date of judgment: | | 27 June 2011 |
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| Catchwords: | | **CORPORATIONS** – Directors and officers – Duties – Functions – Division of functions between Board and management – Non-executive directors – Duties of non-executive directors – Degree of skill required of non-executive directors – Extent to which directors entitled to rely on judgment and advice of management and experts – Duties of chief executive officer – Statutory duty of care and diligence – Standard of care – Duty to read and understand financial statements – Duty to apply background knowledge to review of financial statements  **NEGLIGENCE** – Directors – Failing to take reasonable steps to secure compliance by a company of its obligations in relation to accounting records – Nature of what is required – Relevance of belief that others discharging the obligation – Reliance on others – Whether reliance on internal and external processes discharges duties of directors – Negligence not mistake  **STATUTES** - Corporations Act 2001 (Cth) – ss 180, 344, 601FD, 294, 295A, 296, 297, 298, 299, 200A – Interplay between s 180 and s 344 of the Corporations Act 2001 (Cth)  **PRACTICE AND PROCEDURE** – Pleadings – Principles regarding unpleaded case – Whether parties can depart from pleaded case – No case to answer submission – Election – Procedure in Federal Court of Australia – Federal Court Rules – Order 35 Rule 1 – s 31A of the Federal Court of Australia Act 1976 (Cth)  **EVIDENCE** – Onus and standard of proof in civil penalty proceedings |
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| Legislation: | | *Companies Act 1896* (Vic)  *Companies Act 1929* (UK)  *Companies Act 1938* (Vic)  *Companies Act 1948* (UK)  *Companies Act 1958* (Vic)  *Companies Act 1961* (Vic)  *Companies Act 1981* (Cth)  *Companies Act 2006* (UK)  *Company Law Review Act 1998* (Cth)  *Corporations Act 1989* (Cth)  *Corporations Act 2001* (Cth)  *Evidence Act 1995* (Cth)  *Federal Court of Australia Act* 1976 (Cth)  *Financial Reporting Act 1993* (NZ) |
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| Cases cited: | | *Australian Competition and Consumer Commission v Leahy Petroleum Pty* [2009] FCA 1678  *Browne v Dunn* (1893) 6 R 67  *Commercial Union Assurance Co of Australasia Ltd v Ferrcom Pty Ltd* (1991) 22 NSWLR 389 (CA)  *Compaq Computer Australia Pty Ltd v Merry* (1998) 157 ALR 1  *Dyers v The Queen* (2002) 210 CLR 285  *Freeman v Health Insurance Commission* (1997) 78 FCR 91  *Hunter Resources Ltd v Melville* (1988) 164 CLR 234  *Jones v Peters* [1948] VLR 331  *Kennedy v Wallace* (2004) 142 FCR 185; (2004) FCAFC 337  *Prentice v Cummins (No 6)* (2003) 203 ALR 449; [2003] FCA 1002  *Project Blue Sky Inc v Australian Broadcasting Authority* (1998) 194 CLR 355  *Protean (Holdings) Ltd v American Home Assurance Co* [1985] VR 187  *Rasomen Pty Ltd v Shell Co of Australia* (1997) 75 FCR 216  *Ryan v Fisher* (1976) 51 ALJR 125  *Sampson v Richards* [1949] VLR 6  *Scalise v Bezzina* [2003] NSWCA 362  *Spencer v The Commonwealth* (2010) 241 CLR 118  *Swain v Hillman* [2001] 1 All ER 91  *Trade Practices Commission v George Weston Foods Ltd (No 2)* (1980) 43 FLR 55  *Trade Practices Commission v Nicholas Enterprises Pty Ltd* [1978] ATPR 40-097  *Tru Floor Service Pty Ltd v Jenkins (No 2)* (2006) 232 ALR 532  *Union Bank of Australia v Puddy* [1949] VLR 242  *White Industries (Qld) Pty Ltd v Flower & Hart (a firm)* (1998) 156 ALR 169  *William H Muller & Co v Ebbw Vale Steel, Iron & Coal Ltd* [1936] 2 All ER 1363 |
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| Date of hearing: | 4-7, 12-15, 18-20 April 2011, 2-5, 9-11, 16-18 May 2011 | |
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| Place: |  | |
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| Division: | General Division | |
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| Category: | Catchwords | |
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| IN THE FEDERAL COURT OF AUSTRALIA |  |
| DISTRICT REGISTRY |  |
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| BETWEEN: | AUSTRALIAN SECURITIES AND INVESTMENTS COMMISSION  Plaintiff |
| AND: | BRIAN HEALEY  First Defendant  ANDREW THOMAS SCOTT  Second Defendant  SAMUEL KAVOURAKIS  Third Defendant  JAMES WILLIAM HALL  Fourth Defendant  PAUL ASHLEY COOPER  Fifth Defendant  PETER GRAHAM GOLDIE  Sixth Defendant  LOUIS PETER WILKINSON  Seventh Defendant  ROMANO GEORGE NENNA  Eighth Defendant |

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| : |  |
| DATE: | 27 june 2011 |
| PLACE: |  |

**REASONS FOR JUDGMENT**

# INTRODUCTION

1. The Australian Securities and Investments Commission (‘ASIC’) has made application under ss 1317E, 1317G and 206C of the *Corporations Act 2001* (Cth) (‘the Act’) for declarations of contravention against the defendants in relation to ss 180(1), 601FD(3) and 344(1) of the Act and for orders that each of the defendants pay pecuniary penalties and be disqualified from managing corporations.
2. The conduct relied on by ASIC in support of the relief sought is contained in an amended statement of claim filed in the proceeding dated 26 November 2010 (‘the amended statement of claim’). The allegations in the amended statement of claim concern the approval of the consolidated financial statements of Centro Properties Limited (‘CPL’), Centro Property Trust (‘CPT’) and Centro Retail Trust (‘CRT’) for the financial year ending on 30 June 2007 at a board meeting attended by the defendant directors on 6 September 2007.
3. Other than Mr Nenna (the eighth defendant and Chief Financial Officer (‘CFO’)), the defendants were directors of each Centro company described below. Mr Healey (the first defendant) was the non-executive Chairman. Mr Scott (the second defendant) was the Chief Executive Officer (‘CEO’), and the other directors were non-executive directors.
4. Each of the directors contested the application. Mr Nenna made certain admissions in his Second Further Amended Defence dated 4 April 2011, although did not admit that the general information required by s 299A of the Act was required to be included in the directors’ report. Otherwise, Mr Nenna has admitted contraventions of s 180(1) and s 601FD(3) of the Act. Subject to a hearing as to whether Mr Nenna should be relieved from liability and as to penalty (if any), Senior Counsel for Mr Nenna sought and was excused from attending the further hearing of the proceeding on liability. Nevertheless, Mr Nenna was to be bound by the evidence put before me in the proceeding, and any findings and determination made that he contravened the Act.
5. ASIC has proved that the directors and each of them in the course of participating in the resolutions approving the accounts of CPL, CPT and CRT have contravened ss 180(1), 344(1) and 601FD(3) of the Act to the extent claimed in its amended application dated 26 November 2010.
6. ASIC has proved that Mr Nenna has contravened s 180(1) and 601FD(3) of the Act based upon his admissions and following upon the findings and determination of the Court in this proceeding.
7. I am yet to determine whether any defendant should be relieved from liability for such contraventions and the imposition of penalties (if any).
8. By way of briefest summary, I make the following comments regarding the directors. The directors are intelligent, experienced and conscientious people. There has been no suggestion that each director did not honestly carry out his responsibilities as a director. However, I have found, in the specific circumstances the subject of this proceeding, 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.
9. The 2007 annual reports of Centro Properties Group (‘CNP’) and Centro Retail Group (‘CER’) failed to disclose significant matters. In the case of CNP, the report failed to disclose some $1.5 billion of short-term liabilities by classifying them as non-current liabilities, and failed to disclose guarantees of short-term liabilities of an associated company of about US$1.75 billion that had been given after the balance date. In the case of CER, the 2007 annual reports failed to disclose some $500 million of short-term liabilities that had been classified as non-current.
10. This proceeding is not about a mere technical oversight. The information not disclosed was a matter of significance to the assessment of the risks facing CNP and CER. Giving that information to shareholders and, for a listed company, the market, is one of the fundamental purposes of the requirements of the Act that financial statements and reports must be prepared and published. The importance of the financial statements is one of the fundamental reasons why the directors are required to approve them and resolve that they give a true and fair view.
11. The significant matters not disclosed were well known to the directors, or if not well known to them, were matters that should have been well known to them.
12. In the light of the significance of the matters that they knew, they could not have, nor should they have, certified the truth and fairness of the financial statements, and published the annual reports in the absence of the disclosure of those significant matters. If they had understood and applied their minds to the financial statements and recognised the importance of their task, each director would have questioned each of the matters not disclosed. Each director, in reviewing financial statements, needed to enquire further into the matters revealed by those statements.
13. The central question in the proceeding has been whether directors of substantial publicly listed entities are required to apply their own minds to, and carry out a careful review of, the proposed financial statements and the proposed directors’ report, to determine that the information they contain is consistent with the director’s knowledge of the company’s affairs, and that they do not omit material matters known to them or material matters that should be known to them.
14. A director is an essential component of corporate governance. Each director is placed at the apex of the structure of direction and management of a company. The higher the office that is held by a person, the greater the responsibility that falls upon him or her. The role of a director is significant as their actions may have a profound effect on the community, and not just shareholders, employees and creditors.
15. This proceeding involves taking responsibility for documents effectively signed-off by, approved, or adopted by the directors. What is required is that such documents, before they are adopted by the directors, be read, understood and focussed upon by each director with the knowledge each director has or should have by virtue of his or her position as a director. I do not consider this requirement overburdens a director, or as argued before me, would cause the boardrooms of Australia to empty overnight. Directors are generally well remunerated and hold positions of prestige, and the office of director will continue to attract competent, diligence and intelligent people.
16. The case law indicates that there is a core, irreducible requirement of directors to be involved in the management of the company and to take all reasonable steps to be in a position to guide and monitor. There is a responsibility to read, understand and focus upon the contents of those reports which the law imposes a responsibility upon each director to approve or adopt.
17. All directors must carefully read and understand financial statements before they form the opinions which are to be expressed in the declaration required by s 295(4). Such a reading and understanding would require the director to consider whether the financial statements were consistent with his or her own knowledge of the company’s financial position. This accumulated knowledge arises from a number of responsibilities a director has in carrying out the role and function of a director. These include the following: a director should acquire at least a rudimentary understanding of the business of the corporation and become familiar with the fundamentals of the business in which the corporation is engaged; a director should keep informed about the activities of the corporation; whilst not required to have a detailed awareness of day-to-day activities, a director should monitor the corporate affairs and policies; a director should maintain familiarity with the financial status of the corporation by a regular review and understanding of financial statements; a director, whilst not an auditor, should still have a questioning mind.
18. A board should be established which enjoys the varied wisdom, experience and expertise of persons drawn from different commercial backgrounds. Even so, a director, whatever his or her background, has a duty greater than that of simply representing a particular field of experience or expertise. A director is not relieved of the duty to pay attention to the company’s affairs which might reasonably be expected to attract inquiry, even outside the area of the director’s expertise.
19. The words of Pollock J in the case of *Francis v United Jersey Bank* (1981) 432 A 2d 814, quoted with approval by Clarke and Sheller JJA in *Daniels v Anderson* (1995) 37 NSWLR 438, make it clear that more than a mere ‘going through the paces’ is required for directors. As Pollock J noted, a director is not an ornament, but an essential component of corporate governance.
20. Nothing I decide in this case should indicate that directors are required to have infinite knowledge or ability. Directors are entitled to delegate to others the preparation of books and accounts and the carrying on of the day-to-day affairs of the company. What each director is expected to do is to take a diligent and intelligent interest in the information available to him or her, to understand that information, and apply an enquiring mind to the responsibilities placed upon him or her. Such a responsibility arises in this proceeding in adopting and approving the financial statements. Because of their nature and importance, the directors must understand and focus upon the content of financial statements, and if necessary, make further enquiries if matters revealed in these financial statements call for such enquiries.
21. No less is required by the objective duty of skill, competence and diligence in the understanding of the financial statements that are to be disclosed to the public as adopted and approved by the directors.
22. No one suggests that a director should not personally read and consider the financial statements before that director approves or adopts such financial statements. A reading of the financial statements by the directors is not merely undertaken for the purposes of correcting typographical or grammatical errors or even immaterial errors of arithmetic. The reading of financial statements by a director is for a higher and more important purpose: to ensure, as far as possible and reasonable, that the information included therein is accurate. The scrutiny by the directors of the financial statements involves understanding their content. The director should then bring the information known or available to him or her in the normal discharge of the director’s responsibilities to the task of focussing upon the financial statements. These are the minimal steps a person in the position of any director would and should take before participating in the approval or adoption of the financial statements and their own directors’ reports.
23. The omissions in the financial statements the subject of this proceeding were matters that could have been seen as apparent without difficulty upon a focussing by each director, and upon a careful and diligent consideration of the financial statements. As I have said, the directors were intelligent and experienced men in the corporate world. Despite the efforts of the legal representatives for the directors in contending otherwise, the basic concepts and financial literacy required by the directors to be in a position to properly question the apparent errors in the financial statements were not complicated.
24. The main issues in this proceeding can be summarised as follows:
25. Whether CNP had current interest bearing liabilities of $2.611 billion and CER had current interest bearing liabilities of $598 million which were required to be classified as current liabilities.
26. Whether the entering into of certain guarantees were material events occurring after the balance date, matters or circumstances which significantly affected the state of affairs of CPT and its controlled entities in subsequent years within the meaning of s 299(1)(d) of the Act, and information that members of the CPL would reasonably require to make an informed assessment of the financial position of CPL or its business strategies and prospects for future years for the purposes of s 299A of the Act.
27. Whether the directors knew or ought to have known at the time of approving the 2007 accounts that:
    * + - 1. CNP and CER had very substantial liabilities in the order of $2.611 billion and $598 million respectively, which were due to be repaid or refinanced within 12 months from the balance date and in relation to which there was no unconditional right to defer payment for at least 12 months after the balance date; and
          2. since the balance date, guarantees had been given relating to loans totalling in excess of US$2.8 billion which might significantly affect the current state of affairs of CPL and its controlled entities in subsequent financial years.
28. Whether a reasonable director in the like position of the directors was required to have:
    * + - 1. “sufficient” knowledge of “conventional” accounting principles and practices, including that current liabilities generally mean financial obligations which must be “paid” or “satisfied” within 12 months of the balance date and that significant events which occur after that date must be disclosed in the financial report; and
          2. applied their minds and carried out a careful review of the 2007 accounts to determine whether they accurately reflected the financial position and performance of consolidated entities known to them.
29. Whether the directors received a declaration in accordance with s 295A(2) prior to approving the accounts, and the consequences of any failure to comply with s 295A.
30. Whether the directors failed to exercise their powers and discharge their duties with the requisite degree of care and diligence or failed to take all reasonable steps to secure compliance with the Act
31. Having made these brief remarks in summary, I first turn to outline the nature of the Centro entities so to understand the application in this proceeding, and to briefly set out the statutory requirements and the relevant financial statements.

# THE CENTRO ENTITIES

## Identification

1. At all times during the period from 1 October 2006 until 30 September 2007 each of the following bodies was a public company registered under the provisions of the Act:
   * + 1. CPL;
       2. CPT Manager Limited (‘CPTM’);
       3. Centro Retail Limited (‘CRL’); and
       4. Centro MCS Manager Limited (‘CMCSM’).
2. At all times during the relevant period:
   * + 1. CPT was a managed investment scheme registered under s 601EB of the Act;
       2. CPTM was:
          1. the responsible entity for CPT for the purposes of Part 5C.2 of the Act; and
          2. a wholly owned subsidiary of CPL;
       3. CPL and all the entities controlled by it and CPT and all the entities controlled by it were collectively known as CNP;
       4. each ordinary share in CPL was stapled to an ordinary unit in CPT (‘CNP stapled securities’);
       5. CNP stapled securities were listed for quotation on the Australian Securities Exchange (‘ASX’); and
       6. for statutory reporting purposes, specifically the requirements of Urgent Issues Group Interpretation 1013 “Consolidated Financial Reports in relation to Pre-Date-of-Transition Stapling Arrangements” (‘UIG 1013’) and Australian Accounting Standard 3 (‘AASB 3’), CPL was deemed to be the parent entity of CNP.
3. At all times during the relevant period:
   * + 1. CRT was a managed investment scheme registered under s 601EB of the Act;
       2. CMCSM was:
          1. the responsible entity for CRT for the purposes of Part 5C.2 of the Act; and
          2. a wholly owned subsidiary of CPL;
       3. CRL and all the entities controlled by it and CRT and all the entities controlled by it were collectively known as the CER;
       4. each ordinary share in CRL was stapled to an ordinary unit in CRT (‘CER stapled securities’);
       5. CER stapled securities were listed for quotation on the ASX; and
       6. for statutory reporting purposes, specifically the requirements of Australian Accounting Standards Board Interpretation 1002 “Post-Date-of-Transition Stapling Arrangements” (AASB Interpretation 1002) and AASB 3, CRT was deemed to be the parent entity of CER.
4. Before 1 October 2004:
   * + 1. CPL was called Prime Property Management Limited; and
       2. another company subsequently called Centro (CPL) Limited (‘Old CPL’) was called Centro Properties Limited.

## Corporate Governance in the Centro Group

1. During the relevant period, there was in force for CNP a written Board Charter (‘Board Charter’).
2. The Board Charter provided that the responsibilities and functions of the Board of CPL (referred to therein as ‘the Company’) included the following:
   * + 1. reviewing and approving corporate strategies, budgets, annual business plans and Group policies;
       2. monitoring the Company’s financial position and business results (including the audit process) to understand at all times the health of the Company;
       3. ensuring regulatory compliance and maintaining adequate risk management processes; and
       4. ensuring a high level of transparency reporting to security holders and compliance with the highest ethical standards.
3. It was the policy and practice of the directors that the corporate governance policies and procedures of CNP applied to CER.
4. During the relevant period:
   * + 1. there was a committee of the directors of CPTM called the Board Audit and Risk Management Committee (‘BARMC’);
       2. the members of the BARMC were Mr Kavourakis, Mr Hall and Mr Cooper;
       3. there was in force a written charter for the BARMC (‘BARMC Charter’); and
       4. the functions of the BARMC as defined in the BARMC Charter applied to CPL, CPT, CMCSM and all other entities in CNP.
5. The BARMC Charter provided that:
   * + 1. the objectives of the BARMC included assisting the board in discharging its responsibilities with respect to the financial statements, financial report and annual report;
       2. the key responsibilities and functions of the BARMC included the following:
          1. to oversee the preparation of financial statements and reports; and
          2. oversight of financial controls and systems;
       3. one of the specific functions of the BARMC was to review and report to the board that financial information provided to investors and the board was accurate and reliable; and
       4. the normal procedures for the committee’s audit responsibility included:
          1. determining the reliability and integrity of accounting policies and financial reporting and disclosure practices; and
          2. monitoring compliance with applicable accounting standards and other requirements relating to the preparation and presentation of financial results.
6. At all times during the relevant period the auditor of each Centro company and CPT and CRT was PricewaterhouseCoopers (‘PwC’).

# OVERVIEW OF FINANCIAL REPORTING REQUIREMENTS OF THE ACT

1. By s 292 of the Act, each Centro company, CPT and CRT were required to prepare a financial report and a directors report for the financial year ending on 30 June 2007.
2. By s 295 of the Act, the financial report of each Centro company, CPT and CRT was required to include a declaration by the directors under s 295(4) of the Act:
   * + 1. whether, in the directors’ opinion, there are reasonable grounds to believe that the company, registered scheme or disclosing entity will be able to pay its debts as and when they become due and payable; and
       2. whether, in the directors’ opinion, the financial statement and notes are in accordance with this Act, including:
          1. section 296 (compliance with accounting standards); and
          2. section 297 (true and fair view); and
       3. save for CPTM and CMCSM, that the directors have been given the declarations required by s 295A,

and that declaration was required to be made in accordance with a resolution of the directors, state the date on which the declaration is made and be signed by a director.

1. By s 295A of the Act, the directors’ declaration included in the financial reports of CPL, CPT, CRL and CRT under s 295(4) of the Act was required to be made only after each person who performed:
   * + 1. a chief executive function; and
       2. a chief financial officer function

in relation to CPL, CPT, CRL and CRT (as the case may be) had given to the directors a declaration under s 295A(2) of the Act.

1. Mr Scott and Mr Nenna were the persons who performed the CEO and the CFO function respectively during the relevant period in relation to CPL, CPT, CRL and CRT.
2. By s 296(1) of the Act, the financial report of each of the Centro companies, CPT and CRT for the financial year ending on 30 June 2007 was required to comply with the accounting standards made by the Australian Accounting Standards Board (‘AASB’) pursuant to s 334 of the Act.
3. AASB 101 “Presentation of Financial Statements”, as amended (‘AASB 101’) was an accounting standard made by the AASB pursuant to s 334 of the Act and in force during the whole of the relevant period.
4. At all times during the relevant period, AASB 101 provided that an entity was required to classify a liability as current in its financial reports when:
   * + 1. it expected to settle the liability in its normal operating cycle;
       2. it held the liability primarily for the purposes of trading;
       3. the liability was due to be settled within twelve months after the end of the reporting period; or
       4. the entity did not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting period,

and provided that all other liabilities were required to be classified as non-current.

1. AASB 110 “Events after the Reporting Period” (‘AASB 110’) was an accounting standard made by the AASB pursuant to s 334 of the Act and in force during the whole of the relevant period.
2. At all times during the relevant period, AASB 110 provided in paragraph 21 that:

*If non-adjusting events after the reporting date are material, non-disclosure could influence the economic decisions that users make on the basis of the financial statements. Accordingly, an entity shall disclose the following for each material category of non-adjusting event after the reporting period:*

*(a) the nature of the event; and*

*(b) an estimate of its financial effect, or a statement that such an estimate cannot be made.*

1. By s 297 of the Act, the financial statements and notes forming part of the financial report of each Centro company, CPT and CRT for the financial year ending on 30 June 2007, were required to give a true and fair view of the financial position and performance of the respective company and scheme and, in the case of CNP and CER, of each consolidated entity to which they related.
2. By the operation of s 298 and s 299 of the Act:
   * + 1. each Centro company, CPT and CRT was required to prepare a directors’ report for the financial year ending on 30 June 2007 which included the information required by, amongst other provisions, s 299(1)(d);
       2. the information required by s 299(1)(d) was:

*… details of any matter or circumstance that has arisen since the end of the year that has significantly affected, or may significantly affect:*

*(i) the entity’s operations in future financial years; or*

*(ii) the results of those operations in future financial years; or*

*(iii) the entity’s state of affairs in future financial years…*

1. By the operation of s 298 and s 299A of the Act:
   * + 1. the directors’ report of CPL for the financial year ending 30 June 2007 was required to include the information required by subs 299A(1);
       2. the information required by subs 299A(1) was:

*… information that members of the listed entity would reasonably require to make an informed assessment of:*

*(a) the operations of the entity reported on; and*

*(b) the financial position of the entity reported on; and*

*(c) the business strategies, and prospects for future financial years, of the entity reported on.*

1. By s 314 of the Act:
   * + 1. each of CPL and CPT was required to report to its members for the financial year ending on 30 June 2007 by providing either the financial report for the year together with the other reports mentioned in s 314(1)(a) or a concise report for the year that complied with subsection 314(2);
       2. a concise report for the financial year would comply with subs 314(2) if it consisted of a concise financial report drawn up in accordance with accounting standards made for the purposes of subs 314(2)(a) together with the other reports and documents described in subs 314(2)(b) to 314(2)(c).
2. AASB 1039 “Concise Financial Reports” (‘AASB 1039’) was an accounting standard made by the AASB pursuant to s 334 of the Act and in force during the whole of the relevant period.
3. At all times during the relevant period, AASB 1039 provided that a concise financial report must disclose the information required by paragraph 21 of AASB 110 in respect of each event occurring after the reporting date that does not relate to conditions existing at the reporting date.

# 2007 ANNUAL ACCOUNTS OF CPL AND CPT

1. At a joint meeting of the boards of directors of CPL and CPTM held on 6 September 2007 attended by the directors and each of them, the directors unanimously:
   * + 1. resolved to approve the consolidated financial statements of CPL and its controlled entities for the year ending on 30 June 2007 (‘CPL 2007 Accounts’) and the consolidated financial statements of CPT and its controlled entities for the year ended 30 June 2007 (‘CPT 2007 Accounts’);
       2. with respect to the CPL 2007 Accounts and the CPT 2007 Accounts, resolved that declarations be made in writing by the directors that:
          1. the financial statements complied with Accounting Standards, the Corporations Regulations 2001 and other mandatory professional reporting requirements;
          2. the financial statements gave a true and fair view of the financial position of CPL and CPT (as the case may be) as at 30 June 2007;
       3. resolved that in the opinion of the directors:
          1. with respect to the CPL 2007 Accounts and the CPT 2007 Accounts, the financial statements and notes were in accordance with the Act and the company’s Constitution; and
          2. there were reasonable grounds to believe that CPL and CPT would be able to pay their debts as and when they became due and payable; and
       4. with respect to the CPL 2007 Accounts and the CPT 2007 Accounts, resolved that the Directors’ Reports and Directors’ Statements and the Responsible Entity’s Reports and Declarations be approved, that the reports, statements and declarations be signed by any two directors and that the reports so signed be annexed to the financial statements.
2. On or about 6 September 2007, Mr Healey and Mr Scott, acting as directors of CPL signed the directors’ declaration for the purposes of s 295(1)(c) of the Act to be included in the CPL 2007 Accounts, which was in the following terms:

*In the directors’ opinion:*

*(a) the financial statements and notes set out at pages 53 to 112 and remuneration disclosures on pages 37 to 50 are in accordance with the Corporations Act 2001, including:*

*(i) complying with Accounting Standards, the Corporations Regulations 2001 and other mandatory professional reporting requirements; and*

*(ii) giving a true and fair view of the company’s and consolidated entity’s financial position as at 30 June 2007 and of its performance as represented by the results of their operations, changes in equity and their cash flows, for the financial year ended on that date; and*

*(b) there are reasonable grounds to believe that the Group will be able to pay its debts as an [sic] when they become due and payable; and*

*(c) the audited remuneration disclosures set out on pages 37 to 50 of the directors’ report comply with Accounting Standards AASB 124 Related Party Disclosures and the Corporations Regulations 2001.*

*The directors have been given the declaration by the chief executive officer and the chief financial officer required by section 295A of the Corporations Act 2001.*

*In the opinion of the Directors of Centro Properties Limited the financial statements and notes are in accordance with the Constitution dated 31 July 1989.*

*This declaration is made in accordance with a resolution of the directors.*

1. It is in dispute whether Mr Scott and Mr Nenna did at any time give to the directors a declaration under s 295A of the Act in relation to the financial records and the financial statements of CPL.
2. The CPL 2007 Accounts:
   * + 1. stated in note 1 that:

*The principal accounting policies adopted in the preparation of the financial report are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.*

1. stated in note 1(b) that the financial report had been prepared in accordance with Australian Accounting Standards and the Act;
2. further stated in note 1(w) that its principal accounting policies included the following:

*Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.*

1. at least in the accounts lodged with ASIC, stated in note 18 and in the balance sheet that:
   * + - 1. the total of interest bearing liabilities for CPL and its controlled entities which were classified as current interest bearing liabilities as at 30 June 2007 was $1,096,936,000; and
         2. the total of interest bearing liabilities for CPL and its controlled entities which were classified as non-current interest bearing liabilities as at 30 June 2007 was $2,506,815,000.
2. It seems accepted, but in any event apparent on the evidence that, as at 30 June 2007, CPL and its controlled entities had interest bearing liabilities totalling $2,611,033,581 which:
   * + 1. were required by AASB 101; and
       2. ought under the accounting policy stated in note 1(w),

to have been classified and shown in the balance sheet as current interest bearing liabilities but were classified and shown as non-current interest bearing liabilities.

1. The CPL 2007 Accounts:
   * + 1. stated the following in note 28:

*CONTINGENT LIABILITIES*

*Bank guarantees of $5 million each (2006: $5 million) have been arranged by the Group in the name of CPT Manager Limited, Centro MCS Manager Limited and Centro Funds Management Limited to guarantee obligations under Australian Financial Services Licence and responsible entity requirements (2006: CPT Manager Limited and Centro MCS Manager Limited). CPT Manager Limited has other contingent liabilities of $2.6 million in the form of bank guarantees to the Road Traffic Authority (“RTA”);*

* + - 1. stated the following in note 35:

*EVENTS OCCURRING AFTER REPORTING DATE*

***Proposed Merger of Centro Shopping America Trust and Centro Retail Trust***

*On 27 August 2007, Centro Retail Trust (“CER”) announced its proposal to merge with Centro Shopping America Trust (“CSF”). Under the proposed merger, Centro agreed to contribute approximately $2.2 billion of Australasian and US property assets in return for an investment in the merged entity. This merger proposal is subject to investor approval in October 2007, at which time the assets would be transferred from Centro. The transfer is expected to have a minimal impact on Centro’s earnings and balance sheet position.*

1. Between 30 June 2007 and 6 September 2007, CPL and CPTM as responsible entity of CPT gave the following guarantees:
   * + 1. Amended and Restated Guaranty Agreement (Non-Recourse Carveouts) executed as of 1 August 2007 in favour of JPMorgan Chase Bank NA;
       2. Guaranty Agreement (Payment) executed as of 1 August 2007 in favour of JPMorgan Chase Bank NA;
       3. Guaranty Agreement (JPMCB) executed as of 5 August 2007 in favour of JPMorgan Chase Bank NA;
       4. Amended and Restated Guaranty Agreement executed as of 31 July 2007 in favour of Bank of America, NA.
2. On 6 September 2007, Mr Healey and Mr Scott signed the directors’ report for CPL for the year ended 30 June 2007 (‘CPL 2007 Directors’ Report’).
3. The CPL 2007 Directors’ Report stated at page 49 that:

*There has not arisen in the interval between 30 June 2007 and the date hereof any matter or circumstance that has significantly affected or may significantly affect:*

*(i) the Group’s operations in future financial years; or*

*(ii) the results of those operations in future financial years; or*

*(iii) the Group’s state of affairs in future financial years;*

*except as otherwise referred to in the financial statements or in this Directors’ report.*

1. On 6 September 2007, Mr Healey and Mr Scott, acting as directors of CPTM signed the declaration for the purposes of s 295(1)(c) of the Act to be included in the CPT 2007 Accounts, which was in the following terms:

*In the directors’ opinion:*

*(a) the financial statements and notes set out at pages 53 to 104 and remuneration disclosures on pages 36 to 50 are in accordance with the Corporations Act 2001, including:*

*(i) complying with Accounting Standards, the Corporations Regulations 2001 and other mandatory professional reporting requirements; and*

*(ii) giving a true and fair view of the Trust’s and consolidated entity’s financial position as at 30 June 2007 and of its performance as represented by the results of their operations, changes in equity and their cash flows, for the financial year ended on that date; and*

*(b) there are reasonable grounds to believe that the Trust will be able to pay its debts as an when they become due and payable; and*

*(c) the audited remuneration disclosures set out on pages 36 to 50 of the directors’ report comply with Accounting Standards AASB 124 Related Party Disclosures and Class Order 06/50 issued by the Australian Securities and Investments Commission.*

*The directors have been given the declaration by the chief executive officer and the chief financial officer required by section 295A of the Corporations Act 2001.*

*In the opinion of the Directors of CPT Manager Limited the financial statements and notes are in accordance with the Constitution dated 31 July 1989*

*This declaration is made in accordance with a resolution of the directors.*

1. It is again in dispute whether Mr Scott and Mr Nenna did at any time give to the directors a declaration under s 295A of the Act.
2. The CPT 2007 Accounts:
   * + 1. stated in note 1 that:

*The principal accounting policies adopted in the preparation of the financial report are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.*

* + - 1. stated in note 1(b) that the financial report had been prepared in accordance with Australian Accounting Standards and the Act*;*
      2. further stated in note 1(t) that one of the principal accounting policies adopted in the preparation of the financial report was that:

*Borrowings are classified as current liabilities unless the Trust has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.*

* + - 1. At least in the accounts lodged with ASIC, stated in note 16 and in the balance sheet that:
         1. the total of interest bearing liabilities for CPT and its controlled entities which were classified as current interest bearing liabilities as at 30 June 2007 was $1,096,936,000;
         2. the total of interest bearing liabilities for CPT and its controlled entities which were classified as non-current interest bearing liabilities as at 30 June 2007 was $2,506,750,000.

1. It seems accepted, but in any event apparent on the evidence that, as at 30 June 2007, CPT and its controlled entities had interest bearing liabilities totalling $2,611,033,581 which:
   * + 1. were required by AASB 101; and
       2. ought under the accounting policy stated in note 1(t),

to have been classified and shown in the balance sheet as current interest bearing liabilities but were classified and shown as non-current interest bearing liabilities.

1. The CPT 2007 Accounts:
   * + 1. stated the following in note 24:

*CONTINGENT LIABILITIES*

*The Trust has no contingent liabilities; and*

* + - 1. stated the following in note 31:

*EVENTS OCCURRING AFTER REPORTING DATE*

***Proposed Merger of Centro Shopping America Trust and Centro Retail Trust***

*On 27 August 2007, Centro Retail Trust (“CER”) announced its proposal to merge with Centro Shopping America Trust (“CSF”). Under the proposed merger, Centro agreed to sell approximately $2.2 billion of Australasian and US property assets in return for units in the newly merged entity. This merger proposal is subject to investor approval in October 2007, at which time the assets would be transferred from Centro. The transfer is expected to have a minimal impact on Centro’s earnings and balance sheet position.*

1. Between 30 June 2007 and 6 September 2007, CPTM as responsible entity of CPT gave the following guarantees:
   * + 1. Amended and Restated Guaranty Agreement (Non-Recourse Carveouts) executed as of 1 August 2007 in favour of JPMorgan Chase Bank NA;
       2. Guaranty Agreement (Payment) executed as of 1 August 2007 in favour of JPMorgan Chase Bank NA;
       3. Guaranty Agreement (JPMCB) executed as of 5 August 2007 in favour of JPMorgan Chase Bank NA;
       4. Amended and Restated Guaranty Agreement executed as of 31 July 2007 in favour of Bank of America, NA.
2. On 6 September 2007, Mr Healey and Mr Scott signed the directors’ report for CPT for the year ended 30 June 2007 (‘CPT 2007 Directors’ Report’).
3. The CPT 2007 Directors’ Report stated at page 76 that:

*There has not arisen in the interval between 30 June 2007 and the date hereof any matter or circumstance that has significantly affected or may significantly affect:*

*(i) the Trust’s operations in future financial years; or*

*(ii) the results of those operations in future financial years; or*

*(iii) the Trust’s state of affairs in future financial years;*

*except as otherwise referred to in the financial statements or in this Directors’ report.*

# 2007 ANNUAL ACCOUNTS OF CRT

1. At a meeting of the board of directors of CMCSM held on 6 September 2007 attended by the directors and each of them, the directors unanimously:
   * + 1. resolved to approve the consolidated financial statements of CRT and its controlled entities for the year ended 30 June 2007 (‘CRT 2007 Accounts’);
       2. with respect to the CRT 2007 Accounts, resolved that declarations be made in writing by the directors that:
          1. the financial statements complied with Accounting Standards, the Corporations Regulations 2001 and other mandatory professional reporting requirements;
          2. the financial statements gave a true and fair view of the financial position of CRT as at 30 June 2007;
       3. resolved that in the opinion of the directors:
          1. with respect to the CRT 2007 Accounts, the financial statements and notes were in accordance with the Act and the Constitution;
          2. there were reasonable grounds to believe that CRT would be able to pay its debts as and when they became due and payable;
       4. with respect to the CRT 2007 Accounts, that the Directors’ Reports and Directors’ Statements and the Responsible Entity’s Reports and Declarations be approved, that the reports statements and declarations be signed by any two Directors and that the reports so signed be annexed to the financial statements.
2. On 6 September 2007, Mr Healey and Mr Scott, acting as directors of CMCSM signed the declaration for the purposes of s 295(1)(c) of the Act to be included in the CRT 2007 Accounts, which was in the following terms:

*In the Directors’ opinion:*

*(a) the financial statements and notes set out at pages 36 to 74 and remuneration disclosures on page [sic] are in accordance with the Corporations Act 2001, including:*

*(i) complying with Accounting Standards, the Corporations Regulations 2001 and other mandatory professional reporting requirements; and*

*(ii) giving a true and fair view of the company’s and the consolidated entity’s financial position as at 30 June 2007 and of its performance, as represented by the results of their operations, changes in equity and their cash flows, for the financial period ended on that date; and*

*(b) there are reasonable grounds to believe that the Group will be able to pay its debts as an when they become due and payable; and*

*The directors have been given the declaration by the chief executive officer and the chief financial officer required by section 295A of the Corporations Act 2001.*

*In the opinion of the Directors of Centro MCS Manager Limited the financial statements and notes are in accordance with the Constitution dated 31 July 1989*

*This declaration is made in accordance with a resolution of the directors.*

1. It is again in dispute whether Mr Scott and Mr Nenna did at any time give to the directors a declaration under s 295A of the Act.
2. The CRT 2007 Accounts:
   * + 1. stated in note 1 that:

*The principal accounting policies adopted in the preparation of the financial report are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.*

* + - 1. stated in note 1(b) that the financial report had been prepared in accordance with Australian Accounting Standards and the Corporations Act;
      2. further stated in note 1(s) that one of the principal accounting policies adopted in the preparation of the financial report was that:

*Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.*

* + - 1. at least in the Accounts lodged with ASIC, stated in note 15 and in the balance sheet that:
         1. the total of interest bearing liabilities for CRT and its controlled entities which were classified as current interest bearing liabilities as at 30 June 2007 was $nil;
         2. the total of interest bearing liabilities for CRT and its controlled entities which were classified as non-current interest bearing liabilities as at 30 June 2007 was $1,443,797,000.

1. It seems to be accepted, but in any event apparent on the evidence that, as at 30 June 2007, CRT and its controlled entities had interest bearing liabilities totalling $598,292,097 which:
   * + 1. were required by AASB 101; and
       2. ought under the accounting policy stated in note 1(s),

*to have been classified and shown in the balance sheet as current interest bearing liabilities but were classified and shown as non-current interest bearing liabilities.*

# THE RELEVANT SECTIONS OF THE ACCOUNT ON CLASSIFICATION

1. It is worth observing that the relevant sections of the financial statements (as reported) relating to the classification of liabilities for the year ending on 30 June 2007 are relatively succinct. I accept that these sections appear in a larger context, but they contain important information which could and should be carefully understood by each director.
2. Relevant sections of the statement of financial position of the relevant entities (as reported) are:

|  |  |  |
| --- | --- | --- |
|  |  | **30 Jun 07**  **$000** |
| **CPL and its controlled entities** |  |  |
| **Current liabilities** |  |  |
| Payables |  | 263,341 |
| Interest bearing liabilities |  | 1,096,936 |
| Derivative financial instruments |  | 215,746 |
| Provisions |  | 177,476 |
| **Total current liabilities** |  | 1,753,499 |
|  |  |  |
| **Non-current liabilities** |  |  |
| Payables |  | 54,228 |
| Interest bearing liabilities |  | 2,506,815 |
| Non-interest bearing liabilities |  | 283,724 |
| Provisions |  | 1,667 |
| **Total non-current liabilities** |  | 2,846,434 |
|  |  |  |
| **CPT and its controlled entities** |  |  |
| **Current liabilities** |  |  |
| Payables |  | 48,849 |
| Interest bearing liabilities |  | 1,096,936 |
| Derivative financial instruments |  | 215,746 |
| Provisions |  | 173,249 |
| **Total current liabilities** |  | 1,534,780 |
|  |  |  |
| **Non-current liabilities** |  |  |
| Payables |  | 54,228 |
| Interest bearing liabilities |  | 2,506,750 |
| Non-interest bearing liabilities |  | 149 |
| **Total non-current liabilities** |  | 2,561,127 |
|  |  |  |
| **CRT and its controlled entities** |  |  |
| **Current liabilities** |  |  |
| Trade and other payables |  | 14,097 |
| Provisions |  | 72,564 |
| **Total current liabilities** |  | 86,661 |
|  |  |  |
| **Non-current liabilities** |  |  |
| Interest bearing liabilities |  | 1,443,797 |
| Deferred tax liabilities |  | 17,799 |
| **Total non-current liabilities** |  | 1,461,596 |
|  |  |  |

# SUBSEQUENT EVENTS

1. I make mention of the following events which occurred after September 2007.
2. CNP released its 2007 Annual Report containing the concise version of the CPL 2007 Accounts to the ASX on or about 18 September 2007.
3. CER released its 2007 Annual Report containing the concise version of the CRT 2007 Accounts to the ASX on or about 18 September 2007.
4. The CPL 2007 Accounts, CPT 2007 Accounts and the CRT 2007 Accounts were lodged with ASIC, pursuant to subs 319(1) of the Act, on 28 September 2007.
5. At the close of trading on the ASX on 12 December 2007:
   * + 1. the closing price of a CNP stapled security was $5.70;
       2. the closing price of a CER stapled security was $1.42.
6. On 13 December 2007:
   * + 1. each of CNP and CER requested the ASX to halt trading in their respective stapled securities for two business days until 17 December 2007;
       2. the ASX halted trading in the stapled securities of both CNP and CER until the commencement of trading on 17 December 2007.
7. On 17 December 2007:
   * + 1. CNP announced to the ASX that:
          1. it was revising its projected earnings downwards by approximately 13%;
          2. it was continuing to negotiate refinancing of $1.3 billion worth of debt;
          3. it had obtained an extension until 15 February 2008 of all facilities maturing prior to that date;
          4. it would not pay a distribution for the half year ended 31 December 2007.
       2. after the announcement referred to in paragraph (a), trading in CNP stapled securities resumed and on that day:
          1. trading began at a price of $2.30 per stapled security;
          2. the closing price of CNP stapled securities was $1.36.
8. On 17 December 2007:
   * + 1. CER announced to the ASX that:
          1. it was revising its projected earnings downwards by approximately 5%;
          2. it was continuing to negotiate refinancing of $1.2 billion worth of debt;
          3. it had obtained an extension until 15 February 2008 of all facilities maturing prior to that date;
          4. it would not pay a distribution for the half year ended 31 December 2007, at least until long term refinancing was finalised.
       2. after the announcement referred to in paragraph (a) trading in CER stapled securities resumed and on that day:
          1. trading began at a price of $1.00 per stapled security;
          2. the closing price of the CER stapled securities was $0.85.
9. By letter dated 19 December 2007 to Ms Hourigan Company Secretary, ASX requested CNP, amongst other things, to explain the apparent differences in the classification of, and amounts disclosed as, current and non-current debt obligations in the Group’s Appendix 4E, Annual Report and the recent announcement.
10. By letter dated 20 December 2007 to ASX, Ms Hourigan stated on behalf of CNP, in response to the request, that:
    * + 1. in the appendix 4E the full value of interest bearing liabilities were classified as non-current;
        2. as a result of the identification by management and the auditors of $1,097 million of interest bearing liabilities that should be classified as current, such liabilities were so classified in the financial statements;
        3. at all times since 6 September 2007 the correct classification of current liabilities was available to the market.
11. On 15 January 2008, CNP announced to the ASX that:
    * + 1. it had initiated a review of the classification of its current and non-current debt in the CPL 2007 Accounts;
        2. it considered that there was a prospect that the proportion of current interest bearing liabilities might have been higher than previously reported.
12. On 15 January 2008, CER announced to the ASX that:
    * + 1. it had initiated a review of the classification of its current and non-current debt in the CRT 2007 Accounts;
        2. as at January 2008 the debt maturing in 12 months or less had increased from $0.7 billion to $1.3 billion compared with the position disclosed in December 2008.
13. On 15 February 2008, CNP announced to the ASX that it expected A$1,514,097,090 of interest bearing liabilities which were classified as non-current in the CPL 2007 Accounts to be re-classified as current in addition to the A$1,096,936,000 classified as current in those accounts.
14. On 15 February 2008, CER announced to the ASX that it expected $598,292,097 of the interest bearing liabilities which were classified as non-current in the CRT 2007 Accounts to be re-classified from non-current to current.
15. On 29 February 2008 CNP informed ASX that:
    * + 1. it had restated its prior period comparatives to take into account a change in the presentation of $1,514,097,090 of interest bearing liabilities which were previously presented as non-current in the balance sheet as at 30 June 2007 under AASB 101 Presentation of Financial Statements;
        2. the reason for the reclassification was that the original classification did not accord with the requirements of AASB 101;
        3. as a result of the restatement, the amount (rounded to thousands) of interest bearing liabilities as at 30 June 2007 classified as current liabilities had increased from $1,096,936,000 to $2,611,033,000;
        4. CNP had contingent liabilities as at 31 December 2007 in respect of:
           1. a guarantee of US$1,753 million in respect of Centro Super LLC debt;
           2. a guarantee of US$350 million in respect of Centro Super LLC revolving debt.
16. On 28 February 2008 CER informed ASX that:
    * + 1. it had restated its prior period comparatives to take into account a change in the presentation of $598.3 million of interest bearing liabilities which were previously presented as non-current in the balance sheet as at 30 June 2007 under AASB 101 Presentation of Financial Statements;
        2. the reason for the reclassification was that the original classification did not accord with the requirements of AASB 101;
        3. as a result of the restatement, the amount (rounded to thousands) of interest bearing liabilities as at 30 June 2007 classified as current liabilities had increased from zero to $598,292,000.
17. Various proceedings in the Federal Court of Australia have been commenced against various Centro entities arising out of the omissions and errors alleged in this proceeding.

# THE DIRECTORS

1. I should say something further about some of the directors.
2. The Chairman of the BARMC was Mr Kavourakis. Mr Kavourakis had been appointed as a Director of Centro in November 2003. He had been for a period of eight years the Managing Director of National Mutual Funds Management and during the relevant period was or had been a director of several other listed companies. In a letter dated 24 October 2003 in which he offered Mr Kavourakis an appointment as non-executive director, Mr Healey said “your principal role and responsibilities as a non-executive director of the group is to act in the best interest of the security holders of both Centro and Prime. The role includes approval of the Groups strategy and assisting and overseeing management to execute this strategy. In particular your position on the Board is seen to include your background in the areas of investment and funds management both in general and with specific application to property”.
3. Mr Hall was appointed to the Boards of Centro in September 2005. Mr Hall holds tertiary qualifications in commerce and during the relevant period was a Fellow of CPA Australia and a member of the Institute of Company Directors. He had been Vice President of Group Accounting and Controller at BHP Billiton and a director and CFO of Orica Ltd.
4. In a letter dated 5 August 2005 in which he was invited to join the Boards of Centro, his principal role and responsibilities were identified in similar terms to those of Mr Kavourakis, but it was said, that “in particular, your position on the Board is seen to include your strong accounting and financial management background and experience across the full range of financial activities in which a substantial public company is involved”.
5. Mr Cooper was appointed to the Boards of Centro in October 2006. He had been a practising solicitor and a partner in a major law firm in Melbourne. From 1995 up to and including the relevant time he had been a Director of AXA Asia Pacific Holdings Ltd and a member of the Audit and Compliance Committee of that Board. In a letter dated 31 August 2006, in which he was invited to join the Boards of Centro, his role was described in similar terms to that of Mr Kavourakis and Mr Hall and it was said that “in particular, your position on the Board is seen to include your significant experience in investment banking and corporate advisory work at senior levels and your strong understanding of current and emerging corporate governance requirements and trends”.
6. The Chairman and non-executive directors were well remunerated. The remuneration of the Chairman Mr Healey was a fee of $376,050 pa. Other non-executive directors were entitled to a fee of $115,000 pa. Mr Kavourakis as Chairman of the BARMC was entitled to an additional fee of $16,000 pa and Mr Cooper and Mr Hall as members of that committee were entitled to an additional fee of $8,000 pa.
7. Mr Andrew Scott joined Centro in March 1997, after 15 years with Coles Myer Ltd in various senior property finance and strategy positions. His employment was governed by an Executive Service Agreement which renewed on or about 1 March 2005. Mr Scott was bound to carry out his duties faithfully and diligently with the degree of competence and efficiency appropriate for a person serving the group in the position of Managing Director and CEO. In the year ended 30 June 2007 his total remuneration and benefits were over $3.5 million.

# PRINCIPLES OF LAW

1. Before attempting to summarise the evidence, and to focus attention upon the important aspects of this proceeding, I set out some principles of law I consider are appropriate to apply.

## Application of the *Briginshaw* standard

1. The evidence and issues in this case must be considered by application of what is known as the *Briginshaw* standard. The allegations are serious and, if substantiated, may be taken to have very serious consequences for the personal and professional reputations of the defendants.
2. In *Australian Securities and Investments Commission v Macdonald* *(No 11)* (2009) 71 ACSR 368, (2009) 230 FLR 1, Gzell J recognised that the seriousness of the allegations and the potential consequences of civil penalty proceedings demanded the application of the *Briginshaw* standard. His Honour explained (at [182]-[186]) that:

*Section 140 of the Evidence Act 1995 prescribes the standard of proof in civil proceedings as the balance of probabilities and provides that the court may take into account in deciding whether it is so satisfied, the nature of the cause of action or defence, the nature of the subject matter of the proceedings and the gravity of the matters alleged.*

*This provision reflects Dixon J’s discussion of the quality of persuasion required for this purpose in* Briginshaw v Briginshaw *(1938) 60 CLR 336 at 361–2; [1938] ALR 334 at 342 (Briginshaw). In that case, the High Court held that, on a petition for divorce on the ground of adultery, the standard of proof was not that of proof beyond reasonable doubt.*

*Dixon J said that when the law requires the proof of any fact, the tribunal must feel an actual persuasion of its occurrence or existence before it can be found. In civil matters, the affirmative of an allegation is made out to the reasonable satisfaction of the tribunal:*

The truth is that, when the law requires the proof of any fact, the tribunal must feel an actual persuasion of its occurrence or existence before it can be found. It cannot be found as a result of a mere mechanical comparison of probabilities independently of any belief in its reality. No doubt an opinion that a state of facts exists may be held according to indefinite gradations of certainty; and this has led to attempts to define exactly the certainty required by the law for various purposes. Fortunately, however, at common law no third standard of persuasion was definitely developed. Except upon criminal issues to be proved by the prosecution, it is enough that the affirmative of an allegation is made out to the reasonable satisfaction of the tribunal. But reasonable satisfaction is not a state of mind that is attained or established independently of the nature and consequence of the fact or facts to be proved. The seriousness of an allegation made, the inherent unlikelihood of an occurrence of a given description, or the gravity of the consequences flowing from a particular finding are considerations which must affect the answer to the question whether the issue has been proved to the reasonable satisfaction of the tribunal. In such matters “reasonable satisfaction” should not be produced by inexact proofs, indefinite testimony, or indirect inferences. Everyone must feel that, when, for instance, the issue is on which of two dates an admitted occurrence took place, a satisfactory conclusion may be reached on materials of a kind that would not satisfy any sound and prudent judgment if the question was whether some act had been done involving grave moral delinquency.

*To similar effect is the statement of the majority of the High Court in* Neat Holdings Pty Ltd v Karajan Holdings Pty Ltd *(1992) 110 ALR 449 at 449–50.*

*These are civil penalty proceedings where a pecuniary penalty of up to $200,000 and an order disqualifying the individual defendants from managing corporations for such period as the court considers appropriate, are sought. The seriousness of the nature of the cause of action and the gravity of the matters alleged must be taken into account in deciding whether facts have been proved on the balance of probabilities:* Adler v ASIC *(2003) 179 FLR 1; 46 ACSR 504; [2003] NSWCA 131 at [146]–[148]* (Adler NSWCA)*. This means that, ordinarily, the more serious the consequences of what is contested in litigation, the more a court will have regard to the strength and weakness of evidence before it in coming to a conclusion:* CEPU v ASIC *(2007) 162 FCR 466; 242 ALR 643; [2007] FCAFC 132 at [30]* (CEPU)*. That means that if inferences are to be drawn, ASIC has to establish that the circumstances appearing in the evidence give rise to a reasonable and definite inference and not merely to conflicting inferences of equal degrees of probability:* CEPU *at [38].*

1. Similarly, in the Court of Appeal decision of *Morley v Australian Securities and Investments Commission* (2010) 274 ALR 205; [2010] NSWCA 331; (Spigelman CJ, Beazley and Giles JJA) proceeded upon the basis that the *Briginshaw* standard applied. Their Honours confirmed that that standard finds its modern expression in the terms of s 140 of the *Evidence Act 1995* (Cth) (‘the Evidence Act’) and that the *Briginshaw* standard is routinely applied in civil penalty proceedings.
2. In this proceeding, it is also important to remember that where an applicant’s case rests on inferences from primary facts, it is not enough for the circumstances to give rise to conflicting inferences of equal degrees of probability. The principle was stated by the High Court in *Bradshaw v McEwans Pty Ltd* (1951) 217 ALR 1 and has been adopted repeatedly since (at 5):

*Of course as far as logical consistency goes many hypotheses may be put which the evidence does not exclude positively. But this is a civil and not a criminal case. We are concerned with probabilities, not with possibilities. The difference between the criminal standard of proof in its application to circumstantial evidence and the civil is that in the former the facts must be such as to exclude reasonable hypotheses consistent with innocence while the latter you need only circumstances raising a more probable inference in favour of what is alleged. In questions of this sort where direct proof is not available it is enough if the circumstances appearing in evidence give rise to a reasonable and definite inference: they must do more than give rise to conflicting inferences of equal degrees of probability so that the choice between them is mere matter of conjecture… But if circumstances are proved in which it is reasonable to find a balance of probabilities in favour of the conclusion sought then though the conclusion may fall short of certainty, it is not to be regarded as a mere conjecture or surmise.*

See *Luxton v Vines* (1952) 85 CLR 352, at 358, per Dixon, Fullagar and Kitto JJ; *Nominal Defendant v Owens* (1978) 22 ALR 128 (FC), at 132-133, per Muirhead J (with whom St John J agreed); *Transport Industries Insurance Co Ltd v Longmuir* [1997] 1 VR 125 (CA), at 141, per Tadgell JA, and cases cited there; and *Australian Competition and Consumer Commission v Amcor Printing Papers Group Ltd* (2000) 169 ALR 344; [2000] FCA 17.

## Financial Reporting

1. This proceeding is about financial reporting and the role and responsibilities of directors in relation to that task.
2. It is useful to briefly describe the special treatment given to financial statements over a period of time. A statutory obligation to produce and have audited a financial statement was imposed on the directors of a company in Victoria by s 23 of the *Companies Act 1896* (Vic). That section required a balance sheet complying with some basic requirements to be prepared, audited, sent to the shareholders and kept posted up “in a conspicuous place in the registered office of the company and every branch office where the business of the company is carried on.” The balance sheet sent to shareholders had to be accompanied by a certificate signed by one or more directors on behalf of the board stating that in his or her or their opinion the balance sheet is “drawn up so as to exhibit a correct view of the state of the company’s affairs”.
3. Significant amendments to those requirements were contained in the *Companies Act 1938* (Vic), s 123, derived from the *Companies Act 1929* (UK). They were expanded to include a separate profit and loss account and a report by the directors as to the state of the company’s affairs. The certificate was to be signed by two directors on behalf of the Board and was required to state their opinion that the balance sheet and profit and loss accounts were “drawn up so as to exhibit a true and correct view of the state of the company’s affairs and the results of the business, respectively”.
4. In the *Companies Act 1958* (Vic) the language “true and correct” was altered to “true and fair” and in addition to being certified as such in a statement of the opinion of the directors, the balance sheet and profit and loss account were required in fact to show a true and fair view. A schedule of the requirements for the content of the statements, which had grown considerably since 1896, was included in the legislation.
5. This statutory scheme continued through the company law statutes of Victoria until 1980, although with many additions and modifications accruing over the years. Some, which are relevant in this proceeding, are:
   * + 1. the requirements for the content of the balance sheet were modified in 1961 to include a requirement that current and non-current liabilities (using a payable within 12 month test for the distinction) be shown separately:
       2. a requirement was added in 1964 that the directors’ report state “with appropriate details” whether or not any contingent liability had been undertaken by the company since the date of the previous report;
       3. from 1971, the directors statement had to be made in accordance with a resolution of the directors. The requirements for the content of the directors’ report were also expanded and rewritten at this time. They then required the directors to state:

● whether there exists at the date of the report any contingent liability that had arisen since the end of the financial year and if so the general nature thereof;

● whether there had arisen since the end of the financial year and before the date of the report any item, transaction or event of a material and unusual nature.

1. In the *Companies Act 1981* (Cth), the statutory scheme was retained, but there was a considerable expansion in its coverage. In particular, the directors’ statement was also then required to state that in the opinion of the directors the company was able to pay its debts as and when they fell due. By amending legislation in 1983, the obligation to prepare accounts in accordance with approved accounting standards was introduced.
2. In addition, in forming an opinion as to whether the profit and loss account and balance sheet showed a true and fair view, directors were required to have regard to:

*(i) circumstances that have arisen; and (ii) information that has become available, since the end of the financial year to which the accounts relate, being circumstances or information that would, if those accounts had been made out when the statement is made, have affected the determination of an amount or particular in those accounts.*

1. There were no substantial alterations to the statutory scheme in the *Corporations Act 1989* (Cth) until the passing of the *Company Law Review Act 1998* (Cth), when, the provisions now forming Part 2M.3 (relevantly for present purposes) were enacted.
2. Key elements of the above developments were correctly summarised by ASIC as follows:
   * + 1. the publication of financial statements certified by the directors to be correct, or true and correct, or true and fair, has been part of company law for at least 115 years;
       2. there has been a statutory obligation, by means of a legislated schedule or accounting standards, to distinguish between current and non-current liabilities for the past 50 years; and
       3. post balance date events (especially contingent liabilities such as guarantees) have been required to be dealt with in directors’ reports since the mid-1960s.
3. As ASIC noted, all of the developments above long preceded the business careers of the defendants.
4. There has also been development in the common law.
5. In *Metal Manufacturers Ltd v Lewis* (1986) 11 ACLR 122 Hodgson J observed that a director seeking to perform the duties in what was then s 269 and s 270 of the *Companies Act 1981* (Cth) (in particular the making of the directors’ statement) would have made observations and drawn conclusions from the balance sheet. In the NSW Court of Appeal, where the decision was upheld, Kirby P spoke of a “statutory scheme” encompassing s 229 (duty to act with care and diligence) and the reporting provisions in ss 269 and 270 which require the directors to address their minds to the affairs of the company, and requires a higher level of attention than was the case in the past.
6. In *Statewide Tobacco Services Ltd v Morley* (1990) 2 ACSR 405, another case about insolvent trading, Ormiston J pointed to the then ss 269 and 270 and said (at 406) that the presence of those provisions meant that “a director is obliged to inform himself or herself as to the financial affairs of the company to the extent necessary to form each year the opinion required for the director’s statement.” Later, his Honour said (at 431):

*In the light of the various duties now imposed upon the directors, it would not appear unreasonable that they should apply their minds to the overall position of the company.*

*… Directors are entitled to delegate to others the preparation of books and accounts and the carrying on of the day-to-day affairs of the company. What each director is expected to do is to take a diligent and intelligent interest in the information either available to him or which he might with fairness demand from the executives or other employees and agents of the company.* (own emphasis)

1. In *Commonwealth Bank of Australia v Friedrich and Ors* (1991) 5 ACSR 115. Justice Tadgell expressed his agreement with what had been said in *Statewide Tobacco Services Ltd v Morley* and added this (at 126):

*As the complexity of commerce has gradually intensified (for better or for worse) the community has of necessity come to expect more than formerly from directors whose task it is to govern the affairs of companies to which large sums of money are committed by way of equity capital or loan. In response, the parliaments and the courts have found it necessary in legislation and litigation to refer to the demands made on directors in more exacting terms than formerly; and the standard of capability required of them has correspondingly increased. In particular, the stage has been reached when a director is expected to be capable of understanding his company’s affairs to the extent of actually reaching a reasonably informed opinion of its financial capacity. Moreover, he is under a statutory obligation to express such an opinion annually. I think it follows that he is required by law to be capable of keeping abreast of the company’s affairs…* (own emphasis)

1. Later in dealing with the facts of the case, Tadgell J performed some analysis of the information contained in the 1987 accounts of the relevant company (the National Safety Council of Victoria) and stated a number of propositions about what could be derived from an examination of them. The propositions included observations about the ratio of current assets to current liabilities, increases in debtors and work in progress, and the relationship of those items with a reported increase in turnover. These, he said, would have been found without difficulty upon a consideration of those accounts by a “director seeking to do his duty”. He went on to say (at 185):

*These figures, and the calculations I have indicated, are not complicated. They could, I think, be fairly easily appreciated by any adult person of normal intelligence who had a general knowledge of the company’s activities and an inclination to consider the accounts and the auditor’s report for half an hour. A non-executive director of a company whose figures they were should, in my judgment, have been able to derive from the documents at least the simple propositions I have set out. The company was not an elementary organisation operating in a back yard, but one with a stated annual turnover of $60m, having stated liabilities of at least $131m and the use of very substantial resources and some hundreds of employees: its affairs demanded an appreciable degree of diligent application by its directors if they were to attempt to do their duty. The deserved degree of application should have enabled an appreciation by a director of its 1987 accounts and the audit report thereon at least to the extent I have indicated.* (own emphasis)

1. In *AWA Ltd v Daniels* (1992) 7 ACSR 759, at 864, Rogers CJ Comm Div said:

*A director is obliged to obtain at least a general understanding of the business of the company and the effect that a changing economy may have on that business. Directors should bring an informed and independent judgment to bear on the various matters that come to the Board for decision.* (own emphasis)

1. The New South Wales Court of Appeal in *Daniels v Anderson* considered the matter further. In the course of the relevant part of the judgment of Clarke and Sheller JJA, their Honours said that “the modern cases to which we have referred, set in the context of a legislative pattern of imposing greater responsibility upon directors, demonstrate that the director’s duty of care is not merely subjective, limited by the director’s knowledge and experience or ignorance and inaction.” They went on to endorse observations made in the New Jersey decision of *Francis v United Jersey Bank* (1981) 432 A 2d 814 which included the following:

*Because directors are bound to exercise ordinary care, they cannot set up as a defence lack of the knowledge needed to exercise the requisite degree of care.*

*…*

*While directors are not required to audit corporate books, they should maintain familiarity with the financial status of the corporation by a regular review of the financial statements.*

*… The review of financial statements, however, may give rise to a duty to inquire further into matters revealed by those statements.* (own emphasis)

1. In *Deputy Commissioner of Taxation v Clark* [2003] NSWCA 91 Spigelman CJ (with whom the other members of the New South Wales Court of Appeal agreed) reviewed the authorities, including those mentioned above, and said (at [108]–[109]) that:

*What constitutes breach of the standards of care and of diligence, in a particular case, will depend on a wide variety of circumstances including the precise nature of the business conducted by the company and the composition of its board. However, the case law indicates that there is a core, irreducible requirement of involvement in the management of the company.*

*Although the standard of skill may vary in accordance with the particular skills of the director, the core, irreducible requirement of skill involves an objective test, such as “ordinary competence” (*3M Australia Pty Ltd v Kemish *(at 373) per Foster J) or “reasonable ability” (*Rema Industries & Services Pty Ltd v Coad *(1992) 7 ACSR 251 at 259, per Lockhart J). An equivalent objective test applies to the core, irreducible requirement of diligence, such as “reasonable steps to place themselves in a position to guide and monitor the management of the company”, per Rogers J in* AWA Ltd v Daniels *(at 864), adopted by Clarke JA and Sheller JA on appeal in* Daniels v Anderson *(at 501).* (own emphasis)

1. Justice Austin later stated in *ASIC v Vines* (2003) 48 ACSR 291 at [30] that *Daniels v Anderson* “established an objective duty, broadly in the region of competence, arising out of the director’s duty of diligence. It is therefore a duty capable of being encompassed by the statutory standard of care and diligence.” His Honour later went on to note that the authorities established that the statutory duty was enhanced where the directorial appointment is based on a special skill, and that there was a standard of skill for executive officers who were appointed to positions requiring skill, and that standard was encompassed in the statutory formulation of care and diligence.
2. More recently, in *ASIC v Rich* [2009] NSWSC 1229 Austin J again reviewed the authorities and reiterated what he said in *Vines*, and further that the Court of Appeal did not dissent from that view in the appeal in that case. His Honour accepted ASIC’s submission that the statutory standard encompasses an objective duty of skill or competence in the reading and understanding of financial material, although he thought that for non-executive directors the objective duty of minimum skill and competence may not extend much beyond that.
3. In my view, the objective duty of competence requires that the directors have the ability to read and understand the financial statements, including the understanding that financial statements classify assets and liabilities as current and non-current, and what those concepts mean. This classification is relevant to the assessment of solvency and liquidity. Equally, a director should have an understanding of the need to disclose certain events post balance sheet date. It would not be possible for a director to form the opinion required by s 295(4)(d) without such an understanding. It is not suggested that a director could vote in favour of a resolution in support of the required directors’ statements when he did not hold the opinions referred to at all.
4. The Act explicitly requires that the declaration required by s 295(4) and the annual directors’ report must be made in accordance with a resolution of the directors. In that manner the Act imposes ultimate responsibility for those matters upon the directors in a way that they cannot delegate. They must themselves determine to adopt the required resolution.
5. As is apparent from the above discussion of the legislation history, prior to the commencement of the *Company Law Review Act 1998* (Cth), the corporations legislation imposed the primary obligation with respect to financial reporting on the directors rather than on the company. Directors were required to cause financial statements to be made, laid before the annual general meeting (in the case of a public company) and lodged with the relevant authority. As a result of the 1998 legislation, the obligation to prepare a financial report and a directors’ report was placed on the entity.
6. The director’s obligation, under s 344 is to take all reasonable steps to comply, or secure compliance, with Pt 2M.3 (which deals with financial reports, directors’ reports, audit, reporting to members and lodgement with ASIC). They are under the same duty with respect to the financial records which the entity must keep under Pt 2M.2. If they fail to take all reasonable steps to comply or secure compliance, they contravene the Act.
7. Whilst the Act now requires that the annual directors’ report be prepared by the entity, rather than by the directors themselves, the report must be made in accordance with a resolution of the directors and must be signed by a director. Whilst the obligation to “prepare” it is placed on the entity, the directors have an important responsibility for the contents of the report. Additionally, the financial report which a company must prepare must contain a declaration by the directors that the financial statements comply with the accounting standards and give a true and fair view, and must contain the directors’ opinion as to whether there are reasonable grounds to believe that the entity will be unable to pay its debts as and when they become due and payable and as to whether the financial statements are in accordance with the law: s 295(4). Whilst, again, the obligation to “prepare” the directors’ declaration is placed on the entity, the directors have a primary responsibility for the declaration. In essence, the Act requires directors to take particular responsibility for the company’s financial reports.
8. This is not to say that directors are not entitled to seek assistance in carrying out their responsibilities, and may rely on others.
9. For instance, directors are entitled to rely upon declarations by the CEO and the chief financial officer, such as made pursuant to s 295A of the Act. Section 295A says that in the case of a listed entity, the directors’ declaration for a full financial year must be made only after each person who performs a chief executive function or a chief financial officer function has given the directors a declaration. The declaration must say whether, in the opinion of the person giving it:

* The financial records of the entity have been properly maintained in accordance with s 286;
* The financial statements and notes comply with the accounting standards;
* The financial statements and notes give a true and fair view; and
* Any other matters prescribed by the regulations are satisfied (none have yet been prescribed): s 295A(2).

1. However, even here the extent of reliance should not be taken too far. The purpose of the introduction of s 295A was according to the Explanatory Memorandum to the Bill introducing the requirement to “ensure that those who are responsible for the preparation of financial statements are accountable for their content thereby heightening the accountability of senior management”: Explanatory Memorandum, paragraph 4.330. Section 295A was not to detract from the responsibilities otherwise imposed upon directors.
2. It is apparent that the legislative scheme imposes overall responsibility for the financial report and the directors’ report upon the directors. When the Bill for the legislation that introduced s 295A was introduced, the Explanatory Memorandum also stated that:

*... having executive sign off to the board of directors is the preferred option. This approach will retain the overall responsibility of directors for the financial statements but will at the same time impose a specific requirement on those responsible for preparing the statements to turn their minds to the actual legal requirements and compliance with the accounting standards.*

1. There may be liability under s 344 and the civil penalty provisions for a director who has not taken all reasonable steps to ensure compliance with the declaration requirements of s 295A, whether the director was responsible for making that declaration or was merely one of the board who failed to ensure that the declaration was obtained.
2. The obligation that a director may have to make a declaration, arising out of his or her performance of a chief executive function or a chief financial officer function is in addition to the responsibility that the director has under s 344 to take all reasonable steps to ensure compliance with the financial records and financial reporting requirements: s 295A(8).
3. It is necessary to say something more about s 344. Section 344 provides for contravention of directors for failing to take “all reasonable steps to comply with, or to secure compliance with” Part 2M.2 or Part 2M.3 of the Act. There are two limbs.
4. Section 344 is contained in Chapter 2M of the Act entitled “Financial reports and audit”. Chapter 2M is divided into the following parts: Part 2M.2 relates to the obligations of companies to keep financial records; Part 2M.3 relates to the obligations of companies to prepare financial reports and director’s reports and to have those reports audited and to obtain an auditor’s report; Part 2M.4 covers the appointment and removal of auditors; Part 2M.5 provides for the making of accounting and auditing standards; Part 2M.6 provides for some exceptions and modifications; and Part 2M.7 contains s 344.
5. Section 344 is entitled “Contravention of Part 2M.2 and 2M.3”. Part 2M.3 of the Act is relevantly entitled “Financial reporting”. It is divided into the following divisions: Division 1 relates to the obligations of companies to prepare annual financial reports and directors’ reports (ss 292-301); Division 2 relates to the obligations of companies to prepare half year financial reports and directors’ reports (ss 302-306); Division 3 relates to the requirement to have the financial reports audited and to obtain an auditor’s report (ss 307-310); Division 4 provides for the publication of the financial reports, directors’ report and auditor’s to the members (ss 311-318); Division 5 provides for the lodgement of annual reports to ASIC (ss 319-322); Division 6 contains some special provisions relating to consolidated financial statements (ss 232-232C); Division 7 sets the financial years and half years (s 323D); Division 8 relates specifically to disclosure by listed companies of information filed overseas (s 323DA); and Division 9 relates to the Financial Reporting Panel (ss 323EA-323EM).
6. Divisions 1 and 2 of Part 2M.3 contain details and specific requirements relating to financial reporting obligations by companies in Australia, including: which companies have to prepare financial reports and directors’ reports (s 292); the contents of financial reports (s 295); the making of a declaration by a listed company’s CEO and CFO in relation to the company’s financial records and reports (s 295A); compliance with accounting standards (s 296); the requirement that the financial statements and notes give a true and fair view of the company’s’ financial position and performance (s 297) and the contents of director’s reports (ss 298-300A).
7. Part 2M.3 provides a regime of checks and balances to ensure the integrity of annual financial statements. Directors are responsible for compliance with Part 2M.2 and Part 2M.3, and to the extent that much of those Parts do not refer specifically to directors themselves performing acts, it is understood, by the words of s 344 – in the second limb – that they will not have to perform all the acts contained in those parts themselves. Indeed, there is very little that those Parts require directors to do directly themselves. However, s 295(4) speaks directly to directors requiring them to form an opinion. The regime of checks and balances incorporates reliance upon management in the context of the directors’ opinion to the extent that they may not opine until they receive the s 259A declarations from the CFO and CEO.
8. In this proceeding, the steps that the respective entities had to take to comply with these requirements can be simply stated:
   * + 1. the entities should have correctly classified their interest bearing liabilities as either current or non-current before stating them in the financial statements;
       2. the guarantees should have been identified as:
          1. material post balance date events to be included in the relevant note to the financial statements;
          2. circumstances
9. arising after the balance date which may significantly affect the operations, results or financial position of CNP in future financial years; and
10. about which the members of CPL would reasonably require information to make an informed assessment of the position and prospects of CPL.
11. The important circumstance of this proceeding, which is critical in determining what it was that is actually required of a director under s 344, is that the directors were part of the mechanism and procedures by which Centro attempted to comply with the financial reporting requirements.
12. It is not envisaged by the Act that directors can simply put the discharge of those functions in the hands of apparently competent and reliable persons, for directors are a part of the process themselves by undertaking the task of approving and adopting the financial statements and reports.
13. Insolvency cases have considered specifically what was meant by the words “reasonable steps to comply with”. Although in another context the considerations raised in those cases are instructive. From those cases, the standard of “all reasonable steps” is determined objectively by reference to the particular circumstances of the case. However, the standard requires, at a minimum, that directors take a diligent and intelligent interest in the information either available to them or which they might appropriately demand from the executives or other employees and agents of the company: see *Australian Securities Commission v Fairlie* (1993) 11 ACLC 669 at 14-15; and *Morley v Statewide Tobacco Services Ltd No 1* (1993) 1 VR 423, at 448-9.
14. Determination of contravention of the financial reporting provisions requires consideration of formulations contained in the two principal provisions:
    * + 1. “take all reasonable steps to comply with, or to secure compliance with, Part 2M.2 or 2M.3” as provided in s 344; and
        2. “whether, in the directors’ opinion, the financial statement and notes are in accordance with this Act” including compliance with the accounting standards and true and fair view, as provided in s 294(4)(d).
15. The provisions of the Act should be construed in a manner that considers the words used within a particular provision, in the context of the purpose of the particular regime – which underpins the discrete parts of the Act, and, in the context of the Act as a whole.
16. In the case of s 295(4), the directors themselves must form an opinion. They must form an opinion with all due care and diligence. At a minimum, the directors must inform themselves as to the financial affairs company to the extent necessary to form each year the opinion required.
17. In *Morley v Statewide Tobacco Services*, Ormiston J considered certain duties under the Act, including a provision that required directors to attach a statement to the accounts expressing an opinion as to solvency. At 429:

*More significantly, the directors of a company are now obliged to attach a statement each year to the accounts required to be laid before its annual general meeting expressing the opinion, among other matters, that there are reasonable grounds to believe that the company will be able to pay its debts as and when they fall due: s269(9)(a)(iii). The requirement now contained in subpara(iii) was added at the time of the passing of the 1981 Companies Act (Cth) and so, with the altered provisions contained in s556, has formed part of the legislative scheme since the Code came into effect. Moreover, not only is it an offence deliberately to make such a statement which is false but under the Code it is now also an offence to furnish, or to authorise or permit the furnishing of, a materially false or misleading statement to members without having taken reasonable steps to ensure that the statement ... was not false or misleading: s564(2) (see also s563(3)); and cf s375 and s375A of the Uniform Companies Acts.*

*It is thus apparent without considering the effects of s556, that a director is obliged to inform himself or herself as to the financial affairs of the company to the extent necessary to form each year the opinion required for the directors’ statements. Although that is only an annual obligation, it presupposes sufficient knowledge and understanding of the company’s affairs and its financial records to permit the opinion of solvency to be formed. See also per Hodgson J in Metal Manufacturers Ltd v Lewis (1986) 4 ACLC 739, at 750.* (own emphasis)

1. In *Commonwealth Bank of Australia v Friedrich* (1991) 5 ACSR 115, Tadgell J again considered s 556 of the Companies Code and infused certain objective criteria taken from other general duties at 125:

*My formulation does refer to a person seeking properly to perform the duties of a director of the company, and that criterion is to be understood and applied against the background of the whole of the Code and the principles of common law and equity which govern a director's duties and their discharge. Of course, it may be said in a general way that the law requires a director only to act reasonably and to attain to standards of no more than ordinary competence and to behave with only average prudence, but it is in my opinion unwarrantable and unhelpful to limit the interpretation of s 556(1) by these concepts alone. Section 556 is to be taken to have been drafted on the assumption that a director would comply with the requirements of the law with respect to directors, and especially the requirements imposed upon directors by the Code of which the section is part. What constitutes the proper performance of the duties of a director of a particular company will be dictated by a host of circumstances, including no doubt the type of company, the size and nature of its enterprise, the provisions of its articles of association, the composition of its board and the distribution of work between the board and other officers:* Byrne v Baker *[1964] VR 443 at 450. To speak of a director of ordinary, reasonable or average competence or prudence, or indeed of an ordinary reasonable or average director, is to give no very useful description, whereas a person seeking properly to perform the duties of a director of a particular company can be identified by reference to more specific criteria of which ordinariness, reasonableness and averageness are, or may be, merely ingredients.* (own emphasis)

1. As I have indicated, as a result of the 1998 amendments, the obligation to prepare a financial report and a directors’ report was placed on the entity, and the obligations of the directors became, under s 344, to take all reasonable steps to comply with or to secure compliance with Parts 2M.2 and 2M.3 of the Act. Whether the 1998 amendments have raised or lowered the compliance standard for directors, I need not determine. Of course, any assessment of ‘reasonable steps’ must be made in the circumstances as they were at the time, rather than with the benefit of hindsight.
2. Determination of the steps that reasonably ought to have been taken to secure compliance for the purposes of s 344 requires the making of a number of inquiries. It is first necessary to ascertain what needs to be done to secure compliance with the relevant provision. It is then necessary to ascertain what steps reasonably ought to have been taken by the directors to secure such compliance. The test is an objective test by reference to the particular circumstances of the case. What it is reasonable to expect from a director by way of achieving that object will depend on all of the circumstances.

## Section 344 – Feltex Decision

1. The directors relied upon the recent decision of the District Court of Auckland in *Ministry of Economic Development v Feeney & Ors* (District Court of New Zealand, Auckland CRI-2008-044-29199, 2 August 2010) (the ‘Feltex decision’), which concerned analogous provisions to s 344. Justice Doogue considered the standard required of non-executive directors in connection with securing compliance with the accounting standards. The defendants in that case were the directors of Feltex Carpets Limited. Each of the directors faced two charges under s 36A of the *Financial Reporting Act 1993* (NZ). It was alleged that the financial statements of the company failed to comply with applicable accounting standards and that the directors had failed to prove that they took all reasonable and proper steps to ensure that the requirements of the applicable accounting standards would be complied with. The first charge related to a failure to disclose breaches of certain financial covenants contained in an ANZ Bank facility agreement. The other concerned a failure to classify the ANZ liability as a current liability.
2. In 2005, New Zealand was also in a transition period from its previous accounting standards (Generally Accepted Accounting Principles – ‘GAAP’) to the adoption of the New Zealand equivalent of the International Financial Reporting Standards (‘NZIFRS’). With regard to classification of liabilities, her Honour Justice Doogue noted as follows (at [64]):

*Under the previously applicable GAAP standards, the test represented a substance over form approach by which the liability would be assessed on the basis of the expectation as to whether the company would be required to repay in the upcoming twelve months. Therefore, regardless of the strictly applicable legal terms of the relevant facility, a company could still legitimately classify debt as non-current if it reasonably expected that the debt would not be called up in the next twelve months. By contrast the requirement under the IFRS standards is that the reporting entity have an unconditional right to defer the repayment of the debt for at least twelve months. This created a much more stringent test and was a significant shift in the governing principles of debt classification.*

1. In seeking to demonstrate that they took all reasonable and proper steps to ensure that the accounting standards would be complied with, it was submitted on behalf of the directors that they had:

* placed reliance on a qualified, competent and well-resourced financial management team;
* established a comprehensive transition process from GAAP to IFRS;
* engaged a highly reputable accounting firm (Ernst & Young) to prepare an IFRS assessment report identifying key areas and issues that needed to be addressed in the transition to the new IFRS standard so as to ensure compliance;
* created and established a steering committee comprising Feltex’s own financial management and supervised by Ernst & Young who would actively advise, educate, assist and participate in the review of all the IFRS standards applicable to Feltex and to take measures to ensure compliance;
* engaged Ernst & Young to undertake a review of the 31 December 2005 half year accounts with a particular emphasis on compliance with the new IFRS accounting standards;
* obtained declarations by the CEO and CFO that Feltex’s internal financial controls were adequate and effective;
* used an appropriately constituted audit committee whose responsibilities extended to overseeing the integrity of the financial reporting and control process; and
* in respect of the directors Thomas and Feeney, neither of whom were members of the audit committee, they had relied on the recommendation made to the board by the audit committee that the interim half year accounts were accurate and fully compliant with IFRS standards before taking the decision to approve and issue the accounts.

1. The regulator submitted that the directors should have themselves engaged in a study of the accounting standards, of the way in which they applied to Feltex and the financial statements and of whether in their own individual judgments the financial statements complied. Her Honour noted in the Feltex decision (at [142]):

*This approach necessarily resolves further into an argument that the directors should personally have had the requisite qualifications, expertise and experience to analyse the financial statement from the perspective of the accounting standards and to have reached a conclusion about compliance based on their own judgment. In other words, that they were not entitled to rely on professional expert advice and had to do it themselves.*

1. Her Honour concluded the directors did take appropriate steps to obtain advice upon which they relied as they were entitled to do, describing that the regulator’s “should have done it themselves” proposition was utterly unrealistic. Her Honour’s conclusions were summarised as follows (at [7]):

*…the IFRS standards are highly complex and presume in-depth knowledge of accounting principles. Those applying them and advising in relation to them have usually undergone specialist training because their interpretation and application requires highly specialised expertise within an already specialised field. Specialist auditors look to technical directors [within their audit firm] for assistance on their interpretation and application. These directors were entitled to seek and rely upon specialist advice. Ironically, it seems clear that the company’s specialist advisers were themselves judging the financial statement by reference to the requirements of the previous standards rather than the requirements of the new standards. That is the single most important reason why the directors have ended up having to face this prosecution.*

## Antecedent Legislation

1. It was contended by the directors that support for the view of Doogue J in the *Feltex* decision on the extent to which a director is entitled to place reliance on management and auditors in connection with the accuracy of financial reports can also be found in the antecedent legislation to s 344. Section 162(12) of the *Companies Act 1961* (Vic) stated as follows:

*Every balance-sheet and profit and loss account of a company shall be accompanied by a statement signed on behalf of the directors by two directors of the company, or in the case of a proprietary company having one director only, by that director, stating that in their opinion or his opinion –*

*a) the profit and loss account is drawn up so as to give a true and fair view of the results of the business of the company for the period covered by the account; and*

*b) the balance-sheet is drawn up so as to exhibit a true and fair view of the state of affairs of the company as at the end of that period.*

1. Section 163 of that Act provided that:

*(1) If any director of a company fails to take all reasonable steps to secure compliance by the company with the foregoing provisions of this Division or has by his own wilful act been the cause of any default by the company thereunder, he shall be guilty of an offence under this Act.*

*Penalty: Imprisonment for six months or two hundred pounds.*

*(2) In any proceedings against a person for failure to take reasonable steps to secure compliance by a company with the foregoing provisions of this Division it shall be a defence to prove that he had reasonable ground to believe and did believe that a competent and reliable person was charged with the duty of seeing that those provisions were complied with and was in a position to discharge that duty.*

*(3) A person shall not be sentenced to imprisonment for any offence under this section unless in the opinion of the court dealing with the case the offence was committed wilfully.*

1. In Australian Company Law and Practice (The Law Book Company Limited, 1965) the authors comment that s 163(2) of the *Companies Act 1961* (Vic):

*…comes from the English Act of 1948. It seems to recognize the view that a director is entitled to place reliance upon the competence and reliability of executive officers in the performance of their duties. It appears only to be concerned with those provisions of the Division which must be complied with by a company; that is to say, it is not concerned with the obligations which fall directly on the directors personally…*

1. Section 147 of the *Companies Act 1948* (UK) provided relevantly that:

*(2) For the purposes of the foregoing subsection, proper books of account shall not be deemed to be kept with respect to the matters aforesaid, if there are not kept such books as are necessary to give a true and fair view of the state of the company’s affairs and to explain its transactions.*

*…*

*(4) If any person being a director of a company fails to take all reasonable steps to secure compliance by the company with the requirements of this section, or has by his own wilful act been the cause of any default by the company thereunder, he shall, in respect of each offence, be liable on summary conviction to imprisonment a term not exceeding six months or to a fine not exceeding two hundred pounds:*

*Provided that—*

*(a) in any proceedings against a person in respect of an offence under this section consisting of a failure to take reasonable steps to secure compliance by the company with the requirements of this section, it shall be a defence to prove that he had reasonable ground to believe and did believe that a competent and reliable person was charged with the duty of seeing that those requirements were complied with and was in a position to discharge that duty; and*

*(b) a person shall not be sentenced to imprisonment for such an offence unless, in the opinion of the court dealing with the case, the offence was committed wilfully.*

1. The current UK provision is contained in s 414(4) of the *Companies Act 2006* (UK) as follows:

***Approval and signing of accounts***

*(1) A company’s annual accounts must be approved by the board of directors and signed on behalf of the board by a director of the company.*

*(2) The signature must be on the company’s balance sheet.*

*(3) If the accounts are prepared in accordance with the provisions applicable to companies subject to the small companies regime, the balance sheet must contain a statement to that effect in a prominent position above the signature.*

*(4) If annual accounts are approved that do not comply with the requirements of this Act (and, where applicable, of Article 4 of the IAS Regulation), every director of the company who—*

*(a) knew that they did not comply, or was reckless as to whether they complied, and*

*(b) failed to take reasonable steps to secure compliance with those requirements or, as the case may be, to prevent the accounts from being approved,*

*commits an offence.*

*(5) A person guilty of an offence under this section is liable—*

*(a) on conviction on indictment, to a fine;*

*(b) on summary conviction, to a fine not exceeding the statutory maximum.*

1. Thus, under the current UK provision, a director will not be found liable of an offence unless he or she fails to take reasonable steps to secure compliance and had knowledge that the accounts did not comply with the Act or was reckless as to that fact.
2. Based upon the view of Doogue J and the antecedent legislation, it cannot be denied that directors have been and are entitled to rely upon specialist advice. However, everything will depend upon the circumstances of the case, and whether a director has taken all reasonable steps will depend upon an analysis of the facts before the Court. Undoubtedly, what is encompassed by taking all “reasonable steps” will differ depending upon the entity, the complexity of the entity’s business and the internal reporting procedures within the entity. However, it will also depend on the nature of the task the director is obliged to undertake. I do not take the view, contended for before Doogue J, that the directors should have done it all themselves and become familiar with the complexities of various accounting standards. Of course, they cannot and are not required to take on that task. However, that is not what ASIC is contending for in this proceeding. To this I will return later. Therefore, whilst the views expressed by Doogue J are instructive, they were expressed specifically in relation to the facts as found and on the basis of the allegations made in that proceeding.

## Section 180 of the Act

1. I now turn to s 180(1) of the Act. Section 180(1) of the Act provides that:

*A director or other officer of a corporation must exercise their powers and discharge their duties with the degree of care and diligence that a reasonable person would exercise if they:*

*(a) were a director or officer of a corporation in the corporation’s circumstances; and*

*(b) occupied the office held by, and had the same responsibilities within the corporation as, the director or officer.*

1. The statutory duty imposed by s 180(1) reflects, and to some extent refines, that which applies at general law.
2. In determining whether a director has exercised reasonable care and diligence, as s 180(1) expressly contemplates, the circumstances of the particular corporation concerned are relevant to the content of the duty. These circumstances include: the type of company, the provisions of its constitution, the size and nature of the company’s business, the composition of the board, the director’s position and responsibilities within the company, the particular function the director is performing, the experience or skills of the particular director, the terms upon which he or she has undertaken to act as a director, the competence of a company’s management, the competence of the company’s advisors, the distribution of responsibilities within the company and the circumstances of the specific case.
3. Directors are required to take reasonable steps to place themselves in a position to guide and monitor the management of the company. A director must become familiar with the fundamentals of the business in which the corporation is engaged; a director is under a continuing obligation to keep informed about the activities of the corporation; directorial management requires a general monitoring of corporate affairs and policies, and a director should maintain familiarity with the financial position of the corporation.
4. While directors are required to take reasonable steps to place themselves in a position to guide and monitor the management of the company, they are entitled to rely upon others, at least except where they know, or by the exercise of ordinary care should know, facts that would deny reliance. There was no suggestion in this proceeding that the reliance on others was not warranted, nor was there any prior alerting to cause trust in those whom the directors had relied upon was misplaced.
5. In *Australian Securities and Investments Commission v Adler* (2002) 41 ACSR 72, Santow J (as he then was) said (at [372]):

*Although reasonableness of the reliance or delegation must be determined in each case, the following may be important in determining reasonableness:*

*(a) the function that has been delegated is such that “it may properly be left to such officers”:* Re City Equitable Fire Insurance Co Ltd *above per Romer J;*

*(b) the extent to which the director is put on inquiry, or given the facts of a case, should have been put on inquiry:* Re Property Force Consultants Pty Ltd*, above, per Derrington J at ACLC 1,060;*

*(c) the relationship between the director and delegate, must be such that the director honestly holds the belief that the delegate is trustworthy, competent and someone on who reliance can be placed. Knowledge that the delegate is dishonest or incompetent will make reliance unreasonable:* Dempster & Biala Pty Ltd v Mallina Holdings Ltd *(1994) 13 WAR 124 15 ACSR 1 at 62;*

*(d) the risk involved in the transaction and the nature of the transaction:* Permanent Building Society (in liq) v Wheeler *(1994) 11 WAR 109; 14 ACSR 109 (although in this case the Chief Executive Officer in question also had a conflict of interest);*

*(e) the extent of steps taken by the director, for example, inquiries made or other circumstances engendering “trust”;*

*(f) whether the position of the director is executive or non-executive:* Permanent Building Society (in liq) v Wheeler *per Ipp J, though, in* Daniels v Anderson *above, the majority have moved away from this distinction.*

1. In *AWA Ltd v Daniels* (1992) 7 ACSR 759, Rogers CJ Comm Div considered the circumstances in which directors could rely on management and auditors in connection with the company’s accounts (at 868-869):

*A director is justified in trusting officers of the corporation to perform all duties that, having regard to the exigencies of business, the intelligent devolution of labour and the articles of association, may properly be left to such officers:* Dovey v Cory*, supra, 485–6, 492–3; Re Brazilian Rubber Plantations & Estates Ltd, supra, 438;* Huckerby v Elliot *[1970] 1 All ER 189 at 193, 195. A director is entitled to rely without verification on the judgment, information and advice of the officers so entrusted. A director is also entitled to rely on management to go carefully through relevant financial and other information of the corporation and draw to the board’s attention any matter requiring the board’s consideration. The business of a corporation could not go on if directors could not trust those who are put into a position of trust for the express purpose of attending to details of management: American Law Institute “Principles of Corporate Governments, Analysis and Recommendations” pp 75, 176. Reliance would only be unreasonable where the director was aware of circumstances of such a character, so plain, so manifest and so simple of appreciation that no person, with any degree of prudence, acting on his behalf, would have relied on the particular judgment information and advice of the officers:* Re City Equitable Fire Insurance Co*, supra, 428. A non-executive director does not have to turn him or herself into an auditor, managing director, chairman or other officer to find out whether management are deceiving him or her:* Graham v Allis-Chalmers Manufacturing Co *188 A 2nd 125 at 130.*

*In relation to auditors, if directors appoint a person of good repute and competence to audit the accounts, absent real grounds for suspecting that the auditor is wrong, the directors will have discharged their duty to the corporation. The directors are not required to look at the entries in any of the corporation’s books of record, or verify the calculations of the corporation’s accountants in preparing the financial statements or of the auditor himself. Directors are entitled to rely on the judgment, information and advice of the auditor: cf* Re Denham & Co *[1883] 25 Ch D 752 at 766;* Dovey v Cory*, supra, at 486, 492). Reliance may properly be more complete where the auditor is acknowledged as being more knowledgeable, skilled and experienced in the particular matter in question than the directors or other auditors. A director is entitled to expect the auditor to carry out its duties utilising that higher degree of knowledge, skill and experience. In such circumstances the auditor will be under a higher duty of care than the standard of care of an auditor without such specialist knowledge, skill and experience:* Re Thomas Gerrard & Son Ltd *[1968] Ch 455 at 575;* Pacific Acceptance Corporation v Forsyth *(1970) 92 WN (NSW) 29 at 74;* Haig v Bamford *[1977] 72 DLR (3rd) 68 at 74;* Bartlett v Barclays Trust Co Ltd *[1980] 1 Ch 515 at 534. In the present case, Daniels was a partner in one of the Big Six major international accounting firms. The directors were entitled to rely on the belief that he could draw on all the resources of such a firm. Indeed, if the truth be known, to a large extent it was not lack of knowledge of facts that inhibited the proper discharge by Daniels of his duties.*

1. On appeal, Clarke and Sheller JJA called into question the “reliance exception” in the terms stated by Rogers CJ. In *Vines v Australian Securities and Investments Commission* 2007) 62 ACSR 1, Santow JA (who dissented on the facts but not on principle) clarified the position as follows (at [731]):

*The degree of an officer’s permissible reliance on others will turn on similar considerations as those that determine the overall standard of care for an individual director. They focus particularly on the characteristics of the company, the skills and experience of the officer concerned and the delegate, and the reasonably anticipated risks entailed in so doing. What is expected here is a level of scrutiny as befits supervision, not the detailed direct involvement that is associated with operational responsibility. Where there is no cause for suspicion nor circumstances demanding critical and detailed attention, it is reasonable for an officer to rely on advice, without independently verifying the information or scrutinising the data or circumstances upon which that advice is based: see* Re HIH Insurance Ltd (in prov liq)*;* ASIC v Adler *(2002) 168 FLR 253; 41 ACSR 72; [2002] NSWSC 171 at [372].*

1. The position of non-executive directors (as distinct from directors in general) has also been the subject of judicial consideration. In *ASIC v Macdonald*, Gzell J noted at [255] that:

*While Clarke and Sheller JJA in* Daniels *rejected the test propounded by Rogers CJ Comm Div for the limit of a director’s entitlement to rely on management, they did recognise that the role of a non-executive director was to guide and monitor the management of the company rather than to be involved at an operational level.*

1. It is clear that an objective standard of care is applicable to both executive and non-executive directors.
2. This approach to the standard of care has been adopted by the case law. An example of such is found in *Gamble v Hoffman* (1997) 24 ACSR 369. The court refused to subjectify the standard of care to (namely, in that case) the standard of a person who “left school at the age of 14 years, has no tertiary qualifications and has spent his life…essentially as a fruit and vegetable market gardener”. The court, at [373], rejected the assertion that:

*[S]ubjective considerations of that nature and extent should affect the minimum content of the duty or standard of care required of the respondents in this matter…*

*…*

*[T]he ambit of the duty and the standard of care depend on particular circumstances. However, the test is essentially objective that is did the officer exercise the degree of care and diligence that a reasonable person in a like position in a corporation would exercise in the corporation’s circumstances? I doubt whether the factors which Mr Bates advanced would justify a lower standard of care.*

1. In this proceeding, the directors’ responsibilities and duties were outside the realm of operational responsibility. ASIC does not contend that the directors needed to be involved at “an operational level”. This is not a case concerning the need to verify information or scrutinise data of a type outside each director’s own knowledge. The salient feature here is that each director armed with the information available to him was expected to focus on matters brought before him and to seriously consider such matters and take appropriate action. This task demands critical and detailed attention, and not just ‘going through the motions’ or sole reliance on others, no matter how competent or trustworthy they may appear to be.
2. Directors cannot substitute reliance upon the advice of management for their own attention and examination of an important matter that falls specifically within the Board’s responsibilities as with the reporting obligations. The Act places upon the Board and each director the specific task of approving the financial statements. Consequently, each member of the board was charged with the responsibility of attending to and focusing on these accounts and, under these circumstances, could not delegate or ‘abdicate’ that responsibility to others.
3. The case of *ASC v Fairlie* is instructive, where the defendant was charged with contraventions of both ss 276 and 555 of the *Companies (Tasmania) Code*. The case went to the Supreme Court of Tasmania by way of an appeal by the Commission against the decision of the magistrate to dismiss a number of the charges under both sections of the *Companies (Tasmania) Code*. In the course of his reasons, Zeeman J made a number of observations upon the operation of s 555.
4. Justice Zeeman said (at 682) that subs 555(2) (the now repealed statutory defence) related to conduct and state of mind of the defendant, whereas subs 555(1) required an objective consideration of the actual situation, and a consideration of what that situation requires of a particular director to secure compliance. The state of mind which might provide a defence was not relevant to a consideration of whether all reasonable steps had been taken.
5. Justice Zeeman also said (at 681) that the context in which s 555 appears was also highly relevant to the conclusion that s 555(1) required an objective consideration. That is, it was a provision of a statute which as a whole evinces an intent that directors and persons engaged in the management of companies must remain mindful of their obligations. As to the operation of the section the learned judge then said:

*S 555(1) requires the making of a number of inquiries. First it is necessary to ascertain what steps in fact were required to be taken by the Company in order to secure compliance with the relevant provision of s267. The test is an objective test. It is then necessary to ascertain what steps reasonably ought to have been taken by the respondent to secure compliance. Again, the test is an objective test but by reference to the particular circumstances of the case. What it is reasonable to expect from a director by way of achieving that object will depend on all such circumstances. If one takes s267(1)(a) as an example, the obligation of a company is to keep such accounting records as will correctly record and explain the transactions of the company and the financial position of the company. A director is required to take all reasonable steps to secure compliance with that obligation. It may be reasonable that the director personally discharge the obligation or that he takes steps to ensure that other persons are employed or engaged to do such things as will result in the company discharging that obligation. What is actually reasonably required of a particular director depends upon the facts of the case. The end of whatever it is that is required is to secure compliance and that is to be judged objectively.*

1. The learned judge in *ASC v Fairlie* did not expressly extend these remarks to s 276. There ought to be applied to s 344 of the Act a similar approach to that which Zeeman J outlined in relation to s 555 of the previous legislation. The language of the provisions and their legislative history both support the proposition that they relevantly carry the same meaning, so that what his Honour said about s 555(1) requiring an objective approach to the question of what was required to secure compliance is equally applicable to s 344. Justice Bergin seems to have taken the same view in *ASIC v Loiterton* [2004] NSWSC 172 with regard to s 318 of the Corporations Law as it existed prior to 1998.

## Mere mistakes not negligence

1. Section 180 requires that a director exercise due care and diligence. Merely making a mistake does not demonstrate that due care and diligence was wanting. The standard required of professionals, and directors, is of reasonable care and skill and does not require perfection.
2. In *ASIC v Rich* (2009) 236 FLR 1 at [7239] to [7342], Austin J related the standard of due care and diligence required of directors to common law duties of care owed by professionals. In both instances, the mere making of a mistake does not suffice to demonstrate a failure to exercise due care and skill. Justice Austin explained the position as follows:

*The statutory standard of care and diligence for company directors and officers, like the standard that applies in professional negligence cases, recognises the distinction between negligence and mere mistakes (*ASIC v Vines *(2005) 55 ACSR 617 at [1075], a passage not affected by the Court of Appeal’s judgment). Dealing with duty of care of a solicitor, McLelland CJ in Eq said in* Trust Co of Australia v Perpetual Trustees WA Ltd *(1997) 42 NSWLR 237 at 247:*

*Not every mistake by a solicitor founds liability in negligence. There are many uncertain or difficult areas of the law and the expression of an opinion by a solicitor does not normally constitute a promise that the opinion is correct. The duty of care owed by a solicitor to his client is to exercise reasonable skill and care.*

*Later (at 247–8) he remarked:*

*...Mistakes of the kind which I have held to have been made by [the solicitors] become much more apparent with the benefit of hindsight and in the light of full argument and the opportunity for unhurried investigation and consideration.*

*In that case the court declined to find that the solicitors were negligent, having regard to the circumstances in which they were asked to act, the way the problem was put to them and the way it developed, and the nature of the mistake. It seems to me that his Honour’s observations about mistakes apply, a fortiori, to errors of judgment.*

*In the* Vines *case, I held that the quoted passages from McLelland CJ in Eq’s judgment were applicable to people in the position of officers of a corporation, such as the defendants in that case. They are also relevant to the present case. In* Vines *the facts concerned forecasting in a reinsurance business, whereas in the present case the facts concern, among other things, financial forecasting in a telecommunications company. In both situations, forecasting is a difficult and uncertain process, with much room for mistakes and errors of judgment, and for differences of opinion.*

*The statutory issue under s 180(1) is not whether the defendants made mistakes in the process of financial forecasting, and a fortiori, it is not whether they formed opinions different from the opinions of ASIC or even of the court. The statutory issue is whether they failed to meet the standard of care and diligence that the statute lays down. The statute requires the court to apply a standard defined in terms of the degree of care and diligence that a reasonable person would exercise, taking into account the corporation’s circumstances, the offices occupied by the defendants and their responsibilities within the corporation. That requires the defendants’ conduct to be assessed with close regard to the circumstances existing at the relevant time, without the benefit of hindsight, and with the distinction between negligence and mistakes or errors of judgment firmly in mind. If the impugned conduct is found to be a mere error of judgment, then the statutory standard under s 180(1) is not contravened and it is unnecessary to advert to the special business judgment rule in s 180(2).* (own emphasis)

1. The determination of what constitutes due care and skill in any particular field of endeavour, and the assessment of whether it has been breached in a particular case, does not occur in a vacuum. A court assessing those questions, whether they arise in the context of directors’ standards of due care and diligence under s 180 of the Act, or in the context of negligence by a medical professional, typically receives evidence from others engaged in that field of endeavour. For instance, acceptable practice is relevant in determining the standard of care, but not decisive.
2. It was submitted that ASIC had not, in this case, adduced any evidence of the appropriate conduct of non-executive directors. It was not suggested, however, that this was fatal to ASIC’s case. It was said that the failure to lead such evidence was striking given that ASIC usually does lead such evidence in similar cases. For example: in *ASIC v Rich*, ASIC called expert evidence from two witnesses regarding the duties of directors and the role of a managing director and finance director in a listed company; in *ASIC v Vines*, ASIC adduced expert evidence from a Mr Hogendijk, who was an experienced CFO; in *ASIC v Forge* [2002] NSWSC 760, there was evidence from a Mr Tutt who was described by the trial judge as “an expert witness on the duties and activities of company directors”; and in *ASIC v Adler*, ASIC called expert evidence from an experienced company director as to what a careful and diligent director in Mr Adler’s position would have done.
3. It was contended that this Court has before it no expert evidence led by ASIC of the practices of directors which would inform its assessment of whether the approach adopted by the non-executive directors in this case (both in relation to their approach to the material provided to them and their reliance upon management and auditors) departed from standards of conduct accepted as responsible by experienced company directors. It was submitted that the only evidence bearing on this question that the Court has, is the uncontradicted evidence of Mr Hullah, an expert called by the non-executive directors, that, based on his long experience as an auditor retained by large listed companies, it would be “rare indeed” for members of an audit committee or non-executive directors to pick up a failure to comply with accounting policies. I will return to Mr Hullah’s evidence later.

## Relationship between ss 180 and 344

1. It is now convenient to consider the interplay between s 180 and s 344 of the Act. ASIC relies on the same conduct as giving rise to a breach of both ss 180(1) and 344. The directors submitted that the standard of conduct required of them under s 180(1) does not and cannot rise higher than the obligation imposed under s 344.
2. Undoubtedly, Part 2M of the Act contains a detailed and specific set of obligations on companies and directors in relation to the contents of financial reports and directors’ reports and their release to the market. There are no other provisions of the Act which contain financial reporting requirements. The general duty under s 180(1) must (in respect of directors’ duties concerning financial statements) be read consistently and harmoniously with the specific requirements of s 344 and with the specific requirements of any other provision in the Act.
3. Whether or not I would go so far as to say that the general law duty of the directors reflected in s 180(1) in the context of financial reporting is, in effect, delineated by s 344 I need not finally decide.
4. In my view, the interplay between s 180 and s 344 in the circumstances of this case is simply this:
   * + 1. The directors were required by s 180 to be diligent and careful in their consideration of the resolution to approve the accounts and reports; and
       2. The directors were required by s 344 to take all reasonable steps to secure compliance with the relevant provisions of the Act, and to at least inquire about any potential deficiency in the accounts and reports that they observed or ought by the exercise of the requisite care and diligence to have observed.
5. This approach is consistent with that which was taken by Bergin J in *Loiterton*. The defendants in that case were the directors of a listed company called Clifford Corporation Limited (‘CCL’). In *Loiterton*, her Honour made a number of findings that a director had failed to exercise care and diligence in approving accounts, by failing to make relevant enquiries or raise matters that ought to have been raised, and, in consequence, had failed to take all reasonable steps to secure compliance with the Act.

## Section 601FD(3)

1. The third civil penalty provision which is the subject of the declarations of contravention sought by ASIC, is s 601FD(3).
2. Section 601FD(1) of the Act provides that an officer of the responsible entity of a registered scheme must, among other things:
   * + 1. exercise the degree of care and diligence that a reasonable person would exercise if they were in the officer’s position: s 601FD(1)(b); and
       2. take all steps that a reasonable person would take, if they were in the officer’s position, to ensure that the responsible entity complies with the Act: s 601FD(1)(f)(i).

The duty in paragraph 601FD(1)(b) corresponds with the duty in s 180(1). Section 601FD(1)(f)(i) also encompasses and supplements the duty in s 344(1). Section 601FD(3) provides that a person who contravenes s 601FD(1) contravenes s 601FD(3). Section 601FD is engaged because CPTM and CMCSM are responsible entities of CPT and CRT respectively.

# Published Materials and Expert Evidence of Defendants as to Normal Practice

1. I consider that the published materials on matters of corporate governance, in particular those referring to the role of directors in the review of financial statements, are of some assistance in determining the obligations to be imposed on directors. In *ASIC v Rich* (2003) 44 ACSR 341, Austin J considered the relevance of material which ASIC proposed to tender consisting of relevant extracts from books, articles and papers by learned commentators which described the customary responsibilities and the role of the chairman of a listed public company. His Honour stated (at 358):

*[ASIC’s] evidence does not purport to establish, directly, that Mr Greaves had specific duties on particular occasions. It seeks to establish his “responsibilities” by reference to usual practice. Much of the literature of corporate governance is in the form of exhortations and voluntary codes of conduct, not suitable to constitute legal duties. It is sometimes vague and less than compelling, and must always be used with caution. Nevertheless, in my opinion this literature is relevant to the ascertainment of the responsibilities to which Mr Greaves was subject during [the relevant period].*

*…. It should be remembered, however, that the court’s role, in determining liability of a defendant for his conduct as company chairman, is to articulate and apply a standard of care that reflects contemporary community expectations. It is now commonplace to observe that the standard of care expected of company directors, both by common law … and under statutory provisions, has been raised over the last century or so.* (own emphasis)

1. His Honour concluded that it was open to the court to consider the materials put forward by ASIC and it was preferable for the court to embark upon the task of articulating a standard of care by reference to community expectations rather than to rely on unassisted ‘armchair reflection’.
2. A publication by the Australian Institute of Company Directors (‘AICD’) in 2006 entitled “How to Review a Company’s Financial Reports – A Guide for Boards” (the ‘AICD Guide’) is in evidence. As AICD described the process, directors should consider (ie, ask themselves) a number of questions, and raise issues with management if appropriate. The first question in the section headed “Overview” is:

*Do the financial statements make sense and present realistically the results, cash flows, and state of affairs of the company? Consider the adequacy of disclosures in order to present a “true and fair view”.*

1. Under the heading “Going Concern” it is suggested that directors consider what issues are relevant in determining that the company can pay its debts as and when they fall due. Under the heading “General” the following questions are included:

*Are there any matters included in the financial statements that could be viewed as misleading or confusing?*

*Are any of the directors aware of anything, from their personal knowledge or warnings from outside sources, which should be considered before signing?*

1. In my opinion, these references support an obligation on directors to have an enquiring mind, and look themselves at the financial statements. They reflect my own view of what is required of the directors in this proceeding, and what is required by the Act and the case law.
2. The defendants contend that what ASIC requires of directors is a far cry from what best practice in the real world requires of directors. I do not agree. Keeping in mind the comments of Austin J above, I do not consider that the ‘generalised’ literature tells against the specific obligation sought to be imposed in this proceeding. The directors rely upon the following material, which in my view does not address the issue of the responsibility of a director as alleged by ASIC.
3. The Introduction to the AICD Guide states that it sets out questions that might be posed by the audit committee, while some questions “may be relevant to raise at a periodic board meeting”. The Introduction goes on:

*However, directors need to remember they are not expected to be experts in financial reporting requirements.*

*Nevertheless, it is a director’s responsibility to be satisfied that:*

*• accounting systems applied are adequate*

*• appropriate expertise is applied*

*• the due process is sound*

*• essential elements of the process are scrutinised and tested by directors*

*• where appropriate, independent expert advice is obtained.*

*This will lead to directors’ confidence in the integrity of the outputs of management systems and the reliability of the financial reporting to the board. (emphasis added)*

1. Under the heading “Prudential controls and compliance with the company’s policies and procedures”, the AICD Guide sets out a number of questions a board may ask (at p 4 of the AICD Guide):

*Is there a detailed accounting procedures manual? If so, how often is it updated?*

*• How recently have the external auditors reviewed the manual? Was it satisfactory?*

*• How does management ensure compliance, by all operations, with the company’s established accounting policies and procedures.*

*• How does management satisfy itself that there have been no major breakdowns in internal controls that may have a material effect on the financial statements, either now or in the future?*

*• How have the procedures for GST been comprehensively reviewed to confirm that all requirements have been met and all recoveries have been made?*

1. Further, and under the heading “Compliance with accounting standards”, the guide sets out the following questions, after noting that the accounting standards have the force of law and must be followed when preparing financial statements:

*• How has it been confirmed that the requirements of AIFRS have been properly applied? For example, independent opinion.*

*• What are the key accounting standards that affect the company and how does management ascertain compliance with these standards?*

*• Have there been any other major amendments to existing accounting standards or issues of new accounting standards in the last year that affect the financial statements? If so, how?*

*• Could the company’s adoption of any accounting policies be reasonably challenged?*

1. The directors also referred to a booklet titled “Audit Committees: A Guide to Good Practice” issued by the AICD (the ‘Audit Guide’). The Audit Guide emphasises that the role of the audit committee is one of monitoring and oversight. In describing such a committee’s function, the Audit Guide states:

*[The audit committee] oversees and monitors the company’s audit processes, including the company’s internal control activities. This oversight includes:*

*- internal and external reporting (financial and, in limited areas, non-financial)*

*- oversight of risk management activities*

*- internal and external audit*

*- internal control framework including policies and procedures as they apply to financial reporting*

*- compliance with applicable laws and regulations*

*oversight of activities to control and report on fraud.*

1. It is clear that the Audit Guide does not ascribe to audit committee members, let alone other board members, responsibility for personally ensuring the accuracy of each and every figure in the company’s accounts and personally verifying that the accounting treatment used firstly to arrive at that figure, and secondly to determine the way in which it is characterised in the financial statements, accords with every accounting standard. The Audit Guide anticipates that management will advise the audit committee on matters concerning accounting policies and compliance with accounting standards and that the audit committee may look to the company’s external auditors for assurance in relation to management’s approach to those matters.
2. However, the important point is that whilst an audit committee has an important role of monitoring and oversight, this is not to the exclusion of the role of a director to consider the financial accounts for him or herself in the way I have attempted to explain. This does not involve a director being familiar with every accounting standard, but sufficiently aware and knowledgeable to understand what is being approved or adopted.
3. While ASIC stressed the centrality of the classification of current and non-current debt (rather than say the accuracy of the total debt level and therefore the gearing ratio), the non-executive directors submitted that:
   * + 1. ASIC’s perception of the importance of classification relative to other aspects of the financial statements is a view borne of regulatory hindsight and does not accord with reality within Centro in 2007. The accounting issues which were considered to be facing the Centro Group at the time are contained in the CFO and Mr Belcher’s “Accounting Issues” papers which make no reference to this issue; and
       2. if successful, ASIC’s case would require that non-executive directors have a knowledge of accounting practice generally and accounting standards generally, not merely a knowledge of the basic elements of the one or two standards that have, as matters have transpired, turned out to be critical in this case.
4. I do not consider, in the circumstances of this proceeding, that these submissions should be accepted. Undoubtedly there were important accounting issues being considered by Centro at the time, but this is no excuse for failing to focus on or pay proper attention to the importance of financial reporting.
5. Further, it may well be that directors should have a degree of accounting literacy that requires a knowledge of accounting practice and accounting standards. That is not for decision in this proceeding. All that is being alleged is that where the accounts on their face refer, as here, to classification of debt and post balance date events, the director adopting and approving the accounts should have a knowledge of and apply the basic elements of the one or two standards relevant to this proceeding.
6. As I earlier indicated, the directors also referred to evidence of the expert called by the non-executive directors, Mr Hullah. It was submitted that the evidence of Mr Hullah confirmed that the normal practice of non-executive directors in 2007 accorded with the AICD Guide rather than with the role ASIC seeks to ascribe to them.
7. While the usual practices of non-executive directors in 2007 do not, of themselves, determine the content of statutory norms of conduct, the extent to which the actions of a non-executive director accorded with the practice accepted in the relevant field is relevant in assessing the extent to which a particular director’s actions may have fallen short of the mark.
8. I accept that Mr Hullah’s experience over the course of his career has allowed him insight into the operation of the boards of national and multinational companies and to observe first hand how the board, management and the auditors operate in relation to one another. Mr Hullah has over 40 years professional accounting and audit experience. He has acted as auditor and advisor to large national and multinational companies and has had roles in reviewing the conduct of auditors.
9. Mr Hullah explained that the normal practices for the preparation, auditing and approval of financial statements of a company in a similar position to CNP and CER in 2007 was as follows:
   * + 1. management prepared the financial statements subject to the oversight of the CFO;
       2. management would normally consult with auditors on the application of accounting standards, particularly at the time of the introduction of new standards such as the Australian adoption of the International Financial Reporting Standards (‘AIFRS’);
       3. the transition to AIFRS was so significant that most companies such as CNP or CER established an accounting taskforce to consider the effect of the new standards on the company, and often outside advisors (such as the big accounting firms) were involved;
       4. even the big accounting firms, as well as training their staff in AIFRS, had specialised technical departments, and had a wealth of technical accounting knowledge far in excess of that held even by management of large listed companies;
       5. AIFRS taskforces would usually give a detailed report setting out the differences between AIFRS and the previous standards, including the significant change to the standard governing the classification of liabilities;
       6. if information emerges in what is usually the month or so between the release of the Appendix 4E and the final financial statements which suggest the Appendix 4E was incorrect, not only must the Appendix 4E be corrected, but the difference should be:

*clearly highlighted for the information of the audit committee and the board so that they may enquire into the reasons for these changes and be satisfied as to their validity prior to approving the financial report;*

* + - 1. the board approves the accounts only after:

1. receiving assurances from management that the accounts comply with the accounting standards and give a true and fair view; and
2. receiving the assurance of the auditor that they expect to sign the audit opinion without qualification (audit clearance);
   * + 1. it was usual for staff responsible for preparing the preliminary final report, senior management and the auditors to attend the meeting (it appears of the audit committee) called to approve the report and for other members of the board to be invited to attend the meeting;
       2. in accordance with ASX recommended best practice, it is recommended that at some stage the auditors meet with the audit committee in the absence of management so that the non-executive directors can confirm with the auditors that they have received all the assistance required and there are no matters the auditors wish to bring to the attention of the non-executive directors;
       3. given the number and complexity of the accounting standards, auditors usually ensure compliance of the financial report by use of a checklist; and
       4. auditors usually deal with management regarding the corrections required and the matter is only brought to the attention of the audit committee if management disagree with the auditors or refuse to make a change that the auditor deems necessary.
3. In so far as the non-executive directors of Centro are concerned, they appeared to follow these usual practices in respect of their approval of the accounts of CNP and CER of the financial year ended 30 June 2007. The question is whether the directors went far enough, and took all reasonable steps required of them. I accept that Mr Hullah’s description of the usual practices did not involve the non-executive directors personally conducting a quality assurance process to check the accuracy of the figures in the financial statements and their accounting treatment to the extent the directors say ASIC is contending for in this proceeding. However, I do not accept that ASIC is contending for the ‘high’ standard the directors say ASIC is so contending. As I have indicated, and as I will expand upon later, it is not being alleged that directors need to check the accuracy of figures or accounting treatment. It is being alleged that a director is to have a sufficient knowledge of conventional accounting practice concerning the basic accounting concepts in accounts, and to apply that knowledge based upon the information each director has or should have if he or she adequately carried out their responsibilities.
4. In considering whether the normal practices for the preparation, auditing and approval of financial statements were followed by Centro in respect of the financial statements of CPL, CPT and CER for the financial year ending 30 June 2007, Mr Hullah concluded that, in most respects, they were. Mr Hullah identified four areas where Centro’s practices departed from his experience. For the purposes of the proceeding, I accept that none of those areas of non-compliance were the fault of the non-executive directors and in any event are not pleaded by ASIC as constituting contraventions of the Act against any director. They were as follows:
   * + 1. the audit committee and the Board were not provided with a comprehensive report of the differences between the previously applicable accounting standard – the Australian Generally Accepted Accounting Principles (‘AGAAP’) and AIFRS;
       2. the audit committee and the Board were not advised that the criteria for classification of liabilities under AIFRS were materially different to that which had applied under AGAAP;
       3. the audit committee and the Board were not advised by management and the auditors that the financial reports of CNP and CER for the year ended 30 June 2007 were not in compliance with Australian Accounting Standards; and
       4. the audit committee and the board were not advised that an error had been detected in the CNP preliminary final report after it had been submitted to the ASX, that this error related to the classification of liabilities, and that the financial report had been corrected for this error.
5. It is my view that those responsible for managing the transition to AIFRS should have identified the change to the standards governing the classification of liabilities and brought that change to the attention of the BARMC in the course of their reporting to that committee on their work, or at the very least by including that change in the accounting policy manual used by Centro’s management (which did not occur).
6. For the purposes of this proceeding, I accept that the directors were assured by PwC, by their audit plans, that PwC would audit the accounts to ensure their compliance with accounting standards. Management also assured the non-executive directors that the accounts complied with accounting standards. Further, PwC attended numerous meetings of the BARMC and, whatever form of words may have been used by the relevant advisors at PwC, Mr Cougle and Mr Fekete, there seems no doubt that (in accordance with PwC’s audit plans) they gave the Appendix 4E accounts and the full financial statements audit clearance. Further, there is no evidence in this proceeding that PwC did raise any concerns regarding the accounts or the capability or diligence of management in the private sessions which management did not attend.
7. I also accept for the purposes of this proceeding that neither management nor PwC brought to the directors’ attention the change between the Appendix 4E and the final accounts. If the audit committee and the Board had been advised that a material error had been detected, this should have prompted them to enquire into the nature and reason for the error.
8. In the directors’ submission, the Court should accept Mr Hullah’s evidence, based on the normal practices prevailing in 2007, that:

*In my view it is reasonable for non-executive directors on an audit committee to expect that financial management whose duties include the preparation of financial reports are competent to fulfil this duty and knowledgeable about the rules governing the information to be disclosed in those reports.*

*In my view it is also reasonable for non-executive directors on an audit committee to expect that the auditors who have been engaged to perform the audit of financial reports are competent to fulfil this duty and knowledgeable about the rules governing the information to be disclosed in those reports. This is particularly so given their expertise in this area as I have outlined at paragraphs 6.23 and 6.24 above.*

1. In considering what is required of non-executive directors in order for them to discharge their statutory responsibilities, the directors submitted that this Court should not embrace the standard of perfection said to be contended for by ASIC. It was submitted that Mr Hullah’s report injected a much needed element of reality into these proceedings: in the context of the complexity and volume of the financial information included in the financial reports and the assurances received from management and the auditors, it was simply not reasonable to expect the non-executive directors to detect the error.
2. It was submitted by the directors that the same considerations apply in relation to the role of the non-executive directors in relation to the guarantees and the omission of reference to those guarantees in the full financial statements of CPL. The AICD Guide describes an “area of inquiry a prudent person would make before signing financial statements” to include: “Have all business areas been assessed after balance date to determine any disclosures that should be made in the notes?” As indicated by the AICD Guide, the appropriate steps to be undertaken by a non-executive director in this area involve the taking of steps to ensure that all areas of the business have been properly assessed for post balance date events. It was then submitted that the actual assessment is conducted by management and the auditors. The non-executive director’s function is concerned with process to ensure others are properly conducting the review.
3. When it was put to Mr Hullah that it was good practice in 2007 for members of an audit committee to specifically turn their minds to what subsequent events occurred, Mr Hullah’s evidence was that “They may do, but I don’t say they would necessarily do so”. In expanding on his answer, Mr Hullah said that it was only when there had been “some matter of major significance” such as a warehouse burning down or a major acquisition that he would expect an audit committee member to turn their minds to subsequent events. Mr Hullah did not think that a guarantee in favour of an associated company of US$1.75 billion would necessarily be an event of such significance that an audit committee member would be expected to specifically turn his mind to it, or even that such an audit committee member would consider that the event required disclosure. On this particular issue, I do not accept completely the approach taken by Mr Hullah, who was in my view responding under cross-examination without having had the opportunity to fully consider the specific matter raised with him. I prefer the more considered and detailed approach of Mr Lonergan, to which I will return. Nor do I consider that Mr Hullah’s instances of some matters of major significance are to be treated as exhaustive examples which may require disclosure.
4. The directors concluded their submissions, by saying that in light of assurances given and having regard to the highly skilled composition of the Centro accounting team and the auditors (who gave all the necessary assurances and did not raise any concerns) and the scope of PwC’s retainer (which extended to all areas of compliance with the accounting standards), the directors were entitled to rely on PwC and management to ensure that the necessary disclosures had been made. It was submitted that in the circumstances of this proceeding, failure to detect management’s error and the auditor’s error (if there in fact was an error) does not constitute breach of any duties owed by the non-executive directors.
5. I return to Mr Hullah. In my view, much of what he says (with which I agree) supports ASIC’s case in this proceeding. He accepted that ultimate responsibility for approval of the financial accounts rests with the board. He also considered that at one stage a director should read line by line the financial statements prior to their being adopted by a director. He also made the following observations:

*6.154 … I note that the wording of the accounting policy note (w) to the CNP financial report includes the words “Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 Months after the balance sheet date.” This accounting policy accords with the requirements of the wording in AASB 101, the applicable AIFRS standard, for classification of liabilities. In my view the plain English meaning of this sentence is quite clear. It may be argued that if audit committee members had focussed on this, recalled information they had received at recent board meetings regarding debt rollovers to a date within 12 months and also recalled the schedules entitled “Centro – Finance Facilities” referred to at paragraph 6.158 below they may have queried why no interest bearing debts had been included in current liabilities.*

*6.155 However, in my opinion, given:*

*a) the complexity and volume of financial information included in the financial reports the audit committee had to approve at 30 June 2007 (see paragraph 6.610 below); and*

*b) the assurances received from management and the auditors of the compliance with accounting standards which inter alia cover debt classification*

*I do not consider it reasonable to have expected the non-executive directors to have engaged in such micro management of the financial statement disclosures.*

1. Therefore, Mr Hullah did not have much difficulty understanding the plain English meaning of the classification requirement. Under cross-examination Mr Hullah provided further evidence. As to the complexity and volume of financial information, he later agreed that a board could control the extent to which they received material. Mr Hullah also accepted that no matter how many separate public companies a director may belong to, that would not affect the extent to which the director would need to focus on each company. I interpolate that having to deal with voluminous material cannot excuse failing to take sufficient care and responsibility. Mr Hullah agreed that the non-executive directors could not just blindly accept the information supplied to them by management, and they ought to at least understand the information. Mr Hullah also agreed that in considering the financial statements, and considering whether they made sense and presented realistically the state of affairs of the company, this was not the ‘micro management’ he referred to in the giving of his opinion referred to above. Mr Hullah also agreed that the misclassification of liabilities, as arose in this proceeding, would mean that the financial statements did not provide a true and fair view. Finally, as to the guarantees, he agreed that it would be good practice when considering the financial statements, for directors to consider whether there had been anything significant that had happened in the last two months that might be appropriate for disclosure.
2. This evidence supports the approach ASIC alleges relating to the reading and understanding of financial statements by the directors, and their undertaking the task of approving the financial statements.
3. I accept, as Mr Hullah opines, that it may be rare for an audit committee or non-executive director to pick up a failure to comply with accounting standards. To my mind, this does not mean that a director does not have the responsibility contended for in this proceeding. In any event, to conclude that something is ‘rare’, does not provide a great deal of assistance in determining the reasonable steps that a director needs to take before approving the financial statements.
4. As I have indicated, Mr Hullah did refer to the volume and complexity of the material before the directors. He concluded as follows:

*6.157 In stating the opinions at paragraphs 6.155 and 6.156 above I have taken account of the fact that the Centro board regularly received information regarding group borrowings.*

*6.158 In regard to the information provided to the board on group borrowings I note that each board meeting of the Centro Group had a standard agenda, one section of which was devoted to management reports. “Corporate Finance” was a sub-heading within this section. Under this sub-heading each month was a report entitled “Funding & Financial Risk Management Report”. This report followed a standard pattern of a narrative provided by the Chief Financial Officer (Romano Nenna) and the Corporate Treasurer (Michael Zickert) followed by a number of spreadsheets and schedules. The narrative provided by Mr Nenna and Mr Zickert would show the date as at which the information was current. This date was normally as close to the date of preparation of the schedule as possible and was not therefore synchronised with any financial reporting date. Amongst the attached schedules would be one entitled “Centro – Finance Facilities” which detailed the group borrowings. This schedule showed, inter alia, the total facility, the amount drawn and the average maturity of group borrowings. Information on this schedule agreed to the information provided in Mr Nenna and Mr Zickert’s narrative and would therefore seem to be prepared as of the same date. Throughout 2006 and 2007 the average maturity of group borrowings for CNP varied between 3 and 4.7 years which, in my opinion, would suggest to the reader that the group had no immediate short term debt problem.*

*6.159 Clearly the Centro non-executive directors would have been accustomed to receiving this information amongst the many other items of information that they received each month. However, this information was not provided in the context of approval of the financial reports, did not reconcile to borrowings disclosed in the financial reports, was provided as part of the board meeting package of information and was not included in the audit committee papers.*

*6.160 In reaching my opinion I have also taken account of the fact that production of the annual financial statements was referred to as ‘a massive project – 65 documents with 93 sets of complex financials at an average of 50 pages each equates to over 3,000 pages in total’ [NED.002.019.0039]. this is a huge amount of information for the members of the audit committee to read and understand and may make the failure to observe errors in the financial reports more understandable.*

1. It was submitted by the non-executive directors that on no reasonable basis could it be suggested that the non-executive directors were required to scrutinize and cross check all of the papers and annexures provided to the Board each month in the sort of detail as ASIC propound in respect of the Funding and Financial Risk Management submission. It was submitted that the Funding and Financial Risk Management paper held no particular significance above any of the other Board papers at the time. The non-executive directors considered that the papers in Section B for decision and the CEO’s monthly management reports in Section C were more important than the Funding and Financial Risk Management paper. In my view, this submission ignores that fact that over a period of time the information was provided, and each director would have or should have accumulated sufficient knowledge of what was contained within the papers and annexures, with reference being made to that material and information during discussion or otherwise.
2. In relation to CER’s debt, the non-executive directors submitted that ASIC relied solely on two pages of the CER 2007 Business Plan. Those two pages formed part of a Board pack of more than 1180 pages, provided in May 2007, and the information upon which ASIC relied was not referred to in the Executive Summary section of the CER 2007 Business Plan (which was itself a 72 page document). Nor was the information upon which ASIC relied covered in the presentation on the business plan delivered to the directors at their meeting in June 2007.
3. Whether this was sufficient or not to bring information to the attention of the directors, there was other information the directors had through documents that showed CER’s short-term debt, which was an important issue for the directors:

* A Board Submission dated 26 June 2007 prepared by Mr Shane Dudley which was entitled CER Management Report May 2007 and stated that there had been no change in either Domestic or US funding for CER during the month.
* A Board Submission dated 23 July 2007 prepared by Mr Shane Dudley which was entitled “CER Management Report – June 2007” and stated that there had been no change in either Domestic or US funding for CER during the month.
* The “Centro Banking Facilities Review” paper which in relation to CER Working Capital Facility – Extension of Facility requested the Board to approve a variation to extend the maturity date of the facility from 30 September 2007 to 31 March 2008.
* The minutes of the meeting of the CRL and CMCSM board meeting held on 6 September 2007 which record in relation to CER Working Capital Facility – Extension of Facility that the board approve the variation of the facility agreement with Commonwealth Bank of Australia Limited (‘CBA’) to extend the Maturity Date of the facility from 30 September 2007 to 31 March 2008.

1. In relation to this submission relating to the extent of the papers, I also make the following observations. A board can control the information it receives. If there was an information overload, it could have been prevented. If there was a huge amount of information, then more time may need to be taken to read and understand it. The complexity and volume of information cannot be an excuse for failing to properly read and understand the financial statements. It may be for less significant documents, but not for financial statements. As Mr Hullah accepts himself, the information was provided each month. The fact that information was provided in a different context does not detract from the fact that the directors were in possession of the information. The information was provided to the directors by management for a reason.

# the pleaded case

1. The directors contended that ASIC was bound by its pleaded case. It was contended that ASIC has sought to depart from its pleaded case in a number of respects. ASIC contended that it had not departed from its pleaded case.
2. A proceeding can only be decided upon a different basis to that set out in the pleadings where the parties agree to depart from what is alleged, or the court permits such a departure. As Mason CJ and Gaudron J noted in *Banque Commerciale SA (en liq) v Akhil Holdings Ltd* (1990) 92 ALR 53, by stating with sufficient clarity the case that the opposing party must meet, pleadings ensure what their Honours described as “the basic requirement of procedural fairness”. In the same case, Brennan J (as he then was) put the point in these terms (at 59):

*In* Thorp v Holdsworth *(l876) 3 Ch D 637 at 639, Jessel MR stated the object of pleadings: “The whole object of pleadings is to bring the parties to an issue, and the meaning of the rules of Order XIX was to prevent the issue being enlarged, which would prevent either party from knowing when the cause came on for trial, what the real point to be discussed and decided was. In fact, the whole meaning of the system is to narrow the parties to definite issues, and thereby to diminish expense and delay, especially as regards the amount of testimony required on either side at the hearing.”*

*When the pleadings bring the parties to the issue, the court’s function is to determine that issue and to grant relief founded on the pleadings unless the parties are allowed to alter the issues at the trial without amendment of the pleadings (as to which, see the observations in* London Passenger Transport Board v Moscrop *[1942] AC 332 at 340, 347, 351, 356). The rule is clearly laid down in the judgment of this court in* Dare v Pulham *(1982) 148 CLR 658 at 664; 44 ALR 117 at 121:*

Apart from cases where the parties choose to disregard the pleadings and to fight the case on issues chosen at the trial, the relief which may be granted to a party must be founded on the pleadings (Gould and Birbeck and Bacon [v Mount Oxide Mines Ltd (in liq) (1916) 22 CLR 490 at 517, 518]; *Sri Mahant Govind Rao v Sita Ram Kesho* [(1898) LR 25 Ind A 195 at 207]).

1. The recent decision of the Full Court of the Federal Court in *Castel Electronics Pty Ltd v Toshiba Singapore Pte Ltd* (2011) 277 ALR 116 again confirmed the importance of confining a party to its pleading and held at [304] to [308] that:

*This Court has recently reiterated that “[m]aterial facts must be pleaded with the degree of specificity necessary to define the issues and inform the parties in advance of the case they have to meet”:* Kernel Holdings Pty Ltd v Rothmans of Pall Mall (Australia) Pty Ltd *(1991) 217 ALR 171 at 173;* Betfair Pty Ltd v Racing New South Wales *(2010) 189 FCR 356; 273 ALR 664; [2010] FCAFC 133 at [49]*.

*In* Banque Commerciale SA en Liquidation v Akhil Holdings Ltd *(1990) 169 CLR 279 at 296-297, the High Court confirmed that a party is entitled, at trial, to have the opposing party confined to its pleading because the first party is entitled to come to trial to meet only the issues raised on the pleadings. If, however, the first party allows the other party to raise other material facts and issues for the determination of the court, then the court may proceed to determine the proceeding on those further material facts and issues. See also* Gould v Mount Oxide Mines Ltd (in liq) *(1916) 22 CLR 490 at 517.*

1. This proceeding is not one where the parties have chosen to disregard the pleadings and fight the case on issues chosen at trial.
2. ASIC has made no application to amend its pleading. ASIC is, therefore, bound by its pleading and the relief substantially as claimed in the amended application. Accordingly, the directors submitted that to the extent that there are properly identified areas of departure from the pleaded case, ASIC ought to be confined to its pleaded case and the departures rejected.
3. Based on ASIC’s pleaded case, and the defence of the directors, a key issue in this proceeding is whether ASIC has proved that the directors failed to take all reasonable steps to secure compliance by various entities with s 296 (accounting standards), s 297 (true and fair view) and s 298 (directors’ report) for the purposes of s 344(1) of the Act.
4. In the circumstances of this proceeding, if ASIC fails to prove a contravention of s 344(1), it is difficult to see how there would be a breach of the standard of care and diligence. Further, I interpolate that I approach s 601FD(1)(f), referring to “all steps that a reasonable person would take” in a similar manner to the approach I take in relation to s 344(1). No party suggested I should do otherwise.
5. The directors submitted that in approaching this key issue, the Court must proceed on the footing (in the absence of any allegations to the contrary) that the directors were reasonably entitled to place reliance on the processes which Centro had put in place for the purposes of ensuring that the financial statements were accurate and in accordance with the accounting standards, keeping in mind that accounting and auditing are specialised fields. For example, it was contended that the Court must assume that the directors were entitled to place full trust and confidence in the following matters:
   * + 1. Centro had a competent and qualified CFO, Mr Nenna;
       2. Centro had taken appropriate and adequate steps to manage the transition from AGAAP to AIFRS, which steps resulted in the preparation of a Centro accounting policy manual with input from both PwC and Moore Stephens;
       3. Centro had retained competent and qualified external auditors, PwC, to audit the financial reports of CNP and CER, and:
          1. PwC’s undertaking as auditor specifically included verifying compliance with accounting standards;
          2. PwC had complete access to staff and information to conduct its audit;
          3. PwC’s audit report for the relevant period which was received prior to 5 September 2007 did not raise any issues concerning the accounts or the competence or cooperation of management; and
          4. PwC gave audit clearance of the Appendix 4E financial statements at the August 2007 BARMC and the final accounts at the September 2007 BARMC meeting;
       4. the CFO and Mr Belcher (who during the relevant period was the Group Financial Accounting Manager at Centro) had provided the non-executive directors with “Accounting Issues” papers for the Appendix 4E financial statements at the August 2007 BARMC and the final accounts at the September 2007 BARMC meeting which purported to indentify the accounting issues which they felt needed to be drawn to their attention, but made no reference to any issue with regards to classification of liabilities or disclosure of post balance date events;
       5. the CEO, CFO and Mr Belcher had signed a management representation letter for the Appendix 4E financial statements at the August 2007 BARMC and the final accounts at the September 2007 BARMC meeting which the non-executive directors understood to convey assurance from them that the accounts were correct and in accordance with the accounting standards;
       6. the CFO and Mr Belcher had recommended to the Board that the accounts be approved, and Mr Cougle said at the September 2007 BARMC meeting that he could give comfort to the non-executive directors that the auditors had signed-off on the accounts; and
       7. no-one told the non-executive directors that the Appendix 4E financial statements contained an error when both management (Mr Belcher) and PwC (Mr Cougle) accepted that they should have been told of this.
6. For the purposes of this proceeding, I accept these submissions, and proceed on the assumptions contained within them. ASIC, as I understand its position, does not contend otherwise.
7. In their written submissions the non-executive directors then submitted as follows:

*The critical question the Court needs to determine is whether in the circumstances the obligation under s 344 to take all reasonable steps to secure compliance required the non-executive directors to personally scrutinise each line in the accounts looking for accounting errors or apparent inaccuracies and, even if so, whether it was negligent for them to have failed to detect the relevant errors where both management and PwC had previously missed them.*

*Even if the first limb of s 344 is engaged (if the Act imposes an obligation on a director rather than on the company), directors may still rely on others to assist them in fulfilling a requirement imposed upon them by the Act. In that case, the question for the court remains one of process — was the process such that a director took reasonable steps to secure compliance with the outcome prescribed by statute by relying on others. For example, the Act imposes an obligation on directors in s 306, which requires the directors of a disclosing entity to prepare a directors’ report for the half year. The first limb of s 344 is thereby engaged, but the consequence is not that directors must personally undertake each and every necessary step. On the contrary, directors may still ensure that an obligation imposed on them is discharged by delegating to others various tasks. Taking the example of preparation of the directors’ report under s 306, the directors may delegate the drafting to members of the management team. In that case, the directors may still have taken “reasonable steps to comply with” s 306 for the purposes of the first limb of s 344. To deny directors the capacity reasonably to delegate tasks to management would be to strip out from s 344 the words “take all reasonable steps to comply with” so that it would read “fail to comply with … Part 2M.2 or Part 2M.3”. Such a reading is contrary to the express terms of s 344 and, if adopted, would render those provisions of Parts 2M.2 and 2M.3 (which require steps to be taken by directors) in effect strict liability offences.*

1. In relation to this submission I make the following observations:
   * + 1. ASIC does not allege that the non-executive directors need to personally scrutinise each line of the financial statements as suggested. What is pleaded and contended for by ASIC is that having a sufficient knowledge of conventional accounting practice to enable a director to carry out his or her responsibility, each director had to read and understand the financial statements, and then giving consideration to those financial statements with each director’s accumulated knowledge, draw the error or apparent error to the attention of executive management or the other directors. It is then said, that in failing to draw the attention of the error or apparent error to the executive management or the other directors, the directors, and each of them failed to take all reasonable steps to secure compliance by Centro .
       2. I accept that directors may rely on others to assist them in fulfilling a requirement even where it is one directly imposed upon them by the Act. To a degree, the directors can rely upon the processes they have put in place. However, this is not exclusively the situation in the case of financial accounts, as I have endeavoured to explain. Of course, the drafting of a financial statement will be the domain of management. Nevertheless, the whole purpose of the directors’ involvement in the adoption and approval of the accounts is to have the directors involved in the process at a level and responsibility commensurate with their role. In other words a reasonable step would be to delegate various tasks to others, but this does not discharge the entire obligation upon the directors. A further step is required, so it can be said that *all* reasonable steps have been taken by the directors. To complete the process, this step, as I have said repeatedly in answer to the contentions of the directors, involves the directors and each of them taking upon themselves the responsibility of reading and understanding the financial statements in the way I have described.
2. I now look further to the pleaded case and the case presented by ASIC. I consider that ASIC has maintained its pleaded position to the extent it still persists in the allegations and has not deviated from its pleadings as contended for by the directors. However, I make one preliminary observation.
3. After ASIC closed its case, upon my request for a document setting out the material facts sought to be established, ASIC handed up a document titled “Material Facts Which ASIC Seeks to Establish”. By this document, it was contended by the directors that ASIC again sought to depart from its pleaded case and the case it opened. ASIC does not rely upon this document. The directors have and do rely upon the pleading and the opening. Therefore, I need not concern myself with this document as it has no relevance to defining the issues before the Court. There has been no suggestion that the directors acted, in the course of the trial, on the basis of the information in the document handed to the Court.
4. The case against each director and Mr Nenna is pleaded separately, but in each case in a similar manner. The pleading seeks to define the degree of care and diligence which is required of the director, in the relevant context of the approval of the Centro accounts, in two stages.
5. The first stage relates to the financial literacy and knowledge of the company’s financial position which the law requires company directors to have in particular circumstances.
6. ASIC submitted that the required financial literacy of a public company director extends to a general awareness of the financial reporting obligations of the Act, bearing in mind that directors have a statutory obligation under s 344 to take all reasonable steps to comply or secure compliance with them. This would include the knowledge that directors must approve the accounts and directors’ reports, that accounts must show a true and fair view and comply with accounting standards, and that the law requires the directors’ report to refer to particular things such as events after the balance date.
7. ASIC did not seek to establish that any of the defendants did not possess the necessary degree of financial literacy. In fact the intelligence, experience and knowledge of each director was relied upon to show that the omissions could only have occurred through lack of focus in approving or adopting the financial statements. Nevertheless, ASIC submitted that if the absence of the necessary financial literacy was an explanation for failure of any or all of the directors to notice the deficiencies in the accounts and reports, the failure to acquire such knowledge was itself a breach of the duty of care and diligence.
8. ASIC’s case was that there was an irreducible requirement upon the directors of involvement in the management of the company which includes maintaining familiarity with the company’s financial affairs. In the case of Centro, that required familiarity extended to being aware of the extent of the borrowings and the maturity profile of those borrowings, and aware of the guarantees which had been given in August 2007. It was ASIC’s case that every one of the directors in fact knew of these matters by virtue of various information and reports they were given. However, ASIC contended that if ignorance of these matters was an explanation for failure of any or all of the directors to notice the deficiencies in the accounts and reports, that ignorance itself bespoke a breach of the duty of care and diligence.
9. The second stage in defining the required degree of care and diligence is in the process of review of the accounts by the directors. ASIC submitted that it was the duty of every director to read the financial statements carefully and consider whether what they disclose is consistent with the directors’ own knowledge of the company’s affairs. ASIC’s case against each director was not that he did not look at the accounts. ASIC in its opening contended that each director did not do so with “the necessary degree of care, and application of the mind, to the task”.
10. Consistent with its pleaded case, ASIC, in opening, propounded that every director, whether executive or not, whatever his background, skills and role, had certain “irreducible” duties. ASIC’s senior counsel said:

*… there is an irreducible requirement upon directors of involvement in [the] management of [the] company which includes maintaining familiarity with the company’s financial affairs. In the case of the Centro companies that required familiarity extends to being aware of the extent of the borrowings and the maturity profile of those borrowings and aware of the guarantees which have been given in August. It is ASIC’s case that every one of the directors in fact knew of these matters by virtue of the information and reports they were given as detailed earlier. But if ignorance of these matters is an explanation for failure of any or all of the directors to notice the deficiencies in the accounts and reports, that ignorance itself bespeaks a breach of the duty of care and diligence.*

1. ASIC’s case was plainly focused on duties of care and diligence owed by any director irrespective of their personal qualifications, or background. ASIC also structured its case as to process on the care and diligence standard. Again in opening, ASIC said:

*The second stage, your Honour, of the way in which ASIC defines the required degree of care and diligence is in the process of review of the accounts by directors. It has already been explained that ASIC’s submission will be that it is the duty of every director to read the financial statements carefully and consider whether what they disclose is consistent with the directors’ own knowledge of the company’s affairs. Of course for each of these directors the knowledge of what precisely he did or did not do in this regard is solely his own. Some or all of them may choose later to give evidence about that, and the court may be in a position to make specific findings. ASIC’s case against each director is not that he did not look at the accounts; it is a case that each did not do so with the necessary degree of care and application of the mind to the task.*

1. In what in this proceeding became to be known as the “Blind Freddy” proposition, ASIC’s submission in opening was that the errors in the financial statements were so obvious that breach of the standard of due care and diligence is the inescapable conclusion that this Court must draw. The position is probably best summarised by what ASIC said in opening:

*We will submit that the court can draw the conclusion [as to breach of the standards of care and diligence] from the obviousness of the error to any reader of the accounts who had the requisite financial literacy and the knowledge that these directors had of the affairs of the companies, specifically their debts.*

1. Of course, this was said before evidence was led by each of the directors. It was submitted by the directors that ASIC’s case was that it matters not what mountain of detail obscured the facts that may have revealed the extent of short-term liabilities or that management failed to bring salient facts to the attention of the board or audit committee. It was further submitted that it also apparently matters not that PwC had undertaken in its audit plan to monitor compliance with accounting standards, that major accounting firms seemed to have struggled with this aspect of the transition to AIFRS, or that the Centro accounting policy manual prepared by Centro’s accounting team under the supervision of the CFO and with input from PwC and Moore Stephens misstated the test. The necessary result, it was submitted, if ASIC were to succeed in this proceeding, was that non-executive directors are required to spot accounting errors that numerous expert accountants within management and the independent auditors had missed. It will apparent from what I have already said, that this is not ASIC’s case.
2. It was also submitted by the defendants that ASIC proceeded in a fundamentally unfair and unsatisfactory way in mounting its case on s 344(1). It was contended that ASIC’s primary case was initially one based on due care and diligence. It was submitted that the particulars of the alleged breach of directors’ duties included in the amended statement of claim relate exclusively to the standard of care and diligence. For example, it was submitted that when ASIC pleaded that, in participating in the resolutions regarding the financial statements of CPL and CPT, Mr Cooper failed to exercise due care and diligence (implicitly s 180) and failed to take all reasonable steps (implicitly s 344), the only particulars ASIC gives of the alleged failures relate to s 180. It was contended that no particulars were given of the “reasonable steps” ASIC says that Mr Cooper (or any of the other directors) should have taken to comply with, or secure compliance with, Part 2M.3 of the Act.
3. The High Court observed in *Kirk v Industrial Relations Commission of NSW* (2010) 239 CLR 531 at [26], the “common law requires that a defendant is entitled to be told not only of the legal nature of the offence with which he or she is charged, but also of the particular act, matter or thing alleged as the foundation of the charge”. The Court continued (at [26] and [28]) to explain that the essential factual ingredients of the offence must be set out, and that, where the essence of the offence is a failure to do something, that which ought to have been done must be set out explicitly and with particularity:

*[26] The common law requirement is that an information, or an application containing a statement of offences, “must at the least condescend to identifying the essential factual ingredients of the actual offence”. These facts need not be as extensive as those which a defendant might obtain on an application for particulars. In* Johnson, *Dixon J considered that an information must specify “the time, place and manner of the defendant’s acts or omissions”. McTiernan J referred to the requirements of “fair information and reasonable particularity as to the nature of the offence charged.*

*…*

*[28] The statements of the offences as particularised do not identify what measures the Kirk company could have taken but did not take. They do not identify an act or omission which constitutes a contravention of ss 15(1) and 16(1). The first particular of the s 15(1) offence suggests that the Kirk company had some systems relating to the operation of the ATV in place, but that they were not sufficient. It does not identify the deficiency in the system or the measures which should have been taken to address it. The second particular does not identify what information, instruction or training was necessary to be given to Mr Palmer or the other employee of the Kirk company. The particulars of the s 16(1) offence say nothing about what should have been done to avoid exposing the contractors to risk to their health and safety from the use of the ATV. Needless to say, the appellants could not have known what measures they were required to prove were not reasonably practicable.*

1. In my view, the pleading is clear. The pleading gives sufficient notice to the defendants in accordance with the requirements set out in *Kirk*, assuming those requirements are applicable to this proceeding. For relevant purposes in considering whether the defendants have sufficient notice of what ‘reasonable steps’ should be undertaken, the essential elements of the pleading, taking Mr Cooper for example, are as follows. In paragraph 159 of the amended statement of claim the duty is set out. All ‘necessary steps’ to have sufficient knowledge of certain matters are described, including ensuring the director has sufficient knowledge to enable him to take ‘all reasonable steps’ to secure compliance with the relevant provisions of the Act. I would have thought that the directors, like other members of the community, are required to know the law. However, ASIC pleads in paragraph 159(c) a limited responsibility to take necessary steps to ensure sufficient knowledge of the requirements of Parts 2M.2 and 2M.3 to enable them to take all reasonable steps to secure compliance with the Act. Reading the relevant provisions applicable to one’s responsibilities would seem an appropriate starting point, one not undertaken by the directors in this proceeding. In paragraph 159(f), the duty to read and understand the financial statements and reports, and the duty to draw errors, apparent errors and omissions to the executive management or other directors, is set out. I should indicate that bringing something to management’s attention can be done in a number of ways, including asking questions or making appropriate enquiries and comments. It is then alleged in paragraph 160 that Mr Cooper failed to exercise the duties described previously in paragraph 159.
2. There is no mis-match between what is pleaded in paragraph 159 and paragraph 160. In paragraph 160(a) it is alleged that Mr Cooper failed to exercise his various responsibilities as pleaded in paragraph 159 (a reference to s 180(1)), and in paragraph 160(b) it is alleged there was a failure to take all steps that a reasonable person would take to secure compliance with the Act (a reference to s 601FD(1)(f)). This is made clear in paragraph 161. Paragraph 162 then picks up the allegations made in paragraph 159 and paragraph 160 making them applicable to CPL and CPTM and the specific alleged contravention of s 344(1) of the Act.
3. The particulars to s 160(c) are premised on the basis that “if” Mr Cooper had exercised the care and diligence described in paragraph 159, certain matters would have resulted. The particulars do not attempt to describe the ‘reasonable steps’, this already being achieved by the earlier references in paragraph 159 and 160.
4. The pleading in relation to Mr Scott is equally clear. The allegations against Mr Scott were particularised in a separate letter dated 23 December 2009. However, the scheme of the pleading is the same as that in relation to Mr Cooper. The basic knowledge requirement is set out, which Mr Scott should acquire. The requirement to take reasonable steps is referred to, after taking ‘all steps necessary’ to ensure a knowledge and understanding of Mr Scott’s obligations under s 344, Part 2M.2, 2M.3, s 295A, s 296 and s 297. Then it is set out what reasonable steps should be undertaken, there already being a reference that Mr Scott is alleged to have failed to exercise the degree of care and diligence described in “all, or one or more” of the sub-paragraphs of paragraph 123 (which corresponds to the allegation against Mr Cooper in paragraph 159).
5. The specific steps particularised are to have “carefully and diligently reviewed the accounts”, the “core requirements” being referred to by reference to sub-paragraph 123(f)(i) and (ii), and then it being alleged if this had occurred, the error would have been identified and steps taken to correct it. It is also alleged that if Mr Scott had exercised the care and diligence required of him, he would not have voted in favour of the relevant resolutions. In the body of the pleading, just as in the case against Mr Cooper, it is alleged that he should have drawn the error or ‘apparent’ error to the attention of executive management or the other directors. In the context of the use of the word “apparent”, it is meant to mean, and would be readily understood to mean, seeming to be in error. It has not been alleged that the directors were required to be ‘experts’ in accounting standards and positively pick the error.
6. It is alleged that if the directors had acted appropriately then the omissions would seem to be an error, which the directors should have picked up, and at least brought to the attention of the relevant person, or otherwise not participated in the resolutions without further enquiry.
7. The pleading and the particulars must be considered as a whole. Just because any one particular act or omission may not amount to, say, a failure to take reasonable care, does not mean that taking the allegations as a whole may not lead to that conclusion – see *Doonan v Beacham* (1953) 87 CLR 346, 351-2 (per Williams ACJ).
8. Further, as Kitto J observed in *Doonan* at p 352:

*The function of such particulars is not to divide a single issue of negligence into several distinct issues each requiring a separate finding, and to preclude a verdict from being given for the plaintiff unless he obtains a finding in his favour upon one or more of those issues. It is simply to confine the issue of negligence to the question whether the plaintiff’s injury was caused by negligent conduct of the defendant falling within the limited category of acts and omissions which is defined by the particulars considered as a whole.*

1. The defendants then made a number of submissions regarding the “shifting sands” of the ASIC case, none of which I regard as being made out or of any significance in the resolution of this proceeding.
2. First, I do not regard ASIC as bringing a new case based on s 295(4) of the Act, as contended by the directors. Section 295(4) is a provision which is of significance in a consideration of the scope of a director’s responsibilities. It has been pleaded, and whether or not ASIC in opening made “only passing mention” of that provision, (as suggested by the non-executive directors) hardly puts reliance on s 295 as a new case.
3. Further, the non-executive directors submitted that ASIC has not pleaded any case based on a failure to take reasonable steps under s 344 in relation to the directors’ report which it alleges (in paragraph 31H of the amended statement of claim) breaches ss 299 and 299A. This is not so as ASIC pleads a contravention of s 298, (which in turn refers to ss 299 and 299A), and then later pleads that each director failed to take all reasonable steps to secure compliance with s 298 of the Act, and thereby contravened s 344(1).
4. Then lengthy submissions were made by the directors as to the pleading and the directors’ knowledge of note 1(w) and note 18 to the accounts. Note 18 is not relevantly relied upon by ASIC, and I therefore focus upon note 1(w).
5. The case as pleaded is that the directors should have had sufficient knowledge of conventional accounting practices to enable them to recognise that the accounts were in error or apparent error. It was submitted that the case that ASIC pleaded and opened does not depend upon the non-executive directors having knowledge of note 1(w). It was submitted that notwithstanding its pleaded case, ASIC now seeks to rely on the presence of note 1(w) by suggesting that the directors ought to have read it and been informed that the accounts had not been prepared in a way that conformed with it and were therefore wrong.
6. ASIC submitted that it had pleaded note 1(w) and referred to the following paragraphs of its amended statement of claim (by reference to Mr Scott):
   * + 1. paragraph 29 — this paragraph sets out the content of note 1(w) in the CPL accounts;
       2. paragraph 35 — this paragraph set out the content of note 1(t) in the accounts of CPT (which was in substance the same as note 1(w));
       3. paragraph 42 — this paragraph set out the content of note 1(s) in the accounts of CRT (which was in substance the same as note 1(w));
       4. paragraphs 71-73 — these paragraphs plead the contents of the draft Appendix 4Es sent to the non-executive directors, and does not specifically refer to note 1(w) (and its equivalents). According to ASIC, the failure to pick up note 1(w) (and its equivalents) was just an error in the cross-referencing;
       5. paragraphs 82 and 84 — these paragraphs plead the contents of the Appendix 4E as signed by Mr Healey, and again do not refer to note 1(w) (and its equivalents), ASIC again said this omission was merely an error in cross-referencing;
       6. paragraph 123 — this paragraph refers to the standard ASIC pleads was required to be exercised by Mr Scott as a “reasonable director of a corporation in the circumstances of CPL and CPTM as described in paragraphs 45 to 104”.
7. If not for the error in cross-referencing, note 1(w) (and its equivalents) would form part of the pleaded knowledge which ASIC says the non-executive directors should have had.
8. The directors accept that the pleading relies on note 1(w) (in paragraph 30) to substantiate ASIC’s case as to the proper classification of the liabilities, but say note 1(w) had only this specific role in the pleaded case.
9. As to the non-executive directors’ knowledge, the critical paragraph is paragraph 103 of the amended statement of claim. That paragraph pleads that, by reason of the facts set out in paragraphs 45 to 102 (which paragraphs do not incorporate any reference to note 1(w) only because of the error in cross-referencing), the directors knew or ought to have known of the level of CPL’s and CRT’s short-term debt and the existence and significance of the guarantees. It was submitted that if ASIC’s case was that note 1(w) formed one of the “dots” which the directors should have joined in order to conclude that the accounts were in error or apparent error, it should have referred to it in paragraphs 103 and 104.
10. In my view, the pleading adequately brings to the directors’ attention the existence and significance of note 1(w). The error in cross-referencing would have been apparent to the reader of the pleading. I do not consider any director has been taken by surprise by reference to note 1(w) and the calling in aid by ASIC of the directors’ knowledge or constructive knowledge of it. The note 1(w) was referred to in the pleading, and was part of documents clearly before the directors to which they were said to have knowledge of at the relevant time. In any event, reliance can be placed by ASIC on note 1(w) in response to any suggestion by the directors in their evidence that they were not aware, or were not sufficiently aware, of the conventional accounting practice, and in particular the classification of current liabilities .
11. Another suggested deviation from the pleading related to reclassification following the Appendix 4E.
12. ASIC’s amended statement of claim does not refer to the reclassification of the interest bearing current liabilities of CNP following the release of the Appendix 4E (from nil to $1.1 billion) as a source of knowledge of the directors. It is not pleaded that any or all of the non-executive directors were informed that an error had been identified in the Appendix 4E, that management and PwC had agreed that the JP Morgan domestic bridge facility should have been classified as current and that the JP Morgan domestic bridge facility had in fact been reclassified in the full financial statements of CNP.
13. ASIC led evidence from Mr Cougle and Mr Cronin suggesting that those attending the BARMC meeting on 5 September 2007 were told of the change between the Appendix 4E and the final accounts.
14. ASIC acknowledged that there is no reference in Centro’s company secretary, Ms Hourigan’s notes to the matter having been raised which “would seem surprising [if it had been raised]” and that Mr Belcher did not recall drawing the attention of the BARMC meeting to that change.
15. In relation to this matter, the directors submitted as follows. No allegation was pleaded that the non-executive directors were informed by Mr Belcher (or anyone else) of the reclassification of the Appendix 4E – such a critical factual matter must be pleaded, and ASIC’s failure to plead the matter should be the end of it. In any event, Mr Belcher’s oral evidence was that the matter was not raised — his evidence was unequivocal, he had no uncertainly about his recollection, and his evidence was against his personal interest. If there is any question about what the non-executive directors were told, Mr Belcher’s evidence should be accepted. Mr Belcher’s evidence was supported by Ms Hourigan’s own evidence (she said “nobody said that [there had been an error in the 4E]”) and her careful notes – there is no reference in those notes to the matter having been raised. In view of the depth of detail in her notes, it is inconceivable that the matter was raised and not noted by her. It also beggars belief to suggest that the matter was raised and not one person at the audit committee meeting on 5 September 2007 said anything about it. Finally, on cross-examination, Mr Cougle turned out not to have any specific recollection of the matter having been raised at all, based his evidence on a recollection that changes between versions of accounts usually were raised with the Board.
16. In final submissions, ASIC did not press that I find as a fact that the matter referred to above was raised. I proceed in this proceeding on the basis that the matter was not raised. Therefore, I need not analyse any further whether there was a departure from the pleaded case on this matter.
17. In its amended statement of claim, ASIC allege only that the directors received extracts of the draft financial statements of CPL, CPT and CRT (within the September 2007 BARMC papers) prior to approving the accounts. In its opening, ASIC’s case was that the non-executive directors had not received either the full or the concise financial statement of CNP or CER by the time of the critical BARMC meeting on 5 September 20007. The opening included the following statement:

*Both the full financial statements and the concise financial reports of CNP and CER were completed and ready to be signed (and were in fact signed) on 6 September 2007). It appears that the full financial statements were completed by management on about 4 September 2007, but were still be [sic] considered by the Auditor and were subject to changes…*

*Save that he says that the completed full and concise financial statements were placed in a room at Centro’s head office by 6 September, Mr Belcher is unable to say anything further about the distribution of copies of those documents to the directors or even that they were in the hands of the members of the Audit Committee at their meeting the following day: a meeting which did not take place at Centro’s head office, but early in the morning at its office in Collins Street in the city.*

*If the members of the Audit Committee and the other directors did have available to them on 5 September 2007 a copy of the full financial statements of each of the CER and CNP, or event [sic] the concise reports, then it remains unexplained how they got them.*

1. ASIC only presses the facts now made clearer upon the directors giving evidence. I do not consider there is really much dispute about the sequence of events. The evidence adduced during the trial has established unequivocally that versions of both the full and concise financial statements of CNP and CER were made available to the directors prior to the relevant meetings. The full financial statements were available for review by the directors at the meeting room in Centro’s head office in Glen Waverley (called ‘the Glen’) from at least 2 September 2007. This was the usual Centro practice. The evidence of Mr Belcher was that:

*A version of the full financial statements of the Centro Properties Group, being Centro Properties Limited, and its controlled entities, including Centro Properties Trust, called CNP, was placed in a room at The Glen. The version in that room would have been updated progressively. There would have been a version of the CNP full financial statements in that room at The Glen on Sunday 2 September and Monday 3 September. Mr Belcher cannot say what version was or versions were in that room on those days.*

1. The evidence of each of the members of the BARMC (Kavourakis, Hall and Cooper) was that they attended the Glen to inspect them between 2 September 2007 and 4 September 2007.
2. Further, each of the non-executive directors had been provided with the concise financial statements of CNP and CER by emails sent by Ms Hourigan on 4 September 2007. With the exception of Mr Hall, the evidence of each of the non-executives was that they read or believed they would have read the concise financial statements prior to the relevant meetings. Mr Hall’s evidence was that he did not review the concise accounts because he had read the full financial statement at the Glen in any event. Similarly, Mr Kavourakis’ evidence was that he would not have read the balance sheets in the concise accounts for the same reason.
3. ASIC sought to say that the non-executive directors had not been given sufficient time to review the final accounts prior to the meetings. This was submitted by the defendants to be a shift in its case. In this respect, I do not consider that ASIC was altering its position, but was referring to the circumstances leading up to the approval of the accounts.
4. It was then suggested by the directors that ASIC’s pleaded case requires that directors “get it right”. The directors submitted that ASIC now contends that a director needs only to ask the appropriate questions.
5. The directors submitted that they were required, on ASIC’s case, to have sufficient knowledge of accounting standards to recognise that there were errors or apparent errors in the accounts. This (they submitted) required that the non-executive directors succeed where others (principally management and the auditors) had failed. Having recognised these errors and omissions, ASIC’s case is that the directors were then required to draw the error or omission to the attention of management, the BARMC and/or the other directors. It was submitted that ASIC’s pleaded case is not that the non-executive directors should have simply asked a question of management or the auditors. I have already considered the pleadings and expressed my view concerning ASIC’s case. As I have already indicated, to allege that a director is required to draw an error, apparent error or omission to the attention of management can be done in a number of ways. One way, is to ask a question.
6. Finally, it was submitted by the non-executive directors that ASIC has sought to avoid any suggestion that its case sets an unfeasibly high bar for non-executive directors by requiring that they obtain a working knowledge of the entire range of accounting standards by ASIC now suggesting that this proceeding (as it relates to classification) only requires a “routine and basic application of the test for classification of liabilities”. Putting to one side for the present the argument regarding whether the classification standard is as simple as ASIC would have it, this case, it was submitted departed from the pleaded case.
7. The directors have contested ASIC’s attempt to characterise the application of AASB 101 and AASB 110 as simple and routine. They submit that the application of accounting standards is a specialised field of expertise exercised by accountants and auditors and is complex. It was submitted that the case ASIC brought requires in effect that a director have a good working knowledge of all of the accounting standards, which it was submitted that ASIC seeks to walk away from.
8. As I have indicated, this is not the case ASIC brings in this proceeding. The ASIC case as pleaded is that there is only required a routine knowledge of and basic application of the test for classification of liabilities. It is not suggested, in the pleading or the opening, that the directors have a working knowledge of all of the accounting standards, or even a working knowledge of AASB 101 or AASB 110.

# THE APPLICATION OF THE PRINCIPLES

1. I now turn to apply the principles of law to the circumstances arising in this proceeding.
2. It is important to consider the ASIC case in the context of Centro, its business, the continuing role and participation of the directors, the role and contribution of management and the external advisors to Centro. Each non-executive director and Mr Scott gave evidence, upon which they were cross-examined. No issue of credit arose, and no impugning of the honesty of any director arises in these proceedings. I now turn to this context and the evidence, which in the main is not in contention.

## Context: The Centro Group

### Overview of Centro’s Business

1. The business of CNP was essentially two-fold. The first part of the business involved investment in and management of retail property. CNP invested in its managed funds through a two-tier structure. In the first tier, CNP co-invested with investors in two diversified direct retail property funds: the Centro Direct Property Fund (‘DPF’) and the Centro Direct Property Fund International (‘DPFI’) (collectively, the ‘Diversified Funds’). In the second tier, the Diversified Funds co-invested with investors in CNP’s various listed and unlisted funds (‘Ownership Funds’). The Ownership Funds owned the retail property assets financed by both equity and debt.
2. CNP owned or controlled approximately half of the Diversified Funds which in turn owned or controlled approximately half of the Ownership Funds. This effectively gave CNP a 25% equity share of the underlying retail property.
3. In 2007, CNP had two listed funds: CER and the Centro Shopping America Trust (‘CSF’) (formerly known as the Galileo Shopping America Trust). CSF was acquired by CNP in early 2007, but merged to become part of CER later that year. In 2007, CNP’s unlisted funds comprised approximately 34 direct property syndicates (formerly referred to as the MCS Syndicates) (‘Centro MCS Syndicates’) and two wholesale property funds (‘Wholesale Funds’): namely the Centro Australia Wholesale Fund (‘CAWF’) and the Centro America Fund (‘CAF’).
4. The second part of CNP’s business was in funds management. CNP acted as responsible entity for its managed funds and as custodian of the assets within those funds. It also performed other funds management activities such as securities distribution and new investment fund creation. In contrast, CER was a pure retail property trust.

### The Board of Directors

1. During the relevant period, the board of directors of CPL, CPTM, CRL and CMCSM were identical and comprised the non-executive directors and Mr Scott. Each of the non-executive directors and Mr Scott brought a set of skills to Centro, which was valuable to the group and contributed to the balance of skills Mr Healey, as Chairman, sought to achieve. Mr Goldie and Mr Wilkinson brought retail and property management experience, Mr Cooper expertise in corporate governance, Mr Kavourakis expertise in investment and funds management in relation to property and Mr Hall expertise in finance. Many of the non-executive directors rose through the ranks in commercial life, including Mr Goldie, who began his working life after school as a management trainee at Waitrose supermarkets in the UK, Mr Healey, who left school at age 15, later finishing his secondary education as a mature aged student and Mr Wilkinson, who worked his way up from being a trainee manager of Target Australia to become the Managing Director and CEO of David Jones.
2. With one exception (Mr Hall), the non-executive directors do not hold accounting qualifications. I accept that the non-executive directors are men appointed to the Board so that Centro could benefit from their business acumen and personal skills.
3. The Board generally met monthly. The meetings usually occurred on a Thursday and Friday. The papers for each Board meeting generally comprised about one large binder folder. As a matter of practice, the Board papers were distributed to the non-executive directors by courier on the Friday the week before the meeting. The exception to this practice was for Mr Wilkinson who was based in Sydney, to whom the Board pack was normally delivered on a Monday or Tuesday in the week of the meeting. On the occasion where Board papers were not finalised and ready for distribution in the Board pack, the papers would be emailed to the non-executive directors or tabled at the meeting.
4. The papers provided to the Board each month were voluminous. However, it is to be recalled that this is a matter that is within the power of the Board to control. It is the Board’s responsibility to determine the information it requires or does not require. The papers usually comprised around 450 pages. They were divided into three sections. Section A covered the minutes and matters arising from the previous Board meeting. Section B contained various papers relating to matters requiring Board decision at the meeting. Section C comprised the CEO’s monthly management report together with a large number of reports from management regarding the operation of the various parts of Centro’s business. Those later reports were prepared by management for the CEO and were provided to the Board for information. Each of the non-executive directors had their own individual practice for reviewing the Board and BARMC papers.
5. At Board meetings, the discussions would generally follow the agenda. The first item on the agenda was “Minutes and Matters Arising”. This item covered approval of the minutes of CNP, CER, the MSC Syndicates, the Wholesale Funds, the Diversified Funds and other funds from the previous meeting. The second item on the agenda was “Current Issues”. This item covered various specific matters which needed Board approval such as the approval of financial statements. The third item on the agenda was the “Management Report”. This item comprised a monthly CEO Management Report together with presentations in respect of the following topics: domestic property review, US property review, acquisitions, investment funds, Centro Group and corporate governance matters.

### Executive Committee

1. At all times, the Board delegated the day to day operation and administration of the Centro Group to an executive committee (‘Executive Committee’). In 2007, the Executive Committee comprised Mr Scott as CEO, Graham Terry as Chief Operating Officer, Glenn Rufrano as CEO Centro US, Mark Wilson as Chief Investment Officer, Romano Nenna as CFO, John Hutchinson as General Counsel and Head of Acquisitions and Philippa Kelly as General Manager Institutional Funds Management and Shared Services.
2. In June 2007, the Board resolved to adopt an updated written Delegated Authorities Policies and Procedures (version 5) (‘Delegated Authorities’). By way of example, under the Delegated Authorities, whilst the Board retained authority to approve the establishment, material variation or cancellation of Centro’s debt facilities, it delegated the task of negotiating the same to the Finance Committee of Centro (which comprised the CEO, CFO and Corporate Treasurer).

### Audit and Risk Management Committee

1. At all times, there were a number of sub-committees of the Board which assisted with the implementation of corporate governance practices. These included the BARMC, a Compliance Committee, a Nomination Committee and a Remuneration Committee. In 2007 (as I have said), the BARMC relevantly comprised Mr Kavourakis (Chair), Mr Hall and Mr Cooper.
2. When the meetings of the Board and BARMC were to occur close together, then a copy of the papers for the BARMC would be sent at the same time as the Board pack. The papers for the BARMC would be distributed to a list identified in the agenda which included the Board, the CFO, CEO, the external auditors and other members of senior management.
3. At all material times, the BARMC operated under a set of practices and procedures, which included the following:
4. For all BARMC meetings at which financial statements fell for consideration, the BARMC papers for that meeting would include an “Accounting Issues” paper signed by the CFO and Group Financial Accounting Manager. The purpose of the paper was to inform the BARMC of accounting policy issues and other important matters impacting on the financial reports for the meeting.
5. The CEO, CFO and Group Financial Accounting Manager were required to attend all BARMC meetings. The relevant external auditors were required to attend all BARMC meetings at which financial statements fell for consideration. The other non-executive directors not on the BARMC were invited to attend all BARMC meetings.
6. Prior to all BARMC meetings at which financial statements fell for consideration, the financial statements would be provided to the non-executive directors in the BARMC papers for the meeting or by email or made available for inspection by them at the Glen.
7. At all BARMC meetings at which financial statements fell for consideration, the BARMC would be provided with a management representation letter signed by the CEO, CFO and Group Financial Accounting Manager at the meeting. During the relevant period, Mr Belcher prepared this letter based upon a PwC precedent.
8. At all BARMC meetings at which financial statements fell for consideration, the relevant auditors would be called upon to provide “verbal audit clearance” in respect of the financial statements. In practice, the auditors would provide an indication to the BARMC at the meeting whether or not their audit of the financial statements was complete or substantially complete, and whether or not the financial statements were appropriate for approval by the BARMC and the Board.
9. At all BARMC meetings attended by the external auditors, the non-executive directors would hold a private discussion with the auditors in the absence of management. The purpose of such discussion was to enable the auditors to raise any matters of concerns about management with the BARMC.

### External Auditors

1. During the relevant period, PwC was the external auditor of CNP and CER and the Diversified and Wholesale Funds. In 2007, the partners managing the audit for PwC were Stephen Cougle for the listed entities and Peter Fekete for the unlisted funds. Also part of the PwC Centro audit team at the relevant time were Paul Belcher (prior to 2006), Andrew Cronin (director), Brad Duggan, Angela Evans, Amy Marshall and Will Dunlop.
2. During the relevant period, the auditor of the Centro MCS Syndicates was Moore Stephens. In 2007, the partner managing the audit for Moore Stephens was Kevin Neville. Prior to its merger with CER, Deloitte was the auditor of CSF.

### Centro’s Finance Department

1. At all times, Centro had a finance department responsible for maintaining the financial records and preparing Centro’s financial statements. During the relevant period, the department was headed by Mr Nenna. Also employed in the Centro finance department during that time was Paul Belcher as Senior Financial Accounting Manager and Richard Gore. As referred to above, Mr Belcher had previously worked for PwC. Mr Belcher’s predecessor was Chris Meehan. Mr Belcher reported to the CFO, and Mr Gore reported to Mr Belcher.

### Centro’s Financial Risk Management

1. During the relevant period, the Centro Group maintained a “relatively diverse” lender exposure, dealing with its lenders under bilateral arrangements, rather than in syndicated arrangements. The group had a “core relationship bank group” which comprised ANZ, CBA, NAB, BNP and RBS. It maintained a number of different finance facilities with its lenders which matured from time to time. Prior to late 2007, there had been a strong and consistent history of Centro finance facilities at maturity either being rolled over or refinanced “as a matter of course”. Debt was readily available and there were no concerns about Centro’s capacity to refinance.
2. Whenever a Centro finance facility was due to mature, in accordance with the designated authorities, the Board would be asked to approve a roll over or refinance of the facility which had already been agreed between the lender and management. From time to time the Board was also asked to approve new finance facilities – eg to fund new acquisitions – which had similarly already been agreed between management and the bank. As a matter of practice, the CFO would issue a Board paper recommending each roll over, refinance or new facility.
3. At all times, the Centro Group had in place a number of funding and financial risk management policies, including a policy to maintain a certain average maturity for core debt. In 2007, the policy was set at a minimum of three years. The Board monitored compliance with the funding and financial risk management policies on the monthly basis.
4. It is not in contention that the minimum maturity policy of three years applied to “core” debt, which Mr Healey described as “debt we incurred in the short term to make an acquisition which then would be paid down in one form or another”. Mr Healey was not otherwise familiar with the detailed basis upon which non-core debt figures were prepared.
5. On this aspect of financial risk management, I find the following facts which the non-executive directors knew:
   * + 1. Centro had a large number of facility agreements with staggered maturities;
       2. the business practice was to pay down short-term debt (either by refinancing or equity raising);
       3. the average maturity level of the ongoing, or core business debt, was monitored by the Board on a monthly basis against an approved benchmark (ie through the Funding and Financial Risk Management papers);
       4. management was responsible for arranging to roll over or otherwise satisfy Centro’s debt obligations and was able to do so with no apparent difficulty at all times until December 2007; and
       5. around August to September 2007, refinancing of facilities could occur, although with the market difficulties there might be some impact on price.
6. I also find that none of the non-executive directors had the practice of carefully reviewing the annexures to the operational reports contained in Section C of the Board Papers, although they were aware generally of the information contained therein. The directors certainly would have accumulated knowledge contained in the annexures over a period of time. They each proceeded on the footing that the ordinary practice would be followed, namely that if the information contained in these annexes was important it would be drawn to their attention in the body of the paper or referred to by management at the Board meeting. In the case of the relevant annexures to the Funding and Financial Risk Management papers relied on by ASIC in the amended statement of claim, the documents were not always referred to in the body of the paper and the evidence is that they were not raised by management at any of the relevant Board meetings.
7. I observe that while ASIC does rely upon the annexures to the Funding and Financial Risk Management submission as a key source of information regarding CNP’s position, ASIC also relies upon the following documents as sources of information and proof of the directors’ knowledge of such information:

* Board Submission A7-1 entitled “CNP-Matters Arising” for the June 2007 meeting which contained information about when the CBA Tranche B was due for repayment.
* CNP 2007 Business Plan, in particular Section B.2.3.
* The minutes of the CPL & CPTM Board meeting held on 7 June 2007 which recorded that:

• The board resolved entry by each company on its own account and as trustee or responsible entity of each relevant trust or registered scheme, into an extension of the existing A$75 million unsecured multicurrency cash advance facility provided to CPT by the CBA to 30 June 2008 and an increase in the facility by up to A$100 million to A$175 million on terms generally commensurate with those set out in Centro’s existing working capital facility with CBA;

• The board resolved to approve the variation of the unsecured facilities agreement with BNP Paribas on the following terms:

 Extend the maturity date of the facilities from 15 June 2007 by 90 days;

• In relation to the Funding and Financial Risk Management report, an update was provided to the Board as set out in the board papers and discussed.

* The minutes of the CPL and CPTM Board meeting held on 5 July 2007, which state that in relation to the Funding and Financial Risk Management Report, an update was provided to the Board as set out in the board papers and discussed.
* Board Submission A7-1 entitled “CNP Matters Arising” for the August 2007 meeting which recommended that the directors approve an extension of the maturity date of the existing BNP Paribas Tranche D facility of US$200 million to the earlier of 15 August 2007 and the closing of the proposed US Private Placement Program.
* Mr Nenna’s presentation to the August 2007 board meeting entitled “Financial Risk Management Review” which says on p 6, second slide, “JP Morgan Australian bridge US$930 million (Dec 2007). Repaid from equity sell downs within 12 months”.
* The August 2007 Funding and Financial Risk Management paper itself, which contains information about the maturity of the JP Morgan Australian bridge being 4 January 2008 and the intention to partially repay this bridge from equity sell-downs and to refinance the balance through other relationship banks prior to the scheduled maturity date.
* The minutes of the CPL and CPTM board meeting held on 2 and 3 August 2007 which state:

• The board resolved to approve the variation of the unsecured facilities agreement with BNP Paribas on the following terms:

 extend the maturity date of the facilities to the earlier of 31 August 2007 and the closing of the US Private Placement program;

• In relation to Financial Risk Management Review presentation:

 A presentation was tabled by management and discussed; and

 It was resolved that the Board approve the modification of the Centro Financial Risk Management Policy to exclude specific-purpose, acquisition funding facilities which are to be refinanced or paid down within 12 months.

• In relation to the Funding and Financial Risk Management report, an update was provided to the Board as set out in the board papers and discussed.

* The Centro Banking Facilities Review paper which:

• Stated that of Centro’s total facilities of $4.43 billion, just over $2.14 billion were currently classified as Immediate Short Term. These included the $1.12 billion JPM Australian domestic Bridge, referred to in the last Board paper (which was to mature on 31 December) and residual “Heritage” acquisition bridge facilities from ANZ and RBS (which were to mature on 30 September 2007);

• Attached a schedule entitled “Centro Facilities Review” which among other things, analysed CNP’s borrowing facilities existing at or about 31 August 2007 by bank, showing which were due to mature within six months; and

• Requested the Board to approve among other matters and extension to the term of the unsecured multi currency facility with RBS from October 2007 to April 2008.

* The September 2007 Funding and Financial Risk Management board paper which stated that as previously anticipated Centro’s second US Private Placement settled on 15 August 2007. The total expected issuance was US$180 million on terms identical to those previously provided to the Board.
* The minutes of the September 2007 CPL & CPTM board meeting which stated:

• In relation to the Centro Banking Facilities Review:

 That the boards approve the entry by the company into an agreement to extend the term of the $410 million unsecured multi currency facility with RBS from October 2007 to April 2008;

• In relation to the Funding and Financial Risk Management report, an update was provided to the Board as set out in the board papers and discussed.

1. On the basis of this documentation, without more, I find that there were short-term liabilities as alleged by ASIC which each of the directors were aware of or should have been aware of. This information concerning debt was put before the Board and was readily available to each director over a period of time.
2. I will detail the evidence of the directors later. By way of summary, the evidence of the directors as to short-term debt was as follows. The evidence of Mr Healey was that he did know that CNP had substantial short-term debt in the order of $2.5 billion. Mr Kavourakis was aware that CNP and CER had facilities that had to be refinanced within 12 months of 30 June 2007, not necessarily repaid. Mr Hall’s evidence was that, while he kept himself informed by means of the various papers provided by management and from the annual accounts, he did not think he was otherwise aware in July 2007 of the level of debt of CNP which was maturing within 12 months. Nevertheless, Mr Hall had been given all the information referred to above, in the same way as the other directors. Mr Cooper was aware around the time of reviewing the Appendix 4E financial report that CNP had debts maturing within the year of about $2.5 billion and read the Banking Facilities Review for CNP which provided a figure of $2 billion was due within six months. Mr Goldie was aware there was substantial debt but could not recall the specific figures in September 2007. Mr Goldie was broadly aware in June 2007 of CNP’s debt position. Mr Scott was also aware of the short-term debt position.
3. I conclude that each director knew or should have known that CNP and CER had substantial short-term liabilities which were required to be repaid or refinanced during the year ending on 30 June 2008 as alleged by ASIC.

## Context: Approval of the 2007 Accounts

### July BARMC meeting – interim meeting

1. An ‘interim’ meeting of the BARMC was held on 16 July 2007. Whilst no minutes were taken, the meeting appears to have been attended by, amongst others, the CEO, the CFO, Mr Belcher, the directors, and Mr Fekete, Mr Cougle, and Mr Cronin from PwC. The purpose of this meeting was to consider interim year end accounting issues for CNP for the year ended 30 June 2007.
2. The BARMC pack for the meeting included a Board Audit submission from the CFO and Mr Belcher entitled “Interim Year End Accounting Issues – CNP” dated 18 July 2007. The paper purported to summarise the “key accounting policies and other matters which will impact on the financial report of CNP for the year ended 30 June 2007”. The paper discussed the following matters: accounting policies (which were stated to be consistent with those applied for the half year ended 31 December 2006); the accounting of CNP’s key investments for the year; the accounting of CNP’s acquisition of Heritage; the accounting of CNP/CER’s acquisition of New Plan; the accounting of an exchangeable notes issue which took place in June 2007; a review of CNP’s Treasury Management System (Integra-T) undertaken by Ernst & Young; impairment testing of CNP’s assets under AASB 136; and other matters.
3. For this meeting, the BARMC also received an updated audit plan from PwC for 2007 dated 5 July 2007. The audit plan purported to detail PwC’s activities to date, PwC’s response to the business risks identified in the previous audit plan and provide an update of any new business risks that had arisen from PwC’s perspective in the past six months. The updated risk analysis included exposure to US economic risks given the growth in US assets. The planned response to this risk was described as ensuring a thorough understanding of transactions and application of the appropriate accounting treatments. The action taken to date in respect of this risk was indicated as follows:

*PwC has worked closely with management in relation to the significant transactions in the last six months such as the acquisition of Heritage and New Plan.*

1. The updated risk analysis also included a number of accounting issues and policy matters which were said to be presently under review as a result of transactions or evolving AIFRS interpretations. The planned response was to address the issues in “technical papers” which would be reported to the Board. Finally, the updated audit plan included a year end timetable which included “verbal audit clearance” of the Appendix 4E financial report to the BARMC on 2 August 2007 and “final audit clearance” on the full set of financial statements on 6 September 2007.

### August BARMC meeting – Appendix 4Es

1. The next relevant meeting of the BARMC occurred on 2 August 2007. The meeting was attended by, amongst others, the CEO, the CFO, Mr Belcher, the non-executive directors and Mr Fekete, Mr Cougle and Mr Cronin from PwC. The purpose of the meeting was to consider the Appendix 4E preliminary financial reports for CNP and CER for the financial year ended 30 June 2007.
2. The BARMC pack for the meeting included an “Accounting Issues” Board Audit submission from the CFO and Mr Belcher dated 27 July 2007. The paper purported to summarise the “key issues addressed in preparing the financial reports for CNP and CER for the year ended 30 June 2007”. The paper dealt with the following matters: financial results and highlights; accounting for the New Plan acquisition (which it was said would include an “acquisition note” in the financial statements); subsequent events; accounting of impairment testing; and other matters. In respect of subsequent events, it is stated:

***C. Subsequent Events***

*The financial statements of CNP and CER for the year ended 30 June 2007 may require notes disclosing subsequent events. Whilst no events requiring disclosure exist at the date of writing, the requirements of AASB 110 “Events after the Balance Sheet Date” will be revisited prior to the signing of the CNP and CER financial statements.*

1. For the meeting, the audit committee also received a management representation letter dated 31 July 2007 signed by the CEO, the CFO and Mr Belcher; a Board Audit submission dated 27 July 2007 issued by the CFO and Mr Belcher, recommending that the Board appoint a sub-committee of at least two directors with the power to approve, subject to finalisation, the financial statements of CNP and CER for the year ended 30 June 2007; and draft Appendix 4E financial statements for CNP and CER for the financial year ended 30 June 2007. The draft accounts again contained no current interest bearing liabilities for CNP or CER.
2. At the meeting, the audit committee also received PwC’s audit report for CNP and CER for the year ended 30 June 2007. The covering letter dated 2 August 2007 addressed to Mr Kavourakis stated:

*This report includes matters arising from our audit up until the date of this report. Any subsequent matters will be brought to your attention at the Committee meeting on 6 September 2007.*

*We take this opportunity to thank the management and staff of Centro for the co-operation and assistance extended to us during the audit. In particular, we acknowledge the role and assistance of Romano Nenna, Paul Belcher and their team.*

1. The audit report covered four topics: significant accounting and reporting matters; summary of unadjusted differences; internal controls, including fraud; and auditor independence. The significant accounting matters dealt with in the audit report were: the New Plan acquisition; goodwill impairment; the CER restructure (which involved CNP disposing of its interest in CER to the Diversified Funds); the acquisition of the Centro Watt joint venture (which involved CNP buying out Watt from the joint venture); the acquisition of the Galileo America Shopping Centre Trust (CSF); the treasury function (which involved valuation of cross-currency transactions); the exchangeable notes issued by CNP in June 2007; and the recognition of revenue. No internal control weaknesses and no fraudulent activities were identified in the report. The audit report raised no issues of concern to PwC.
2. The company secretary, Elizabeth Hourigan, took handwritten notes during the meeting. She was a very diligent note taker, and her notes are comprehensive and detailed. It is apparent from her notes that the following relevant events occurred at this meeting. The CFO presented his accounting issues paper. Mr Cougle presented PwC’s audit report. Mr Cougle of PwC indicated that PwC’s audit was largely complete. There followed a detailed exchange between the members of the BARMC, the CEO, the CFO, Mr Fekete and Mr Cougle about various accounting issues which had been raised. The meeting then conducted a “page turn” of the CNP and CER draft Appendix 4E statements led by Mr Kavourakis, and punctuated by questions from the members of the BARMC and answers from management or the auditors. The BARMC then had its usual private discussion with the auditors in the absence of management. Following the return of management, the management representation letter was tabled. Mr Kavourakis asked if anyone had any queries. Mr Hall raised a point regarding future cash resources. Finally the BARMC resolved to recommend to the Board that the Appendix 4Es be adopted. This meeting dealt with the accounts for CNP and CER subject to receiving audit finalisation.
3. The meeting of the sub-committee of the Board followed on 7 August 2007, attended by the CEO, Mr Healey and Ms Hourigan. At that meeting, the sub-committee agreed to approve the Appendix 4Es for signature and release to the ASX. The Appendix 4E preliminary financial reports for CNP and CER for the financial year ended 30 June 2007 were signed by the Chairman of the Board and released to the ASX on 9 August 2007. The accounts contained no interest bearing liabilities in the balance sheet of CNP or CER.

### August BARMC meeting – CSF

1. There was another meeting of the BARMC on 24 August 2007. The meeting was attended by, amongst others, the CEO, the CFO, the Group Financial Accounting Manager (Mr Belcher), the non-executive directors and representatives of Deloitte. The purpose of the meeting was to consider the Appendix 4E preliminary financial statements of CSF for year ended 30 June 2007.
2. This meeting adopted the same practices as followed for the listed entities. The BARMC received an “Accounting Issues” Board Audit submission from the CEO and Mr Belcher; management representation letters; an audit report from Deloitte dated 22 August 2007; and draft Appendix 4E preliminary financial statements of CSF for the year ended 30 June 2007. The BARMC ultimately resolved to recommend to the Board the appointment of a sub-committee of at least two directors including two of the Chairman of the Board, the Chairman of the BARMC and the CEO to finalise CSF’s Appendix 4Es for the year ended 30 June 2007.

### September BARMC meeting – final accounts

1. There was a final meeting of the BARMC on 5 September 2007. The meeting was attended by, amongst others, the CEO, the CFO, Mr Belcher, the non-executive directors and Mr Fekete, Mr Cougle and Mr Cronin from PwC. The principal purpose of the meeting was to consider the financial reports for the unlisted entities for the financial year ended 30 June 2007. The meeting was also convened for the purpose of considering approval of the financial statements of CNP and CER for the year ended 30 June 2007.
2. For this meeting, the BARMC received a Board Audit submission issued by the CFO and Mr Belcher, recommending that the Board approve the financial statements of CNP and CER for the year ended 30 June 2007; and a management representation letter dated 5 September 2007 signed by the CEO, the CFO and Mr Belcher. Further, at 10.30 am on Tuesday, 4 September 2007, Ms Hourigan sent an email to the non-executive directors attaching a copy of the draft concise financial reports of CNP for the year ended 30 June 2007. Later that day, Ms Hourigan was provided with the draft concise financial reports of CER for the year ended 30 June 2007, for forwarding to the directors. Whilst she cannot remember specifically, Ms Hourigan believes she would have forwarded the draft concise financial reports of CER to the non-executive directors in the ordinary course, and I accept this occurred. In any event, there is no dispute that the concise financial statements for the relevant entities were distributed to the directors. In addition, in accordance with ordinary practice, the full financial statements for CNP and CER were available at the Glen for review prior to the meeting.
3. The company secretary, Elizabeth Hourigan, again took handwritten notes during the course of the meeting. I again accept her notes as giving a sound basis for determining what occurred at the meeting. It is apparent from her notes that the following events occurred at this meeting. The CFO presented his accounting issues paper (relating to the unlisted entities). There followed another detailed exchange between the members of the BARMC, the CEO, the CFO and Mr Fekete and Mr Cougle, about various accounting issues relating to the unlisted entities. The discussion then turned to the listed entities. Mr Kavourakis said the audit committee should be given two to three days to review the financial statements for CNP and CER and it had not been given this time. In evidence, Mr Kavourakis explained this comment as referring to the need to fit in one’s other commitments with the approval process. He was not suggesting that there was not sufficient time to consider the financial statements. The CEO said there would be practical consequences if final amendments to the annual report were not done that day. Mr Cougle of PwC said that he could “give comfort that the auditors had signed-off on the full accounts”. Mr Hall enquired whether this included the remuneration report. Mr Cougle said yes. Finally the BARMC resolved to recommend to the Board that the financial statements of the listed entities be adopted.
4. At a joint Board meeting held on 6 September 2007, the Boards unanimously resolved to approve the full financial statements of CNP and CER. The final financial statements of CNP and CER for the year ended 30 June 2007 were signed by the Chairman and the CEO on 6 September 2007. They contained PwC’s independent audit report containing an unqualified audit opinion. The accounts contained no interest bearing liabilities in the balance sheet of CER, and $1.096 billion of current interest bearing liabilities for CNP.

## Context: New Plan Guarantees

1. On 20 April 2007, Centro Super LLC (jointly owed 50/50 by CNP and CER) acquired 100% of the issued share capital of the New Plan Excel Realty Property Trust (‘New Plan’).

### April Board Meeting – Due Diligence Committee

1. There was a meeting of the Board of CNP and CER on 29 March 2007. The Board pack for the meeting included the usual “Matters Arising” Board submission from Ms Hourigan. The paper sought the Board’s approval to take out certain funding for “Project Super”, which was the Centro code name for the New Plan acquisition. The proposed funding which had already been negotiated by management and the banks involved two facilities. First, an Australian facility provided by JP Morgan Australia (US$1.853 billion). Secondly, a US facility provided by JP Morgan Chase Bank to the bid company secured by the New Plan assets, referred to as the “Secured Bridge Loan” (US$1.853 billion). The US loan was proposed to be used in part, to repay an existing margin loan established as part of the bid process referred to as the “Margin Facility” and certain other debt of New Plan on closing of the acquisition. The paper relevantly stated:

*The Secured Bridge Loan is, subject to the following exception, non-recourse to the Centro Properties Group and the Centro Retail Group. JP Morgan has agreed to extend a fixed amount of funds in respect of the Secured Bridge Loan, regardless of the value of the New Plan properties securing the Secured Bridge Loan, in order to ensure that adequate funds are available to repay the Margin Facility and the other applicable debt of New Plan. Notwithstanding that agreement, JP Morgan has underwritten the Secure Bridge Loan upon an assumption that the value of the New Plan properties securing the Secured Bridge Loan yields a loan-to-value ratio not in excess of 85% (“LTV Threshold”). As a result, JP Morgan has required Centro Properties Group provide the Secured Bridge LTV Guarantee in order to guarantee the Excess LTV Amounts (and only such amount), if any. Based on Centro’s analysis of the property values, it is not expected that this guarantee will be called upon. In addition to the extent that the Secured Bridge exceeds the LTV Threshold, this incremental amount could be funded by Centro at the Australian level to avoid JP Morgan called on the Secured Bridge LTV Guarantee. The Secured Bridge LTV Guarantee may be a single document or may consist of separate guarantee documents.*

1. The Board pack for the meeting also contained a Board submission from the CEO and Mr Hutchinson dated 29 March 2007. The paper contained an overview of the proposed funding arrangements for the New Plan acquisition. In particular, the paper indicated that funding was proposed in the following stages:

#### Stage 1: Execution of the Merger Agreement (US$3,717 million)

Management established Centro’s capacity to fund the acquisition of all stock outstanding in New Plan by the provision of commitment letters for Bridge Funding, both in the US and Australia from JP Morgan. The Bridges remain as follows:

* US (US$1,853 million) – Loan to US Bid Vehicle secured against the equity of the New Plan; and
* Domestic (US$1,863 million/A$2,358 million) – Unsecured bridge loan to Centro.

#### Stage 2: Close of the Tender Process/Immediate Post Acquisition Funding – JP Morgan US Bridge (US$3,714 million)

Upon acquisition, it is contemplated that a JP Morgan US Bridge (up to US$3,714 million) will be drawn and applied to retire the margin loan to the US Bid Vehicle (US$1,853 million), meet transaction costs and, subject to consultation with New Plan management, potentially repay assumed New Plan debt (including convertible notes, unsecured bonds and back facilities).

#### Stage 3: Take-Out (Longer Term) Funding

US Bridge – The final profile of the long term debt funding of the vehicle and US bridge (US$3,714 million) take out to be finalized over the course of the next few months to ensure the best outcome taking into consideration the views of the New Plan management, immediately post closing.

Domestic Bridge (US$1,853 million) – Prior to the expiry of the JP Morgan domestic bridge funding in nine months, the following “take-out” options are contemplated:

* Various Equity Sources (US$942 million) – To date US$389 million (equivalent) has been raised through the CNP and CER placements and the CER institutional entitlement issue. A further US$553 million is contemplated though the issue of the Exchangeable Notes by CNP; and
* Domestic Bridge Facilities – New Bridge facilities provided by Centro’s Australian relationship banks (up to US$922 million equivalent). The amount of drawn debt funding required from the relationship banking group may be reduced should the Exchangeable Note Offer into CER proceed and/or to the extent that equity sell-downs are achieved.

1. At the meeting, the Board of CNP resolved to approve the establishment of a new managed fund and a due diligence committee in respect of the New Plan acquisition.

### May Board Meeting – Update on Long Term Funding

1. There was another meeting of the Board of CNP and CER on 3 May 2007. For this meeting, the Board received a Board Submission from the CEO and Mr Hutchinson dated 27 April 2007, containing an update on the “take-out” or long term funding for US and Domestic Bridges.

### July Circular Resolution – Guarantees / Amended US Bridge

1. The Board subsequently received a Board submission from the CFO dated 24 July 2007, entitled “Refinancing Proposal for New Plan Bridge Loan (US$1.89 billion)”. In short, the paper was seeking the directors’ approval to refinance the New Plan US Bridge loan (US$2.474 billion) with an amended JP Morgan Bridge Facility (U$790 million), new Club Bridge Loans with Centro’s other US relationship banks (US$1.1 billion) and a commercial mortgage backed security (‘CMBS’) issuance (US$750 million). In addition, the paper sought the Board’s approval to offer the following guarantees: a payment guarantee from CPL and CPTM (excluding US$140 million of JP Morgan debt); a “non-recourse carve out guarantee” for the amended JP Morgan Bridge in the same form as already provided; and a “springing guarantee” from CPL and CPTM for the Bank of America Revolving Credit Facility (US$350 million).

### August Board Meeting – Guarantees/Amended US Bridge

1. There was a meeting of the Board of CNP and CER on 2 and 3 August 2007. The Board pack for the meeting included a Board submission from the CFO dated 2 August 2007 entitled “Refinancing Proposal for New Plan Bridge Loan – Initial CMBS Issuance (US$180 million)”. The paper contained an update on the refinancing proposal for the New Plan US Bridge loan. The gist of the paper was that the proposed CMBS issuance (US$750 million) should be deferred for the “short term”, and that agreement had been reached with JP Morgan to extend the existing US Bridge, which needed Board approval. The paper also indicated that JP Morgan require a limited “springing” guarantee from CPL and CPTM.
2. At the meeting, the Board resolved, inter alia, to approve the execution by CPL and CPTM of the following documents:

* one or more loan agreements and amended and restated loan agreements evidencing a loan or loans in an aggregate amount of up to US$2.6 billion (‘Bridge Loan’) each between Super LLC and one or more of JP Morgan, Wachovia Bank, RBS, Key Bank Association and Bank of America;
* one or more payment guarantee agreements granted by each of CPL and CPTM in favour of the proposed financiers with respect to an aggregate of approximately US$1.754 billion of the principal amount of the loans;
* one or more non-recourse carveout guarantee agreements granted by each of CPL and CPTM in favour of one or more of the proposed financiers, pursuant to which each company guarantees the liabilities arising as a result of typical carveouts to the non-recourse liability of Super LLC under the loan agreements;
* a “springing” guarantee agreement granted by each of CPL and CPTM in favour of Bank of America NA in connection with the amended and restated US$350 million Centro NP LLC Revolving Credit Agreement; and
* a limited “springing guarantee” granted by each of CPL and CPTM in favour of JP Morgan in connection with the Bridge Loan, the “springing guarantee” to apply only if the consummation of the CMBS loans, or the proceeds of such loans, are insufficient to repay JP Morgan in the amount of US$843 million.

1. The guarantees referred to in the preceding paragraph are the guarantees relied on by ASIC in its amended statement of claim.

# VERSIONS OF THE ACCOUNTS

1. The full financial statements of CNP and CER are dated 6 September 2007. The concise financial statements of CPL, CPT and CRL are also dated 6 September 2007. It is clear that:
   * + 1. drafting and consideration of the full financial statements of CPL continued up to and after the accounts were signed by Mr Healey on 6 September 2007; and
       2. there are differences between the notes in the full financial statements of CPL as compared with the CPL concise financial statements.
2. The directors contended that having regard to the changes and versions of the accounts it was not possible on the *Bringinshaw* standard to draw inferences regarding the content of the version of the full financial statements of CNP inspected by the BARMC members prior to the meeting on 6 September 2007.

## Differences between versions of the full financial statements

1. ASIC’s pleading relates to the contents of the “CPL 2007 Accounts”, the “CPT 2007 Accounts” and the “CRT 2007 Accounts” (paragraphs 25 and 38 of the amended statement of claim). Each of these defined terms refers to the consolidated accounts of CPL, CPT and CRT (and their controlled entities), referred to as “full financial statements”.
2. The full financial statements of CPL and its controlled entities filed with ASIC relevantly specified a figure of $1,096,936 in current interest bearing liabilities, with a reference to note 18. Note 18 relevantly contained the following sentence:

*In the Appendix 4E issued on 9 August 2007 all interest bearing liabilities were classified as non-current.*

1. The full financial statements of CPT and its controlled entities filed with ASIC relevantly specified a figure of $1,096,936 in current interest bearing liabilities, with a reference to note 16. Note 16 did not contain any reference to the Appendix 4E.

## Differences in the concise financial statements

1. As I have already indicated, on 4 September 2007, Ms Hourigan emailed the “current version” of the CPL consolidated financial statements to the Board. Her email attached the concise financial statements of CPL (with no note 18). The document apparently attached to Ms Hourigan’s email on 4 September contained a signed directors’ declaration dated 6 September 2007 and a signed audit report also apparently dated 6 September 2007. Ms Hourigan received and distributed an equivalent document in relation to CER just after 5.30 pm on 4 September 2007. This document also contained a signed directors’ declaration dated 6 September 2007 and a signed audit report dated 6 September 2007. The electronic signatures were used by Centro staff to prepare these printer’s proofs prior to the meeting of the BARMC on 5 September 2007 and the meeting of the Board on 6 September 2007.

## PwC versions of the full financial statements

1. PwC had at least seven versions of the full financial statements of CNP as follows:
   * + 1. Draft #1, dated 24 August 2007 — this version had 6 September 2007 pre-printed as the date of the directors’ declaration. It included a handwritten note stating “[c]hanges discussed with client 30/8/07”. It also included a handwritten notation recording the proposed reclassification of the JP Morgan facility to current liabilities;
       2. Draft #2, dated 1 September 2007 — this version contained the figure of $1.1 billion for interest bearing current liabilities but did not contain any reference to the Appendix 4E in note 18;
       3. Draft #3, which is undated (although PwC’s electronic audit file includes a step document in relation to Draft #3 which was completed by Angela Evans on 5 September 2007) — this version had a section for current interest bearing liabilities inserted in note 18, but does not contain any reference to the Appendix 4E;
       4. Draft #4, emailed from Brad Duggan of PwC to Margot le Bars of PwC at 1.04 pm on 5 September 2007, which was after the BARMC meeting commenced at 9 am on that day — this version did not contain the one or two sentences in note 18 referring to the Appendix 4E and re-financing;
       5. Another Draft #4, undated (although PwC’s electronic audit file includes a step document in relation to Draft #4 which appears to have been completed by Angela Evans on 7 September 2007) —contained the first sentence of note 18 which was found in the full financial statements of CPL filed with ASIC;
       6. Draft #5, undated (although PwC’s electronic audit file includes a step document in relation to Draft #5 which was completed by Angela Evans on 7 September — this version contained a handwritten note adding the second sentence to note 18, which did not appear in the accounts as lodged with ASIC; and
       7. Draft #6, which is undated on its face, but appears to be the version emailed by Angela Evans of PwC to Joanne Khoo of Centro at 7.42 am on 20 September 2007 — this version again contained both sentences of note 18.

## Version made available to BARMC members

1. It was submitted by the non-executive directors that there was no evidence whether PwC’s Drafts #1, #2 and #3 were provided to Centro. There was no evidence of what versions of the full financial statements were made available to directors in the room at the Glen prior to the BARMC meeting, and prior to the approval of the full financial statements on 6 September 2007. It was submitted by the directors that the only findings that can be made with any certainty are as follows:
   * + 1. that the version of the full financial statements available immediately prior to the BARMC meeting on 5 September 2007 was not the final version of the full financial statements of CPL filed with ASIC; and
       2. that no-one told the non-executive directors that the versions available prior to the BARMC meeting on 5 September 2007 had changed (if in fact they had) by the time the Board met on 6 September 2007, or that changes were still being made to the accounts after 6 September 2007.
2. By the time the BARMC met at 9 am on 5 September 2007, Brad Duggan had not yet sent his emailed version of Draft #4 — that occurred at 1.04 pm that day. When Mr Duggan sent his version of Draft #4 at 1.04 pm, it did not contain any reference to the Appendix 4E in note 18. Given the time at which Mr Duggan sent his Draft #4, the version which was available to the BARMC in the meeting room at the Glen prior to the 5 September 2007 meeting, was probably not the final version of the full financial statements of CPL filed with ASIC.
3. The only evidence suggesting the point at which the reference in note 18 to Appendix 4E was first added to the CPL full financial statements is the date of PwC’s record regarding the Draft #4 (the second version of which contained the first sentence), and those records indicate a date of 7 September 2007.
4. In light of the evidence, there is considerable uncertainty about precisely what was available for review and what was contained in the full accounts at the time Mr Healey signed the relevant pages. As Mr Healey had not read what he signed on 6 September 2007, he cannot confirm what was contained in the document he did sign. Therefore, Mr Healey’s evidence cannot be taken to verify the presence or absence of any figure or note from the version available on 6 September 2007 or signed by him on that day.
5. It seems to me that on this evidence it can be concluded, at least, that the information in version Draft #4 of the accounts, emailed on 5 September 2007, which was before the directors on 6 September 2007, included the current interest bearing liabilities in the balance sheet and note 18 (but without the reference to the Appendix 4E). This seems to be accepted by ASIC, as they do not contend that the reference to Appendix 4E was in note 18 when the non-executive directors approved the accounts of CPL.

## Final Full Financial Statements of CER

1. The evidence of Mr Belcher as to the final full and concise financial statements of CER that were prepared for and available to the BARMC and the Board at the meetings on 5 and 6 September 2007 was as follows:
   * + 1. the final financial statements for CNP and CER (CPL, CPT, CRL and CRT) would have been completed prior to the BARMC meeting on 5 September 2007, but he understood there were some cosmetic changes made at the request of PwC after that;
       2. the full final financial statements would have been ready not long before the meeting; and
       3. all the financial statements (both full and concise) were placed in a room at the Glen available for review.
2. There was a balance sheet of CRT and its controlled entities included in the audit committee pack sent out on 31 August 2007. It was identical to the balance sheet in the final signed accounts of CER, as lodged with ASIC.
3. It is likely that Ms Hourigan sent a printer’s proof of the CER concise financial report to the directors on 4 September 2007. I find that the balance sheet in this report is in the same form as the final concise balance sheet in the CER annual report.
4. I note also that each of the members of the BARMC have said that they read CER’s full financial report at the Glen on one of 2, 3 or 4 September 2007. In the absence of any evidence of any change to the balance sheet throughout the relevant period, I can more readily conclude that the full financial accounts of CER available to be read on those days were in the same form as those ultimately filed with ASIC and relied upon by ASIC in these proceedings.

# CURRENT AND NON-CURRENT LIABILITIES

1. I now deal further with the question of current and non-current liabilities, and the position taken by the directors. It is useful to recall the relevant accounting standards.

## 2007 Accounting Standards

1. For the financial year ending 30 June 2007, the classification of current and non-current liabilities was governed by AASB 101 (Presentation of Financial Statements). Under the heading “Current/Non-current distinction”, paragraph 51 of AASB 101 provided that an entity:

*shall present current and non-current assets, and current and non-current liabilities, as separate classifications on the face of its balance sheet … except when a presentation based on liquidity provides information that is reliable and is more relevant. When that exception applies, all assets and liabilities shall be presented broadly in order of liquidity.*

1. According to paragraph 60 of AASB 101:

*A liability “shall be classified as current” when it satisfies any of the following criteria:*

*(a) it is expected to be settled in the entity’s normal operating cycle;*

*(b) it is held primarily for the purpose being traded;*

*(c) it is due to be settled within twelve months after the reporting date; or*

*(d) the entity does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting date.*

*All other liabilities shall be classified as non-current.*

1. Paragraphs 61 to 67 contained further explanation of the classification of current liabilities.
2. Paragraphs 63 and 64 provide that:

*63. An entity classifies its financial liabilities as current when they are due to be settled within twelve months after the reporting date, even if:*

*(a) the original term was for a period longer than twelve months; and*

*(b) an agreement to refinance, or to reschedule payments, on a long-term basis is completed after the reporting date and before the financial report is authorised for issue.*

*64. If an entity expects, and has the discretion, to refinance or roll over an obligation for at least twelve months after the reporting date under an existing loan facility, it classified the obligation as non-current, even if it would otherwise be due within a shorter period. However, when refinancing or rolling over the obligation is not at the discretion of the entity (for example, there is no agreement to refinance), the potential to refinance is not considered and the obligation is classified as current.*

## The former Accounting Standards

1. Prior to the introduction of AASB 101, AASB 1040 (Statement of Financial Position) governed the distinction between current and non-current liabilities. The main features of that standard (as set out at p 5 of the standard) were as follows:

*This Standard:*

*(a) requires current assets and current liabilities to be presented separately from non-current assets and non-current liabilities unless presenting assets and liabilities in the broad order of their liquidity provides more relevant and reliable information*

*(b) defines a current asset as one that is expected to be realised within twelve months of the reporting date or in the normal course of the entity’s operating cycle or that is held primarily for trading purposes or that is cash or a cash -equivalent asset*

*(c) defines a current liability as one that is expected to be settled within twelve months of the reporting date or in the normal course of the entity’s operating cycle*

*(d) requires that a long-term interest-bearing liability that becomes due within twelve months of the reporting date continue to be classified as non-current when the entity has agreed to refinance the obligation on a long-term basis...*

1. Current liabilities were described at paragraph 4.4(b) of AASB 1040 as “those liabilities arising and *expected to be settled in the normal course of the entity’s operating cycle*”. The standard went on to prescribe that the default position was to classify liabilities as non-current, if specific criteria were not met. Paragraph 4.5(b) of AASB 1040 provided that long-term interest-bearing liabilities had to be categorised as non-current, even if they were due to be settled within twelve months of the reporting date when “the original term was for a period of more than twelve months” and “the entity is committed to an agreement to refinance, or to reschedule payments, prior to the *time of completion* of the financial report”.
2. Under the old GAAP definition, a debt could be classified as non-current even if it fell due within 12 months of the balance date provided the entity “expected” that settlement of the debt would be extended beyond that date.
3. Mr Fekete explained the application of the old standard as follows:

*That is that you look at the substance of the thing and you ask yourself whether you expect to have to pay this debt out of your own money within the next 12 months and, if the answer is yes, it’s current. If the answer is expected to be no, it’s non-current.*

*That’s the way the industry interpreted it, isn’t it? That’s my belief. Yes, it is.*

1. It was submitted by the directors that there was a lack of proper understanding of the significance of the change in the standards on the part of Centro’s independent auditors and other experts.
2. Angela Evans, an employee of PwC, was working on the audit of Centro. Ms Evans corresponded by email with Richard Gore of Centro. In the process of finalising the full financial statements of CNP, Mr Gore sent an email to Ms Evans on 18 August 2007. Mr Gore provided responses to an “open items list”, prepared by PwC, which considered whether material could be produced to show that the JP Morgan facilities could be extended beyond 6 September 2007. The question of whether a facility can be extended after the balance date, but before the reporting date, is a highly relevant enquiry under the old standard, but is quite irrelevant under the new standard. The evidence seems to indicate that both Mr Gore and Ms Evans were operating under the old standard.
3. There is also evidence that all of the big four accounting firms, to varying degrees, misunderstood or failed to appreciate the significance of the changes to the classification of current and non-current liabilities brought about by the introduction of AIFRS. This led to the submission by the non-executive directors that ASIC brings this case on the explicit basis that classification issues were simple and the directors should have had knowledge of the standards such that they should be able to identify, when competent experts have not, that the accounts of CNP and CER misclassified certain liabilities.

## Transition to AIFRS and the Centro accounting policy manual

1. The directors also relied upon problems arising in the transition to the new accounting standards and errors in the Centro accounting policy manual.
2. Centro established a project team to manage the transition to AIFRS.
3. The BARMC was provided with updates as to the progress of the work being performed by the AIFRS project team which was being assisted by PwC. In particular, for the meeting of the BARMC held on 4 August 2005, attended by, amongst others, the CEO, the CFO, the directors and Mr Cougle and Mr Winter from PwC, the BARMC pack included a Board Audit submission which stated, inter alia.

*In 2004, Centro established a project team comprising senior management and PwC representatives to manage the transition to AIFRS.*

*During 2005, the AIFRS transition team has:*

*• Held weekly meetings and worked to a comprehensive timetable;*

*• Completed a detailed review of AIFRS requirements (more than 1,000 pages);*

*• Planned changes to existing processes to ensure Centro’s financial information systems will capture the information necessary to report under AIFRS in FY06;*

*• Identified areas where accounting policy changes will be required; and*

*• Quantified (where practical) the likely financial impact of accounting policy changes.”*

1. The BARMC pack for a meeting held on 2 February 2006, included an “Accounting Issues” Board Audit submission dated 27 January 2006, which reported on the progress of transition to AIFRS. The paper provided:

*As noted in previous Board Audit Committee papers, the transition to AIFRS has necessitated several changes to accounting policies. The impact of these accounting policy changes is summarised in the table below which reconciles net profit for the half year ended 31 December 2005 under AIFRS with the net profit that would have been reported under the previous accounting standards (“AGAAP”).*

*…*

*CNP’s balance sheet has also been affected by the transition to AIFRS primarily due to a “substance over form” approached being applied for the merger of CNP and the Prime Retail Group (“PRX”) whereby CNP is regarded as the acquirer under AIFRS whereas PRX was regarded as the acquirer under AGAAP. This change resulted in a reduction in goodwill from $675.7 million at 30 June 2005 under AGAAP to $306.1 million at 31 December 2005 under AIFRS.*

*To ensure that the accounting policy changes adopted by CNP and CER in transitioning to AIFRS are consistent with their peers, management has reviewed:*

*• The financial reports of peers with December year ends who have already reported under AIFRS (including Westfield and Australand);*

*• Investor presentation that have been made by several peers;*

*• The results of several surveys of the listed property trust sector.*

*Presentations were recently made to Centro investors and staff to assist them in understanding the impact of the transition to AIFRS will have on Centro’s financial information systems and the financial results of CNP, CER and Centro’s unlisted investment vehicles.*

*Significant work has also been undertaken in recent months (in consultation with PwC) compiling a comprehensive Centro group accounting policy manual that is expected to be included in draft form in the Audit Committee papers for the next month’s Board Audit Committee meeting for the Syndicates financial statements.*

1. A draft accounting policy manual was presented to the BARMC ahead of its meeting on 3 March 2006. That meeting was attended by, amongst others, the CEO, the CFO, Mr Fekete from PwC and Mr Belcher, who was at that time, employed by PwC. The BARMC pack for the meeting included a Board Audit submission from the CFO dated 24 February 2006. The paper stated, inter alia:

***Draft Centro Properties Group Accounting Policy Manual*** *– An initial draft of the Centro Properties Group Accounting Policy Manual (which has been prepared in consultation with PwC and Moore Stephens) is included in Appendix D. The Centro Properties Group Accounting Policy Manual is fully AIFRS compliant and is intended to:*

*• Provide a comprehensive summary of the accounting policies to be applied in the preparation of financial information for all group entities;*

*• Be used as a source of reference for existing employees with accounting responsibilities;*

*• Be used as an induction and training aid for new staff with accounting responsibilities and existing staff assuming new accounting responsibilities.*

1. At that meeting, the draft Centro accounting policy manual was discussed, and Mr Fekete and a Mr Neville noted that PwC and Moore Stephens appeared satisfied with the reasonableness of the position adopted by management in relation to the matters outlined in the accounting issues paper.
2. In July 2006, the Centro accounting policy manual was finalised and distributed to the Executive Committee and other Centro staff. When it was distributed it was noted that the manual had been compiled by the financial accounting and management teams in conjunction with PwC.
3. Both the draft and final Centro accounting policy manual stated:

***(iii) Other Assets and Liabilities***

*Assets and liabilities expected to be realised within a period no longer than one year must be classified as current assets [sic] in the balance sheet. All assets and liabilities expected to be held for a period of longer than a year should be classified as non-current in the balance sheet.*

1. The accounting policy manual was not AIFRS compliant. Importantly though, for the purposes of this proceeding, there is no evidence that the directors themselves relied upon the accounting policy manual. The submission of the non-executive directors was that the non-executive directors could rely upon its accuracy and could rely upon it as representing the culmination of the great deal of work done by the Centro finance department and the auditors, to ensure that the accounts produced by Centro would be fully AIFRS compliant. However, there is no evidence that any director’s understanding or lack of understanding arose because of the contents of the accounting policy manual.
2. Ahead of its meeting on 3 August 2006, the BARMC received an audit plan from PwC for 2006. The key audit issues identified in the audit plan included “AIFRS accounting policies and procedures”. The audit plan further stated that PwC’s audit objectives included:

* Independent assurance that the financial statements of Centro entities are presented fairly and in accordance with relevant accounting standards.
* Objective feedback on:

– accounting policies and practices; and

– Centro’s approach to, and disclosure of, compliance with ASX Principles of Good Corporate Governance.

* Independent assessment of Centro’s first year AIFRS implementation.
* Communicating areas of high audit risk.
* Reporting significant control weaknesses and issues in relation to financial systems.
* Providing annual independence letter and bi-annual independence declarations.

1. The audit plan for 2007, provided ahead of the BARMC’s meeting on 1 February 2007, provided assurance that PwC would ensure compliance with AIFRS and accounting standards. In the audit plan, one of the identified audit risks was a number of “accounting issues and policy matters presently under review as a result of transactions or evolving AIFRS interpretations”. The audit plan further stated that PwC’s audit objectives included:

* Independent assurance that the financial statements of Centro entities are presented fairly and in accordance with relevant accounting standards.
* Objective feedback on:

– accounting policies and practices; and

– Centro’s approach to, and disclosure of, compliance with ASX Principles of Good Corporate Governance.

* Independent assessment of Centro’s first year AIFRS implementation.
* Communicating areas of high audit risk.
* Reporting significant control weaknesses and issues in relation to financial systems.
* Providing annual independence letter and bi-annual independence declarations.

1. Around 5 July 2007, PwC issued an updated audit plan for 2007. The updated audit plan updated the risk analysis and also included a number of accounting issues and policy matters which were said to be presently under review as a result of transactions or evolving AIFRS interpretations. PwC’s planned response was to address those issues in “technical papers” which would be reported to the Board. PwC recorded as the “Action taken to date” that it had “finalized a number of accounting issues in technical papers provided to Centro Australia management.”
2. I accept that the non-executive directors reasonably expected that accounts produced by the accounting staff of the Centro Group would comply with AIFRS standards and that, if they did not for any reason comply, PwC or Centro’s accounting staff would identify the error. The non-executive directors equally had no reason to expect that the staff of its independent expert auditors, PwC, would also fail to appreciate the significance of any changes to the relevant standards. In this proceeding, ASIC has not criticised the processes and procedures of the Centro Group or suggested that any “red flags” ought to have alerted the directors to deficiencies in the processes or personnel of Centro or its auditors.
3. The directors also submitted that there was some lack of clarity surrounding the new standard.
4. Mr Belcher stated that the accounting profession was still “grappling with what AIFRS entailed” in mid 2007. Mr Fekete explained that the application of the new AIFRS standard in 2007 was not “necessarily black and white”. However, this comment was not so much as to the interpretation of the standard. He said that in order to apply the classification of Centro’s finance facilities under the new AIFRS standard you would need to look at the loan documentation and the correspondence between Centro and the banks to determine whether there was a contractual entitlement to extend the facility.
5. The directors then made the followings submissions:

* Even when the issue of possible misclassification came to light in early 2008, the classification of Centro’s debt facilities under the AIFRS standard was considered by management and PwC to be a complicated question. Mr Belcher gave evidence that there were “areas of greyness” being discussed at the time between PwC and management, and that PwC were keen to explore the “greyness” of the classification. Mr Belcher said that, while the Board wanted an early resolution of the issue, PwC was reluctant to review its work. Mr Fekete gave evidence that Ivan St Clair told the Board in January 2008 that the classification of liabilities was a “grey area”, and Mr Fekete said he used words to similar effect at the time. It took more than a month before management was prepared to recommend to the Board that the debts should be reclassified. Ivan St Clair, who was a partner of Ernst & Young acting as CFO while Mr Nenna was unwell, found the issue difficult. On 11 January 2008, Mr St Clair was of the view that the existing disclosure was incorrect, but by the next day, he had changed his mind and was convinced that a significant portion of the debt with a maturity date expiring within 12 months from June 2007 was non-current. He changed his mind again before the corrections were announced to the market on 15 February 2008.
* To know that a facility, when entered into, had a particular expiry or maturity date is only the start of the enquiry as to classification in view of Centro’s business practices and history of having no current interest bearing liabilities. As Mr Cronin put it, it would only be an “indicator” that a debt was current. To actually form a view as to the proper classification of any facility in circumstances where the disclosing entity regularly extended, rolled over and refinanced debt, it would be necessary to examine the facility agreements and consider any negotiations. Without proper enquiry into those negotiations and other circumstances, the maturity date is apt to mislead as to whether the debt is a current liability. Mr Fekete also explained that he would need to see not only the loan agreements, but also correspondence passing between the company and the bank, and speak to the CFO to determine what discussions had been had with the bankers. Working out the correct classification of the facilities was not a task that PwC thought it could accomplish in 48 hours.
* It should be noted that the facility agreements in question are not one page term sheets. Rather, they are complex legal instruments. Some aspects of this complexity emerged in the evidence of Mr Scott. He explained that there was “an 18 month extension right within the document, but in finance terms as I use it and as I thought it was used in this document that would have been a renegotiation or refinancing opportunity, that even though there was a right to extend at a higher margin, it’s not expected that you would use that; you would actually then extend the maturity or renegotiate it.” The existence of such embedded rights to extend (albeit at a high cost and which Mr Scott did not anticipate would be utilised) may go some way to explaining why, when PwC reclassified the JP Morgan domestic bridge of $1.1 billion, it regarded the other facilities as “open-ended” or “evergreen” and correctly classified as non-current. PwC’s view at the time that the other debts were classified as non-current was formed notwithstanding that:
  + - 1. PwC clearly reviewed the minutes of the meeting of the Board on 3 June 2007 at which approval was given for the amendment or extension of various facilities; and
      2. PwC received bank confirmations which recorded maturity dates within 12 months of 30 June 2007.
* Nor should it be supposed that note 1(w) recorded everything one might need to know about the accounting standards. The accounting standards contain three levels: the standard, guidance, and “basis for conclusions”, which comes out of the international framework, but is not reproduced with in the standards. The summary of accounting policies contained in the financial reports does not and cannot purport to be a comprehensive statement of the accounting standards which ultimately govern the financial reports.

1. I do not accept these submissions have any significance to this stage of this proceeding. First, there is no evidence that the transition phase (which probably was over by June 2007 in any event) was a cause or a contributing factor to the directors’ actions in this proceeding. They did not say it was, and there is no evidence to connect any lack of clarity or uncertainty in the minds of third parties to the directors.
2. As Mr Hullah said in relation to the classification of the debt, the plain English of note 1(w) was clear, which reflected the relevant standard. No director needed to be apprised of the changes made in the standards; he just needed to understand and apply the standard applicable in 2007, which on its terms was straightforward. Mr Scott did display some confusion over his understanding of ‘current liability’, and believed it was a complicated area. However, he had read note 1(w), and whilst he believed it was a summary, did not have any difficulty understanding its plain meaning. All that the directors, including Mr Scott, had to know was clearly stated in note 1(w), which they either read or should have read and understood.
3. Secondly, the fact that there was a lengthy period, or explanation of “greyness” in the classification in late 2007 and early 2008, does not indicate that any problem lay in understanding the accounting standard or applying it. Undoubtedly, when difficulties arose in late 2007 and 2008, a thorough investigation took place. I would expect there to be a full and proper enquiry into the circumstances of the errors having been made, and this would involve investigating much documentation. This is not the task that ASIC seeks to place upon the directors in this proceeding.
4. Thirdly, I accept that to form a final and proper view of the correct classification may involve an investigation of the facilities themselves, and whether agreement had been reached regarding any extension, roll over or refinancing. However, this is not what is being asked of the directors in this proceeding. They must have known or at least thought simply because negotiations were taking place to refinance or extend, that the expiry or maturity date of the facilities was short-term.
5. This is all that they needed to know, along with a general or basic understanding of the classification requirement, to raise the question as to the appropriateness of the classification. The complexity of the documentation is neither here nor there on this issue – the maturity date would be apparent, and unless it had been extended, negotiations taking place were immaterial, no matter how optimistic Centro was about the future.
6. Fourthly, I accept that note 1(w) does not record everything that “one needs to know about the accounting standards”. However, it was all each director needed to know to have a sufficient knowledge of the accounting standard relating to classification so that each director would have been able to read and understand the financial statements and apply his own knowledge to that task.

# EVIDENCE RELATING TO THE DIRECTORS

1. I now turn to information and the knowledge of the directors and their evidence in addition to that to which I have already referred. Some of this evidence is relevant to the position relating to the post balance date events, a topic upon which I will return.

## Guarantees and Debt

1. Each of the directors had knowledge of the guarantees by at least the following means:
   * + 1. Each was provided by email from Ms Hourigan with Mr Nenna’s paper of 24 July 2007 in which the refinancing proposal for the New Plan US bridging loan was explained. The matter was the subject of discussion amongst the directors and the circular resolution was agreed;
       2. Each was also provided with the further paper by Mr Nenna dated 2 August 2007 in which he put forward a modified refinancing proposal which was brought about by the fact that, due to the recent disturbances in the US credit markets, it had been decided to defer the intended US$750 million CMBS issue for CER’s share of the bridging loan. The recommendations in that paper were approved and the resolutions duly recorded in the minutes;
       3. The draft minutes of the August meeting were included in the Board pack for September and the evidence of each non-executive director was that he read those draft minutes.
2. In relation to the debt position, whilst I have referred to documentation and summarised the evidence of the directors above, I make the following further observations.
3. Following the settlement of the Heritage acquisition in late 2006, there was a significant increase in CNP’s debt levels and a shortening of its maturity profile, which is illustrated by the following from the annexures to the Funding and Financial Risk Management papers for the October and November meetings:

|  |  |  |  |
| --- | --- | --- | --- |
| **Meeting Month** | **Drawn Facilities In A$** | **Facilities Maturing in < 1 year (A$)** | **Average Debt Maturity (yrs)** |
| October | 1,591,146,227 | 440,164,070 | 3.0 |
| November | 4,089,812,985 | 1,888,231,418 | 1.5 |

1. The directors were informed in the paper for the November meeting that CNP had facilities of A$1.9 billion maturing within the ensuing 12 months which it was intended to repay from the proceeds of equity sell-downs and property disposals.
2. This was a situation about which it was necessary for the directors to keep themselves informed as they in fact did. The information available to them for this purpose included the Funding and Financial Risk Management reports included in the Board packs for every meeting and the accompanying schedule of facilities. This told them the following (selected months only):

|  |  |  |  |
| --- | --- | --- | --- |
| **Meeting Month** | **Drawn Facilities In A$** | **Facilities Maturing in < 1 year (A$)** | **Average Debt Maturity (yrs)** |
| February 07 | 2,898,301,639 | 1,481,406,668 | 1.5 |
| June 07 | 4,321,729,753 | 3,410,635,789 | 1.5 |
| July 07 | 3,757,021,411 | 2,828,374,687 | 1.6 |

1. The further increase in both total and short-term debt shown in this table in June and July 2007 was attributable to the New Plan acquisition. The facilities schedule for the July meeting also contained the information that the bridging finance facility established through JP Morgan for the jointly owned bidding vehicle for this acquisition (Super LLC) stood at US$2,473,921,000. This was the debt that was subject to the refinancing proposal in connection with which the guarantees were approved.
2. In the Funding and Financial Risk Management paper for the August Meeting, Mr Nenna referred to the fact that the $1.1 billion domestic JP Morgan bridge facility established for the New Plan acquisition had a scheduled maturity date of 4 January 2008. The directors were advised that this was intended to be repaid in part from the proceeds of equity sell-downs, with any balance being replaced by a new short-term facility. The directors were also informed that management was engaged in discussions with Centro’s banks with a view to restructuring facilities so as to extend the overall average debt maturity.
3. The results of this exercise were set out in a paper included in the Board pack for the September meeting, entitled “Centro Banking Facilities Review”. In that paper, Mr Nenna informed the Board that he was providing, as an attachment to the paper, an overview of the current position, dividing the current facilities into:
   * + 1. “Core” – greater than 12 months;
       2. “Short-term” – (6-12 months); and
       3. “Immediate short-term” – less than six months.
4. The board was informed that of CNP’s total facilities of $4.43 billion, just over $2.14 billion was currently classified as immediate short-term. This included “the $1.12 billion Australian domestic bridge referred to in the last Board paper and residual ‘Heritage’ acquisition bridge facilities from ANZ and RBS (which mature on 30 September 2007).”
5. The paper went on to inform the Board about the various proposals for additional facilities and extensions which were the subject of negotiations with the banks, and upon all of which Centro was awaiting bank credit committee approval.
6. It was not suggested to the board in any of the foregoing information that CNP had any unilateral right to extend the due dates of any of its facilities. Indeed, there was no such right for any of CNP’s current liabilities, and it would have been quite inconsistent with the presentation of the facilities in the schedules provided to the Board at each meeting, and the tenor of the Banking Facilities Review paper, if any such rights had existed.
7. The position of CER was not discussed in the Funding and Financial Risk Management reports referred to above, but this subject was a standard part of the CER management report that was included in the Board pack for each meeting.
8. The directors were informed of CER’s funding position as at May 2007 by a table in the CER Strategic Business Plan, which was included in the Board pack for the June strategy meeting. In that table it was shown that CER had total domestic debt facilities of $951 million, of which $470 million was due to mature in the second half of 2007. A list of US$ debt facilities was also provided, which included one facility for US$9.5 million due to mature in June 2008. No indication was given that CER had any right to extend these maturities.
9. The CER Management reports for May and June referred to above indicated that in each case there was no change in CER’s domestic or US$ debt facilities during the month.
10. CER’s financial position was referred to in the Accounting Issues Paper presented to the August audit committee meeting, where it was said that:

*As was the case at 30 June 2006, CER's balance sheet at 30 June 2007 showed a deficiency in net current assets with its only significant current liability being a provision for distribution. CNP has committed to provide a $30 million facility to enable CER to meet its short term cash flow requirements until new facilities are established. This is anticipated to occur by September 2007.*

1. This statement was made on the incorrect footing, demonstrated in both the CER preliminary final accounts and in its 2007 financial report, that none of CER’s debt facilities were current liabilities. In fact CER had a net current asset deficiency of the order of $500 million, and for CNP itself the true figure was a deficiency of about $1.9 billion.
2. At the August audit committee meeting, Mr Hall pointed out that paragraph 25 of the management representation letter was limited to cash resources to cover working capital and capital expenditure and queried whether it should refer to debt. Mr Scott agreed that another section would be added to refer to financial obligations arising from debt funding obligations, and that there was reason to believe that these could be refinanced on a timely basis. This highlights the significance of the short-term debt position to any consideration of the ability of CNP and CER to pay their debts as and when they fell due, and reinforces the evident necessity for the directors to be aware of the extent to which the debts of both entities were maturing in the 2007-08 year and in particular in the last six months of 2007.
3. However, I make the following comments.
4. I accept the position of the non-executive directors, that in the period leading up to 6 September 2007, the information regarding the state of the economy and fundraising was fundamentally positive.
5. The advice given to the non-executive directors by Centro’s CEO and CFO would not have led the non-executive directors to hold any concerns about the Group’s ability to raise debt or equity or the realisable value of its assets. For example, at the Board meeting on 3 August 2007, the non-executive directors were told that:
   * + 1. Mr Scott advised that different markets were impacted differently;
       2. Mr Scott did not think there was a “credit crunch” and just because credit was not available at the “euphoric” rates previously enjoyed, that did not mean there was a “crunch”;
       3. Mr Nenna advised that a “tightening of standards” should be expected;
       4. Ashley Reed stated that CMBS and “RMS” perform well, but Collateralised Debt Offerings (‘CDOs’) were the problem area;
       5. Mr Kavourakis’ assessment was that credit had been cheap for some time and was getting “re-rated”; and
       6. Mr Scott noted that the Australian equity market had not closed down for reasonably priced equity raisings for 15 years and that the Australian property sector would stand up if anything happened overseas.
6. The slides to Mr Nenna’s presentation similarly presented a picture of a short-term issue of pricing impact. It noted that: real estate fundamentals remained strong; pricing was returning to historic levels; interest rate hedging would largely mitigate the impact of margin volatility; management had quantified the impact of additional financing costs at $7 million per annum; the next Australian CMBS product was “still considered viable but may experience timing delay”; liquidity issues were expected to be short-term; and management believes it has sufficiently strong relationships with its core banks to extend existing facilities until capital market demand recovers.
7. Further, at the August 2007 Board meeting, Mr Scott undertook to come back to the Board if there was a change in the position. In his evidence, Mr Scott confirmed his positive outlook on the availability of debt around September 2007. In September 2007, Mr Scott’s belief was that facilities were going to be refinanced or rolled over and that the only issue was that margins might have been a bit higher. In Mr Scott’s assessment, it was not until December 2007 and into January 2008 that the Global Financial Crisis (‘GFC’) was “starting to hit” and that it “did hit” in 2008 and 2009.
8. The Banking Facilities Review paper, which formed part of the Board pack for the Board’s meeting in September 2007, similarly reported positively on negotiations to refinance various of CNP’s facilities. The discussion at the September 2007 Board meeting was again positive about the company’s progress in arranging re-financing. As Mr Scott stated in his evidence, debt had been readily available “almost on nothing” for 15 years, and he was not focused on the recording of current versus non-current liabilities. At the Board meeting in September 2007, the Board was told by Mr Nenna that the banks were “obliging re extending short-term facilities” and detailed the level of accommodation of different banks. Mr Nenna also detailed the visit that ANZ and NAB had taken to the US, at which they were accompanied by Mr Reed (of Centro’s finance department), they were taken around by Mr Rufrano of New Plan and were “very impressed”. The Board was told by Mr Nenna that “all banks on the sheet are at the in principle agreement stage” and all banks were in the “process of getting credit approval”, at which stage lenders were not expected to “fall off”. Indicative of the situation at that time was that another lender, Westpac, was “very keen to come back in”. The “one caution” of which the Board were advised was that interest rates were increasing.
9. As was the case with the August 2007 Board meeting, there was nothing said in the September 2007 Board meeting which ought to have raised concerns any further on the part of the directors regarding the management of maturing facilities and management’s program to roll over, extend or refinance maturing facilities.
10. Each of the non-executive directors has given evidence that he did understand that CNP had substantial short-term liabilities due to mature before 30 June 2008 and that CER had some debt facilities due to mature in 2008. However, I accept this understanding in the context of:
    * + 1. Centro’s long and consistent history of rolling over or extending its finance facilities;
        2. the positive information the non-executive directors were given at the August and September 2007 Board meetings by the CFO and CEO as to Centro’s ability to re-finance those short-term or maturing liabilities.
11. I now turn to some specific evidence and admissions of the directors as to the debt position.

### Mr Healey:

* + - 1. as with the other non-executive directors, did not admit knowledge of the debt position of CNP or CER in his pleading;
      2. read the CEO’s Management Report in Section C of the Board papers carefully, and other papers within his area of expertise (property and funds management performance, corporate governance etc) and read the remainder of the papers in section C in less detail (eg funding and financial risk management) and said that he would generally scan any attachments or annexures to these papers;
      3. followed this practice in reading the several board and BARMC packs (and the July circular resolution);
      4. would not have read attachments to Board papers, but would have expected the more financially literate members of Board to examine schedules more closely;
      5. knew the Funding and Financial Risk Management submission was provided at every board meeting from 2005 to 2007;
      6. knew in 2007 that the New Plan acquisition was to be funded with large amounts of bridging finance which was to be re-financed through a range of measures in 2007;
      7. if he had read the finance facility schedule of the March 2007 Funding and Financial Risk submission he could have determined how much of the debt in the schedule was (short-term) CNP debt but doubted he would have looked at the attachment (Finance Facility Schedule);
      8. knew that as at the end of the 2007 financial year, CNP had short-term debt of close to $2.5 billion that had to be financed within 12 months of the balance date;
      9. knew that CER had around $400-$500 million dollars of debt maturing within 12 months;
      10. in relation to the July Funding and Financial Risk Management submission did not ‘specifically refer to it’ at the July Board meeting but agreed that had he done so he would have seen that the facilities maturing in less than one year were $2.828 billion;
      11. in relation to the August Funding and Financial Risk Management submission, of the drawn facilities totalling $3.453 billion, $2.438 billion was due in under 12 months, and with regard to the average debt maturity of 3.6 years, agreed that if he had read this it would have alerted him to the fact that there was a much larger figure due in a short period than the average maturity indicated; Mr Healey stated that despite this he would not have treated that fact as significant because he expected the short-term facilities to be renewed before they matured;
      12. knew at the time of the August Board meeting (when the CNP Appendix 4E was to be approved) that there were debts that had to settled within 12 months;
      13. knew of CNP’s short-term debt of $2-2.5 billion, and knew ‘broadly speaking’ that current liabilities must be paid within 12 months. He had read the balance sheet, and saw no line for current debt but did not make the connection;
      14. did not ‘pick and choose’ what to read in the papers, but would read in more detail the sections that he felt were very important to him as chairman, for example the CEO’s report;
      15. read the first section of the Board papers that contained decision papers more carefully;
      16. was familiar with and would read the funding and financial risk management submission, but only scan the attachments;
      17. would look at the attachments if specific reference was made to one of them, but expected that the directors with specific expertise would take a greater interest in those sections;
      18. If there was no reference to the schedule of finance facilities that was attached to that submission in the body of the paper, or any reference to it by management, he would not read that attachment in any detail;
      19. agreed that one would have to read attachments to the Board papers thoroughly to understand them, but did not think it was something that he was obliged to do;
      20. did not fully understand the basis for calculation of ‘core debt’ or how it related to short-term debt;
      21. was aware of Centro’s significant debt but believed that Centro would be able to repay the debt as it had done in previous years;
      22. believed that the debt should be monitored and was being monitored.

### Mr Scott :

* + - 1. made admission in his defence that he received the various Board papers referred to in the amended statement of claim, attended the meetings referred to, and thereby had been informed of the matters the subject of those Board papers and resolutions and that the information so provided was to the effect that the maturity dates of the various borrowing facilities (which did not include the Bank SA facility) was in the 12 month period post 20 June 2007;
      2. was generally aware of the level of debt of CNP and CER as disclosed in their respective strategic business plans;
      3. as at August 2007 knew there were a number of debt liabilities maturing within 12 months of 30 June 2007 and that these included the JP Morgan domestic bridge of $1.1 billion;
      4. was aware of the Centro facilities schedules, and knew that unless they were refinanced they would have to be repaid.

### Mr Kavourakis:

* + - 1. did not admit knowledge of the debt position of CNP or CER in his pleading;
      2. said in his practice was to read all of the Board papers prior to the meeting and generally to scan the attachments;
      3. stated that he followed this practice for the June, July, August and September Board meetings in 2007;
      4. stated that his practice was to read all of the BARMC papers prior to the relevant meeting;
      5. stated that he followed this practice for the BARMC meetings in July, August and September 2007;
      6. said that he was aware that from November 2006 onwards there was an elevated level of debt due to the Heritage and New Plan transactions, and that was something he would be monitoring, and keeping himself informed about the amount of the debt and the maturity profile of the debt;
      7. agreed that he had no knowledge in July or August 2007 of any right that CNP had to extend any of its facilities;
      8. confirmed that he had no other knowledge in September 2007, apart from that contained in Mr Nenna’s finance facilities paper (which identified a whole range of agreements and proposed agreements subject to credit committee approval) which would change that position;
      9. agreed that he should have known in June 2007 that CER had debt facilities of $470 million (being approximately 50% of its borrowings) maturing in financial year 2007/08 but does not now recall whether he did know that;
      10. agreed that he was aware in early September 2007 that CER had liabilities at 30 June 2007 that were under facilities maturing in the 12 months following that date which, if not refinanced, would be required to be repaid in the amount of $500 million.

### Mr Hall:

* + - 1. kept himself informed about the amount of debt of CNP by reading the Board papers every month;
      2. agreed there was a funding and financial risk management report every month for information. If there was a regular attachment to a regular Board paper that he found useful, and it had valuable information, he would probably look at it. Mr Hall also agreed that if there was some strong point in the Board paper that took him to the need to go to the annexures to understand the point or to validate it he would look at it;
      3. read the CER business plan review. He would have seen from reading page 160 that about half of the CER domestic debt facilities had a commercial maturity with the financial year 2007/2008;
      4. could not recall if he was aware at the start of July 2007 of the actual approximate amount of total borrowings and did not think he was aware of the amount of borrowing facilities of CNP that were maturing in 12 months;
      5. knew at the time that one of the things he had to do as director in the course of the finalisation of the annual accounts was to form an opinion about whether the company could pay its debts as and when they fell due. As a part of this it was necessary to know the total amount of debt the company was carrying, and what was maturing in the short-term (in the context of being able to meet the obligations or seek to have them rolled over);
      6. read the banking facilities September 2007 review paper before the board meeting. Where the paper refers to facilities which were classified as immediate short-term, he understood that these were facilities which if not rolled over or extended or refinanced with that bank would be required to be repaid. He understood those facilities categorised as short-term, six to 12 months, were facilities which if not agreed to be rolled over or refinanced with that bank would also be required to be repaid. If there was no rollover they would mature on a date and that is when they would need to be paid.

### Mr Cooper:

* + - 1. At all relevant times between June and September 2007, Mr Cooper knew in general terms of the debts of CNP and CER that were due to mature within 12 months of the balance date;
      2. in June 2007 he knew that the CNP Strategic Business Plan revealed debt maturing within 12 months of the balance date in an amount in excess of $2 billion;
      3. in June 2007 he knew that the CER Strategic Business Plan revealed debt of CER in the order of $470 million maturing within 12 months of the balance date;
      4. in relation to the July finance facilities schedule did not think he enquired as to whether the maturity dates specified in the right hand column were other than dates upon which the facility expired, did not turn his mind to it;
      5. made no enquiries at the Board meetings about whether facilities expiring in less than one year were able to be extended or rolled over;
      6. in August 2007 when reviewing the CNP Appendix 4E, knew there were facilities that were described as falling due or maturing within the year in the relevant schedule in the order of $2.5 billion.

### Mr Goldie:

* + - 1. at all relevant times between June and September 2007, Mr Goldie knew in general terms of the debts of CNP and CER that were due to mature within 12 months of the balance date -
         1. in August and September 2007 he knew that CNP had short-term debts in the order of $2.5 billion or at least that were substantial; and
         2. in August 2007 he knew that CER had short-term debts in the order of $.5 billion;
      2. knew that guarantees involved or included a guarantee by CNP of $1.75 billion of the US New Plan debt.

### Mr Wilkinson:

* + - 1. was aware that there was a funding and financial risk management paper in the Board pack every month and it was his practice to read some part of the pack documents and scan the remainder of the material. Scanning would involve reading the main body of the document and seldom if ever referring to the attachments;
      2. read in full sections A and B of the pack, then worked his way through section C, reading the reports that particularly interested him, such as the property-related ones and the CEO’s report, and then when he came to this report he might have a quick look at it or he might read it more carefully;
      3. was aware at the June 2007 Board meeting that CNP and CER had recently acquired New Plan for about US$4 billion, a large part of which was raised by way of short-term bridging finance arranged through JP Morgan and that broadly speaking this had increased Centro’s gearing levels to historically high levels;
      4. was aware broadly that about $2.6 billion was under facilities that were to mature in the next financial year and that this is high figure;
      5. could not say for certain whether he read the table of CER’s domestic debt facilities as at May 2007 but there was a reasonable chance he did, and broadly speaking it would tell him about the extent CER’s debt and maturity;
      6. was aware that when reference was made to maturity it meant that the debt drawn down on that facility had to be repaid unless it was rolled over or extended;
      7. was aware broadly that unless and until the facilities were extended, they would have to be repaid. He thought it would have been drawn to the attention of the Board if Centro had some unilateral right to extend the facilities anyway.

## **Directors’ knowledge of the requirements of the Act and accounting matters**

1. I now turn to the evidence of the directors as to the requirements of the Act and the accounting matters.

### Mr Healey

* + - 1. he was accustomed to dealing with balance sheets and profit and loss statements, and could read and understand them;
      2. he generally understood conventional accounting concepts, including that liabilities in balance sheets are classified as current or non-current;
      3. he understood, in August and September 2007, that the period for determining whether a liability was current was that it had to be satisfied or repaid in less than 12 months, but he had no real understanding of accounting standards requirements for current and non-current liabilities;
      4. he did not understand that a current liability generally meant a financial obligation which must be paid or satisfied within 12 months of the balance date;
      5. he cannot say for certain that he never read note 1(w) before it was drawn to his attention after the calendar year 2007 during the reclassification. He also said that he was unclear about what note 1(w) says, he could not say he never read it but did not recall it being significant in his mind;
      6. he was aware that in signing the financial statements that he had certain duties under the Actbut could not give details (because he was out of date and not familiar with them);
      7. he was unable to say what he was required under the Act to do in 2007, and relied on advice from management, the auditors and the audit committee;
      8. he said in relation to post balance date events, that he would rely on advice as to whether it should be in the statements.

### Mr Scott

1. Mr Scott knew the conventional classification of liabilities into current and non-current. By the time of approval of the financial statements in September 2007 he had been dealing with the financial statements of the Centro group of companies for 10 years, and with financial statements of other companies and had built up a thorough understanding sufficient to enable him to read and understand them.
2. As I have already indicated, in relation to his knowledge of the definition of a current liability, Mr Scott in giving evidence seemed confused. In any event, Mr Scott had read note 1(w) in the accounts and had no difficulty understanding it. He knew that liabilities in financial statements were conventionally classified in the balance sheet as either current or non-current.

### Mr Kavourakis

1. Mr Kavourakis became a professional company director in about 1998. In 2005 he was:
   * + 1. chairman of Traffic Technologies Limited. He was not a member of the audit committee, but attended meetings as the chairman of the board;
       2. a director of Ticor Limited and chair of its audit committee; and
       3. a Centro director since 2003, and a member of the audit committee from that time. He was chair of the audit committee from about mid 2005.
2. Mr Kavourakis had no formal accountancy qualifications, but did not think that would impede him from carrying out the role as chairman of the audit committee for Centro or Ticor. By 2006 he had considerable experience at high level in a number of companies, could read and understand financial statements and knew it was expected that he be financially literate as a member of the Centro audit committee.
3. Mr Kavourakis’ understanding as at 2006 was that a current liability was, generally speaking, one that matured within 12 months and had no possibility of being extended. Mr Kavourakis’ understanding was that a debt was a current liability unless the borrower could extend it. With the benefit of hindsight Mr Kavourakis would have liked to know more about accounting standards before he signed the accounts.
4. Mr Kavourakis knew that there was an accounting standard prescribing the disclosure of events after the balance date.
5. At the beginning of September 2006 Mr Kavourakis knew:
   * + 1. the financial report had to comply with accounting standards;
       2. the financial report had to show a true and fair view;
       3. the financial report had to be signed off by the CEO and the CFO and approved by a directors’ resolution;
       4. directors had to form the opinion of true and fair view and solvency;
       5. a directors’ report had to be made which contained review of operations, disclose post balance day events, and give shareholders information that they would reasonably require to make informed assessment of the position and prospects of the entity.

### Mr Hall

1. Mr Hall:
   * + 1. was a qualified accountant and a very experienced former CFO with extensive experience on the audit committees of listed companies;
       2. said he was reasonably clear that AIFRS required an agreement to refinance to be in place at the balance date for liability to be non-current, but he was not 100% clear on the ‘balance date’ aspect;
       3. understood that material events after the balance date needed to be disclosed in the accounts; and
       4. knew the director’s report should refer to matters subsequent to the end of the financial year.

### Mr Cooper

1. Mr Cooper:
   * + 1. knew in August and September 2007 that significant events occurring after the balance date must be disclosed in the annual financial reports;
       2. understood that in conventional accounting practice liabilities in balance sheets are classified as current or non-current and considered himself to be financially literate;
       3. in August and September 2007 understood that a current liability generally meant a financial obligation which must be paid or satisfied within 12 months of the balance date; and
       4. was aware that significant events occurring after the balance sheet date must be disclosed in the annual financial reports.

### Mr Goldie

1. Mr Goldie:
   * + 1. understood broadly that in conventional accounting practice liabilities in balance sheets are classified as current or non-current from years of reading balance sheets ;
       2. had a perception that short-term debt was debt that had to be dealt with in the next 12 months, and if it was carried over or refinanced it went into long-term debt;
       3. clearly did not have an up-to-date clear understanding of classification of current/non-current liabilities; and
       4. was aware that significant events occurring after the balance sheet date must be disclosed in the annual financial reports.

### Mr Wilkinson

1. Mr Wilkinson:
   * + 1. considered himself well able to read and understand a financial report, and to be commercially financially literate;
       2. he was accustomed to reading financial statements, along with the notes that accompanied them, and knew:
          1. the accounts had to comply with accounting standards;
          2. had to show a true and fair view;
          3. it was necessary to classify assets and liabilities as current and non-current in the balance sheet;
          4. that current liabilities generally meant financial obligations which must be paid or satisfied within 12 months after the balance date (although at one point he had some confusion about exact definition, but this was clear to him by 2007); and
          5. that financial reports had to disclose material post balance date events;
       3. by 2007 Mr Wilkinson also knew:
          1. the CEO and CFO had to sign-off on the financial reports;
          2. directors had to approve the reports by resolution;
          3. the resolution had to state that the directors were of the opinion that the report complied with the standards, showed a true and fair view, and that the company could pay its debts as and when they fell due;
          4. the directors’ report had to be prepared, which contained a review of operations and disclosed significant post balance date events; and
          5. for a public company the report had to give shareholders information that they would reasonably require to make an informed assessment of the company’s operations, position and prospects.

## The directors’ evidence of their review of the accounts

1. I now turn to the director’s evidence of their review of the accounts.
2. The focus of the BARMC meeting held on 5 September 2007 was on the unlisted entities and not the listed entities. Most of the witnesses agreed that the main focus of the BARMC meeting on this day was on the unlisted entities. As Mr Scott said, it was not the focus of the BARMC meeting to be looking in detail at the financial statements for the listed entities because “we had already done that.”
3. I now deal with each directors evidence as to his review of the 2007 accounts of Centro.

### Mr Healey:

* + - 1. did not believe he had to read all the financial statements to be confident about signing them. He also said that he had sat through the Appendix 4E page turn and meeting earlier on 5 September 2007 when there were clearances. There were a number of factors that influenced his signing of the financial statements without reading them;
      2. did not read the full financial statements or the annual report of CER before signing;
      3. signed the full financial statements of CNP on 6 September 2007 but did not read them before doing so;
      4. did not focus on the current debts in the balance sheet because he had total confidence in the people both within the company, within PwC and within Centro’s audit committee engaged to review the balance sheet;
      5. did not focus on whether short-term debt should be disclosed in the balance sheet of CNP because he expected them to be renewed;
      6. read the concise financial reports the day before the Board meeting on 6 September 2007 and looked at the balance sheet but did not read it line by line;
      7. did not believe he had to read all the financial statements to be confident about signing them;
      8. did not focus on whether the existence of short-term debt should be disclosed in the balance sheet of CNP;
      9. did not focus on the current debts in the balance sheet because he had total confidence in the people both within the company, within PwC and within Centro’s audit committee engaged to review the balance sheet;
      10. did not focus on whether short-term debt should be disclosed in the balance sheet of CNP because he expected such debt to be renewed;
      11. believed it was necessary for him as Chairman to “form an opinion” with regard to the accounts;
      12. read the balance sheet in the CNP Appendix 4E but it did not occur to him that the allocation of the debt within the ‘current liabilities’ was incorrect. This was because he had no clear understanding of the requirements for the official Appendix 4E and the financial statements;
      13. knew at the time he signed the full financial statements that no current debt had been disclosed in the Appendix 4E;
      14. stated that if he had known of note 18 regarding the difference between the Appendix 4E and the final financial statements then he would have said “How has this come about?”;
      15. agrees that if he had read the balance sheet in the financial statements as lodged with ASIC he would have seen nearly $1.1 billion of current liabilities disclosed that had not previously been disclosed in the Appendix 4E, if he had remembered that in the Appendix 4E there were no current liabilities;
      16. there was no “page turn” of the financial statements of CNP or CER at the BARMC meeting on 5 September 2007;
      17. assumed that because the BARMC had recommended the approval of the financial statements, that it had given proper consideration to the financial statements, but does not recall one way or the other whether members of the BARMC had read the full financial statement; and
      18. did not sign the annual report, the signature on the annual report was an electronic signature.

### Mr Hall:

* + - 1. went to the Glen on both 2 and 3 September 2007 and read the full statements for CNP, CER and over 10 other entities and syndicates;
      2. said that the statements he looked at on the Sunday and Monday appeared complete in that they contained the elements shown in the table of contents;
      3. did not specifically consider whether or not the guarantees were matters that ought to have been disclosed in the directors’ report as matters subsequent to the end of the financial year, but did consider the heading at the time;
      4. did not read the profit and loss and balance sheet extracts in the papers for the September 2007 audit committee meeting because it would be a waste of time, as he knew he would be going out to the Glen to read the full financial statements;
      5. when he read the full financial statements of CNP on the Sunday the balance sheet did not have $1.1 billion as current interest bearing liability. He would have highlighted it as there was nothing in the previous year, and it would have told him that there was a net current asset deficiency;
      6. agreed he probably received an email from Mr Hourigan on 4 September 2007 with concise financial statements but did not read the concise financial report attached as he had read the full financial statements;
      7. accepted that the CNP balance sheet in the report emailed to him showed $1.1 billion as current liabilities.

### Mr Kavourakis:

* + - 1. would have a looked at the balance sheets and associated profit statements for CNP, CPT and CRT in the September audit committee pack, but he regarded them as secondary because of what had happened before, with approval of the Appendix 4Es, and would not expect any changes because the statements had already been approved and released to the market;
      2. could not recall which version of the financial statements he read at the Glen but would have passed quickly through the balance sheets because he would expect no change from the Appendix 4E;
      3. for the same reasons, he did not have pay attention to the balance sheets in the concise financial report as he had read the balance sheet in the full financial statements the day before;
      4. his comments at the audit committee meeting about not having two or three days to review were just an expression of irritation, that it might put others out who were more busy than him.

### Mr Cooper:

* + - 1. acknowledged that as part of his functions as a director of approving financial statements, whether Appendix 4E or full financial statements, he should read them;
      2. applied no system to the reading of the financial statements of the companies, but merely read them from the first page to the last page to back;
      3. did not analyse the balance sheet because based on his experience he expected the numbers to be correct as they had gone through a thorough process of development by accounting staff and had been reviewed by senior executives and also by the audit team. Further in Mr Cooper’s experience and in his experience in years past, they had been right;
      4. said that when he read the current liabilities part of the balance sheet he did not think about the level of short-term debt that he knew CNP had;
      5. did not think to ask any questions about whether or not there should be some disclosure in the balance sheet under the heading “Current Liabilities”, because he did not draw the connection;
      6. did not make the connection between what he knew of the debts of the companies and what the balance sheet disclosed in relation to the full financial statements approved on 6 September 2007.

### Mr Goldie:

* + - 1. Did not read the financial statements at the BARMC meeting or the Board meeting in September 2007, as he had previously read the content of what he thought was the same information;
      2. did identify that the financial statements were there in the room at the Glen;
      3. did try to read the Appendix 4E during the page turn on 3 August 2007, at which time he did not read the balance sheet in detail, as he did not have time to read the whole of each page as it was turned.

### Mr Wilkinson:

* + - 1. believed he did read the concise report at least before the board meeting on the Thursday. He would have paged through the whole document, including looking at the balance sheet;
      2. cannot recall noting that $1.1 billion was shown as being a current interest bearing liability;
      3. cannot recall if he compared the current assets with the current liabilities but it is possible that he did;
      4. thought it was possible that if he had read the balance sheet carefully he would have noticed the $1.1 billion figure and it would have raised questions in his mind but he cannot recall;
      5. presumed that at some point before September 2007 he would have read the summary of significant accounting policies, and would have been surprised if he had not read the note about current liabilities;
      6. likely read the board papers on 5 September 2007, including the minutes of the previous meeting which would have reminded him that there had been a decision in August to grant various guarantees. It did not cross his mind when looking at the matters reported in note 6 about events after reporting date, that the payment guarantee of $1.75 billion and the springing guarantee of $823 million might also need to be mentioned there. One of the possible reasons for this is that when he got to this part of the balance sheet he did not turn his mind to the question of whether there was anything else that he knew that might be mentioned;
      7. would certainly have read the previous minutes, and acknowledged that the guarantees were a significant matter that ought to have been mentioned in the accounts. It did not occur to him that the guarantees should be mentioned in the directors’ report.

### Mr Scott:

* + - 1. gave an account of the considerations that justified his participation in the board approval of the CNP and CER accounts, which included the page turn at the August audit committee meeting, his ‘standard account checking processes’ for both the August and September 2007 audit committee meetings, and his review of the printer’s proofs of the concise accounts;
      2. he stated:

*Although I do not recall having reviewed the final full accounts of CNP and CER, I was comfortable that I had either done so or relevant audit committee members had done so*

When cross-examined about this, he maintained that he could not recall but believed he had read the full financial statements because otherwise he would not have felt comfortable at the board meeting;

* + - 1. Mr Scott said that he did not read the financial statements in detail or line-by-line but focused on key risk areas. He did not focus on current non-current liabilities in early 2007 because he thought they could be refinanced or rolled over. He spent more time on matters that investors would be interested in. He said he was not focused on current liabilities or post balance date events but read the relevant sections.
      2. He said in cross-examination that he simply did not focus on the classification of liabilities but on the ‘key risk issues’ that the board and the company wanted him to look at. He did not believe that the constituency that he had in mind ( Real Estate Investment Trust or ‘REIT’ investors) had any interest in the classification of debt as current or non-current, despite the fact that he focused on CNP’s gearing and the market reaction to it when reading the accounts;
      3. said he did not consider it was his role or function to scrutinise each line item in the accounts nor to consider whether any particular line item complied with the accounting standards.

1. I will return to making conclusions and additional findings based on this evidence later.

# POST BALANCE DATE EVENTS

1. ASIC alleges that the New Plan Guarantees were material and required disclosure under AASB 110 (Events subsequent to balance date) and AASB 1031 (Materiality). The giving of those guarantees was not referred to in CNP’s accounts for the full year ending 30 June 2007.
2. ASIC relied upon various reports of an expert, Mr Lonergan.
3. Mr Lonergan’s main affidavit exhibited three reports:
   * + 1. a report dated 26 November 2011 (which considered the question of whether specified liabilities were current or non-current) (the first report);
       2. a report dated 28 January 2011, which considered whether four guarantees should have been disclosed in the accounts of CPL and CPT as material post balance date events (for the purposes of AASB 110) and whether those guarantees should also have been disclosed in the directors’ report under ss 299 and 299A of the Act (the second report); and
       3. a report dated 31 January 2011, which addressed the “significance” of the matters which Mr Lonergan opines should have been the subject of disclosures (the ‘omitted matters’) for users of CNP and CER’s financial statements between 18 September 2007 14 December 2007, the relevance of those matters to an assessment of the value of CNP and CER stapled securities in that period, and whether disclosure of the omitted matters was likely to “influence” users of the financial statements who were considering whether to buy, sell or hold (the third report).
4. The directors have objected to various parts of the second report. The directors also say that the third report is wholly irrelevant to the matters the subject of the liability phase of the proceeding. Alternatively, the directors objected to those paragraphs of the reports set out in their written objections.
5. In his second report, Mr Lonergan comes to the question of compliance with AASB 110 (events subsequent to balance date) by considering the materiality of the guarantees under AASB 1031 (materiality). Assessment of materiality requires an assessment of whether the non-disclosure of the information in question has the potential to “influence the economic decisions of users taken on the basis of the financial report”. Mr Lonergan’s conclusion that the first guarantee should have been disclosed rests on a series of conclusions set out in paragraph 110 of his second report. Those conclusions in part relate to the potential consequences if CNP were required to pay $1.75 billion on behalf of Super LLC and concern matters such as:
   * + 1. the availability of capital;
       2. the impact of raising new debt (and scale of that impact) on CNP’s future earnings if new debt could be raised;
       3. the impact of raising new debt on CNP’s ability to roll over other debt commitments;
       4. CNP’s capacity to raise equity;
       5. the existence and extent of “financial pressure” on CNP;
       6. the ability of CNP to raise equity at all and even then only with a “significant discount to existing equity values”; and
       7. the prices at which CNP could sell assets, specifically at “significant losses”.
6. In his third report, Mr Lonergan answers six questions (three for each of CER and CNP). Mr Lonergan answers these questions by reference to what he considers to be the impact of an increase in the current liabilities of CER and CNP and the impact on CNP of a call being made on the guarantees, again addressing matters such as the impact on the companies’ financing prospects.
7. Opinion evidence is only admissible under s 79 of the Evidence Actwhere the person “has specialised knowledge based on the person’s training, study or experience”.
8. It was contended that Mr Lonergan was not suitably qualified to give the evidence in his reports. It was not disputed that Mr Lonergan has expertise in the valuation of companies and company shares, and the interpretation of financial statements and other financial information.
9. Further to his earlier affidavits, in an affidavit sworn on 29 March 2011, Mr Lonergan set out in detail his experience and expertise qualifying him to give the evidence detailed in his reports, including the third report. He has been engaged actively in stock market trading for more than forty years, monitoring market developments on a daily basis as well as monitoring broker and other research material relevant to market matters. He has extensive corporate finance and valuation experience, and his accounting and financial expertise spans across a wide range of capital matters.
10. Based on the evidence before me in this proceeding, I am satisfied that Mr Lonergan has the expertise to opine as he does in his reports, and has not gone beyond his field of specialisation. Without going into detail of all of his ‘experience’, the affidavit sworn on 29 March 2011 satisfies me that Mr Lonergan is able to opine within his area of specialist knowledge on the impact of the relevant omissions in the accounts on users of the financial statements.
11. I interpolate that to the extent that my approach to the admissibility of Mr Lonergan’s evidence is different to that expressed by Austin J in *AAPT Ltd v Cable & Wireless Optus Ltd and Ors* (1999) 32 ACSR 63, at [13] to [16], this is because of the evidence before me in this proceeding as to Mr Lonergan’s experience and the nature of the dispute before this Court.
12. In his second report Mr Lonergan (to a lesser or greater extent) opines upon:
    * + 1. the likelihood of the guarantees being called;
        2. the availability of credit and debt to CNP;
        3. the terms upon which debt or equity could be raised by CNP;
        4. the impact of debt raising on CNP’s future earnings;
        5. the financial pressure on CNP;
        6. the decline of market values and market liquidity;
        7. the value at which assets could be sold; and
        8. CNP’s ability to roll over debt.
13. I do not accept that only an expert in the relevant equity and debt markets would be qualified to give opinions on the likely impact of disclosure on the availability of debt or equity financing to CNP or CER or the terms upon which it might be provided. Mr Lonergan could, if appropriately instructed on the nature of the New Plan investment, the operations of that business, its holdings and business plans, give evidence of the likelihood of Super LLC being unable to meet its obligations which were the subject of the guarantees or the value which could be realised if any US assets had to be sold. Similarly, Mr Lonergan could, if appropriately instructed on the nature of CNP and CER’s Australian holdings, bring to bear the necessary expertise in order to give an admissible opinion on the value which might be realised if any Australian assets were to be sold. However, to so opine he would need to do so upon proper material, or alternatively, evidence to support any assumptions would need to be before the Court.
14. Many of the conclusions which are the subject of Mr Lonergan’s second and third reports are conclusions that relate to, or depend upon, his views as to the impacts of the worsening state of what later became known as the GFC. The materials referred to by Mr Lonergan that support his statements regarding the potential state of the financial markets is in part material before the directors and which is in evidence as part of the information they had at the relevant time. On this information alone Mr Lonergan’s views are supportable.
15. Mr Lonergan is entitled to rely upon material, to the extent it is in evidence, to support the views he holds looking at the position of the companies and the impact upon the market. For instance, just focusing on the passages from the presentation to CNP’s Board, these can be and are relied upon as information which was with the directors, and from this an expert (or for that matter the Court) can conclude as to the market conditions at least known to the Board. From that position, an expert such as Mr Lonergan is able to then opine on the application of the accounting standards.
16. To the extent Mr Lonergan refers to matters that are factual which are not proved, this does not impact on the admissibility of his opinion: see eg *Neowarra v Western Australia (No 1)* (2003) 134 FCR 208; *Quick v Stoland Pty Ltd* (1998) 87 FCR 371, at 373-374. However, the weight to be accorded to an opinion or conclusion that is not founded on a fact established will be reduced.
17. The non-executive directors relied upon the comments of the New South Wales Court of Appeal in *Makita (Australia) Pty Ltd v Sprowles* (2001) 52 NSWLR 705 where Heydon J (at [85]) emphasised the need for experts to operate only within their fields of specialised knowledge, and to make their reasoning explicit and to demonstrate the ways in which they have applied their specialised knowledge in arriving at their opinions:

*[T]he opinion of an expert requires demonstration or examination of the scientific or other intellectual basis of the conclusions reached: that is, the expert’s evidence must explain how the field of “specialised knowledge” in which the witness is expert by reason of “training, study or experience”, and on which the opinion is “wholly or substantially based”, applies to the facts assumed or observed so as to produce the opinion propounded. If all these matters are not made explicit, it is not possible to be sure whether the opinion is based wholly or substantially on the expert’s specialised knowledge. If the court cannot be sure of that, the evidence is strictly speaking not admissible, and, so far as it is admissible, of diminished weight. And an attempt to make the basis of the opinion explicit may reveal that it is not based on specialised expert knowledge, but, to use Gleeson CJ’s characterisation of the evidence in* HG v The Queen *(at 428 [41]), on “a combination of speculation, inference, personal and second-hand views as to the credibility of the complainant, and a process of reasoning which went well beyond the field of expertise”.*

1. I accept that where the process of reasoning by which an opinion has been formed is not made explicit, that process of reasoning cannot be effectively tested by cross-examination. Further, the expert can only operate within their field of knowledge, the issue I have just addressed.
2. In my view, on a fair reading Mr Lonergan’s second and third reports, these reports do not contain statements which are unsupported by any articulated chain of reasoning, and are based on his specialised field of knowledge that has been applied in reaching those views. It was said that an examination of paragraph 110 of Mr Lonergan’s second report illustrates the deficiencies in his approach. I do not agree. Assuming expertise, Mr Lonergan analyses why ‘Guarantee 1’ was a material item and should have been disclosed. Assuming “volatile market conditions” (which was a matter reported to the Board of CPL and CPT in any event subject to qualification), the opinion is reasoned and (as the submissions of the non-executive directors and cross-examination showed) was able to be properly tested and analysed. To a certain extent the opinion is ‘speculative’, but this is because of the nature of the inquiry as to whether disclosure of the guarantees was required and the impact on the market.
3. In relation to the third report, I take a similar approach.
4. Therefore, I regard each of the reports of Mr Lonergan as admissible, and I do not uphold the written objections of the directors, subject to one qualification. To the extent that Mr Lonergan recites or opines about the law, I take that to be only referred to as introductory to the opinions he finally expresses in his field of expertise. It is for the Court to determine and apply the law.
5. I do make this observation. As submitted by the directors, the question of contravention is to be assessed at 6 September 2007 or at the latest 18 September 2007. Whilst Mr Lonergan in his third report looks to the period 18 September 2007 to 14 December 2007, his report is not irrelevant to the issues in the liability part of this proceeding. At the very least, the seriousness of the consequences of any alleged contravention is relevant to the steps to be taken to avoid the contravention and the standard of care required by each director as part of the ‘calculus of negligence’: see eg *Wyong Shire Council v Shirt* (1980) 146 CLR 40;and *Ryan v Fisher* (1976) 51 ALJR 125.
6. It was also argued by the directors that the second and third reports should be rejected on discretionary grounds. Pursuant to s 135 of the Evidence Act, the court may refuse to admit evidence where its probative value is substantially outweighed by the danger that the evidence might be unfairly prejudicial, misleading or confusing or cause or result in undue waste of time.
7. It was contended that there are several factors that would, in any event, justify exercise of the residual discretion to exclude those parts of the second report which are the subject of objection and Mr Lonergan’s third report under s 135:
   * + 1. even if the third report is relevant to the liability trial, it can only be of very tangential relevance;
       2. Mr Lonergan’s failure to articulate his process of reasoning compromises the ability of the defendants effectively to challenge his views in cross-examination;
       3. Mr Lonergan’s sweeping and unsupported conclusions regarding the likelihood of a call being made on the guarantees and the consequences for CNP (in terms of the availability of debt or equity financing, the terms upon which finance might be available, and the price at which assets might be sold) are prejudicial in circumstances where those opinions are outside Mr Lonergan’s field of expertise, and without any proper foundation.
8. I do not agree. I have already indicated some views on Mr Lonergan’s analysis. I would not characterise the third affidavit as having ‘tangential’ reliance. I see no basis to reject the affidavits on discretionary grounds. The weight I give to Mr Lonergan’s views is a separate consideration.
9. I now turn to the content of Mr Lonergan’s reports.
10. Mr Lonergan, in relation to the guarantees, expressed the following opinions:
    * + 1. in order for the financial reports of CPL and CPT to comply with AASB 110 and s 296(1) of the Act, the following additional disclosure in relation to the four guarantees granted by CPTM and CPL on or about 1 August 2007 would have been necessary under the heading “Events occurring after reporting date”:

*A bridging facility previously secured to fund the acquisition of New Plan had been increased from US$2.47 billion to US$2.6 billion and extended from 19 October 2007 to 14 December 2007.*

*The following guarantees were granted by the Group/Trust in relation to the amended bridge facility or New Plan’s financing:*

* *a guarantee of the payment of US$1.75 billion in respect of Super LLC’s bridge facility was granted in favour of various financiers of the bridge facility. In the event that Super LLC (the borrower) fails to pay all or any part of the amount due relating to this portion of the bridge facility, the Group/Trust, being the guarantor, will be liable to pay the financiers the due amount on behalf of the borrower;*
* *a non-recourse carveout guarantee was granted in favour of the financiers of the bridge facility. The liability of the guarantors is limited to the extent of the loss or damages caused by actions such as negligence, fraud, misconduct and misrepresentation by Super LLC and other related entities;*
* *a limited guarantee was granted in relation to the payment of US$843 million. The guarantee is effectively limited to the shortfall from an intended CMBS issue of the same amount; and*
* *a guarantee was granted in relation to New Plan’s US$350 million revolving credit facility which was extended from 20 October 2007 to 31 December 2007. The liability of the guarantors is limited to specific circumstances. The likelihood of the guarantee becoming effective as at the date of this report appears very low.*

*Management considers it difficult to estimate the potential impact of the above guarantees on the future financial performance and financial position of the Group/Trust.*

* + - 1. in order to provide the details required by s 299(1)(d) of the Act, the directors report of CPL and CPT should have provided an additional disclosure with respect to the abovementioned four guarantees, or referred to the relevant disclosure in the accompanying financial statements of CPL and CPT. In particular, a disclosure to the following effect under the heading “Matters subsequent to the end of the financial year” should have been included in the directors report of CPL and CPT:

*The following events which have arisen in the interval between 30 June 2007 and the date hereof have significantly affected, or may significantly affect:*

*(a) the Group/Trust’s operations in future financial years; or*

*(b) the results of those operations in future financial years; or*

*(c) the Group/Trust’s state of affairs in future financial years.*

*A bridging facility previously secured to fund the acquisition of New Plan had been increased from US$2.47 billion to US$2.6 billion and extended from 19 October 2007 to 14 December 2007.*

*The Group/Trust granted four guarantees in relation to the amended bridge facility or New Plan’s financing. Further details of the guarantees are provided in note [to insert] to the financial statements.*

* + - 1. members of CPL would reasonably require the information on the four guarantees similar to that set out above in order to make an informed assessment of CPL’s business strategies and prospects for future financial years.

1. It is appropriate that Mr Lonergan was in effect required to consider the hypothetical situation, as no disclosure of the guarantees was made in the financial statements.
2. In determining whether the guarantees were material and required disclosure under AASB 110 and s 296(1) of the Act it was necessary for Mr Lonergan to consider the potential likelihood of the guarantees being called. If the guarantees were material and non-disclosure could influence the economic decisions of users of the financial statements then disclosure is required. AASB 110 gives a specific example with respect to the “entering into significant commitments or contingent liabilities, for example, by issuing significant guarantees”.
3. Mr Lonergan made reference to AASB 137. AASB 137 - Provisions, contingent liabilities and contingent assets - defines a “contingent liability” as either:
   * + 1. a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or
       2. a present obligation that arises from past events but fails the criteria for recognition as a liability or provision because:
4. it is not probable that an outflow of economic resources will be required to settle the obligation; or
5. the amount of the obligation cannot be measured reliably;

and requires contingent liabilities to be disclosed, unless the possibility of an outflow of resources embodying economic benefits is remote.

1. As Mr Lonergan says, had the guarantees been in place as at 30 June 2007 disclosure would have been required under AASB 137 as follows (per paragraph 86 of AASB 137):

*Unless the possibility of any outflow in settlement is remote, an entity shall disclose for each class of contingent liability at the reporting date a brief description of the nature of the contingent liability and, where practicable:*

*(a) an estimate of its financial effect, measured under paragraphs 36-52;*

*(b) an indication of the uncertainties relating to the amount or timing of any outflow; and*

*(c) the possibility of any reimbursement.*

1. In order to determine whether the guarantees were material and whether settlement was remote (which he interpreted to mean “slight, faint or unlikely”), Mr Lonergan considered:
   * + 1. the size of the guarantees (opining that the collective amount of the guarantees was clearly material and if called in substantially or in their entirety the potential impact on Centro was clearly very significant);
       2. the nature of the guarantees; and
       3. the likelihood that the guarantees could be called and an outflow of resources could occur.
2. In order to assess whether the outflow of resources was remote, he considered the following:
   * + 1. the financial position of Super LLC;
       2. the financial position of CPL, CPT and CRT; and
       3. developments in the credit market in July to September 2007.
3. Mr Lonergan’s assessment was primarily based on the following sources of information:
   * + 1. ASX announcements made by Centro;
       2. the equity accounting disclosure made in the information contained in the financial statements of CPL, CPT and CRT;
       3. the financial position of CPL, CPT and CRT (including the reclassification of liabilities to ‘current’ and the status of debt refinancing as per the banking facilities review documents considered in his first report);
       4. events relating to the funding arrangements for the New Plan acquisition (principally the Board submission) as summarised in Appendix E of the second report;
       5. the state of the credit market in the period July to September 2007 as evidenced in:
          1. the CPL and CPT Board submission dated 2 August 2007;
          2. the financial press; and
          3. broker and analyst reports;
       6. a “first principles” review of the financial position of CPL, CPT and CRT.
4. In preparing his third report, Mr Lonergan was asked to consider certain omitted matters (ie the incorrect classification of liabilities and disclosure of guarantees as a non-adjusting post balance date event). In this report he considered the impact of the omitted matters on users of the financial statements, principally investors or potential investors in CNP Stapled Securities and CER Stapled Securities.
5. In assessing the impact of the omitted matters it was necessary to consider how users of the financial statements would have reacted if the omitted matters had been included in the financial statements. As they were not disclosed it was necessary to consider what impact their disclosure would have had under the (necessarily) hypothetical or “but for” scenario if proper disclosure had been made.
6. In his third report, Mr Lonergan expressed the following opinions by reference to six questions asked of him:

#### First Question

If Centro had lodged with ASX on 18 September 2007 the Notional Amended CNP Annual Report, in his view, users of the annual financial statements and reports of CNP in the period from 18 September 2007 to 14 December 2007 would have been made aware of the following significant matters:

* + - 1. as at 18 September 2007, based on the financial information then available:
         1. CNP’s refinancing risk had increased very significantly over a six month period (31 December 2006 to 30 June 2007). In particular:

● CNP’s current liabilities significantly exceeded its current assets;

● CNP had significant interest-bearing liabilities to be repaid/refinanced in less than 12 months;

● even if CNP could refinance some or all of its short-term debts, higher borrowing costs were likely;

● CNP’s negotiating position with lenders was likely to have been very weak due to its poor liquidity position and financial pressure.

* + - * 1. CNP had substantial contingent liabilities as a result of the grant of various guarantees subsequent to the balance date that could have very serious adverse financial consequences. In particular:

● the guarantees exposed CNP’s assets to very large additional liabilities of its US joint venture and potentially very significant losses;

● the guarantees potentially jeopardised CNP’s ability to refinance or roll over its own short-term debt commitments;

● if the guarantees were called, there would be substantial negative impact on CNP’s net asset position, profitability, liquidity and credit standing.

* + - 1. over the period from 18 September 2007 to 14 December 2007, in the context of the deepening of the financial crisis in the US, CNP’s refinancing risk had become significantly worse as financial pressure on CNP increased.

The inclusion of the CNP omitted matters would have drawn to the attention of the users of CNP’s annual financial statements and reports the significant increase in CNP’s liquidity risk and refinancing risk.

This can be clearly seen from the examination of the relevant financial indicators of CNP as at 30 June 2007 compared to those as at 31 December 2006 and 30 June 2006 as shown below:

|  |  |  |  |
| --- | --- | --- | --- |
|  | **30 Jun 07**  **Adjusted**  **$m** | **31 Dec 06**  **Reported**  **$m** | **30 Jun 06**  **Reported**  **$m** |
| Current assets | 1,338 | 971 | 714 |
| Current liabilities | (3,268) | (532) | (262) |
| **Net current assets** | (1,930) | 439 | 452 |
|  |  |  |  |
| Current assets/current liabilities (%) | 41 | 182 | 273 |
|  |  |  |  |
| Current interest bearing liabilities | (2,611) | - | - |
| Non-current interest bearing liabilities | (993) | (2,426) | (1,537) |
| **Total interest bearing liabilities** | (3,604) | (2,426) | (1,537) |
|  |  |  |  |
| Current interest bearing liabilities / total interest bearing liabilities (%) | 72% | - | - |
|  |  |  |  |

In particular:

* + - 1. CNP had a net current asset deficiency (calculated as total current assets less total current liabilities) of A$1.93 billion as at 30 June 2007 compared to a net current asset surplus of A$0.44 billion as at 31 December 2006.

In essence, as at 30 June 2007, CNP’s current assets could only meet 41% of its current financial obligations. This had declined from the reported surplus positions of 182% and 273% as at 31 December 2006 and 30 June 2006 respectively.

It is normal commercial practice for current assets to exceed current liabilities. Unless this is so, there is a serious risk that the entity may not be able to meet its debts as and when they fall due.

* + - 1. as at 30 June 2007, CNP had significant interest bearing liabilities (A$2.61 billion) due to be repaid/refinanced within 12 months compared to nil as at 31 December 2006 and 30 June 2006.
      2. the proportion of short-term debt funding (less than 12 months) increased from 0% as at 31 December 2006 to 72% as at 30 June 2007. That is, over a six month period, CNP’s funding position had changed from being entirely funded by medium to long-term finance (greater than 12 months ) to being mostly funded by short-term finance.

Even if CNP could have refinanced some or all of its commitments, CNP was likely to incur significantly higher funding costs as credit spreads had increased. Furthermore, CNP’s short-term commitments were so great and its liquidity position so poor that its negotiating position with lenders would have been very weak.

To try and ameliorate its financial pressure, it was likely that CNP would need to raise substantial new equity. Due to its significant financial issues, this could only be done (if at all) at a deep discount to underlying net asset value (thus eroding the market value of existing issued capital).

In addition to CNP’s on balance sheet debt and its substantial refinancing risk, CNP had substantial contingent liabilities as a result of various guarantees granted in relation to the New Plan US$2.6 billion bridge facility.

Disclosure with respect to the above guarantees in the Notional Amended CNP annual report would have highlighted to the users of CNP annual financial statements and reports that:

* + - 1. CNP had effectively guaranteed the payment of a US$2.6 billion (A$3 billion) bridge facility due to be repaid in December 2007;
      2. the guarantees exposed CNP’s assets and equity to very large additional liabilities and potentially a loss significantly greater than the initial investment in New Plan of A$0.95 billion;
      3. if the guarantees were called for on any significant amount, there would be very serious adverse financial consequences. CNP would have to:
         1. raise new debt in a debt market where credit spreads had widened significantly and limited capital was available; and/or
         2. raise new equity at a time when CNP was under refinancing pressure. CNP might not be able to do so unless a significant discount to existing equity values were to be offered; and/or
         3. sell assets in volatile market conditions where investors had become considerably more risk-adverse and asset values and market liquidity were declining;
      4. the guarantees would potentially jeopardise CNP’s ability to roll over its own A$2.61 billion short-term debt.

In the context of the deepening of the GFC in the US over the period from 18 September 2007 to 14 December 2007, it would have been apparent to the users of CNP’s financial statements that CNP’s refinancing risk must have become worse during this period.

During the 18 September 2007 to 14 December 2007 period:

* + - 1. there were numerous announcements by large US banks and overseas financial institutions of record losses due to the drop in earnings and/or massive write-downs. For example:
         1. on 15 October 2007, Citi Group announced that its third-quarter profit fell 57% with net income down to $2.38 billion from $5.51 billion a year earlier;
         2. on 19 October 2007, Wachovia announced a 10% decline in third-quarter profit to $1.69 billion from $1.88 billion a year earlier, having suffered $1.3 billion in write-downs resulting from credit market turmoil;
         3. on 24 October 2007, Merrill Lynch announced it had suffered the biggest quarterly loss in the company’s 93 year history and the first since 2001 after writing down $8.4 billion of its CDOs backed by subprime mortgages;
         4. on 30 October 2007, UBS reported a third-quarter pre-tax loss of CHF726 million ($624.8 million) after it took a charge of CHF4.2 billion on subprime-related losses in its fixed income investment;
         5. on 13 November 2007, Bank of America wrote-off $3 billion in subprime losses;
         6. on 14 November 2007, HSBC raised its subprime bad debt provision by $1.4 billion to $3.4 billion;
      2. there was a very significant increase in credit spread between corporate bonds and US treasury bonds. For example, the spread between high-yield corporate paper and US treasury bonds had doubled between June and November 2007 from 260 to 520 basis points (ie 2.6% to 5.2%);
      3. the European covered-bond market (a US$2 trillion market for mortgage debt) was suspended for the first time because of falling prices on 21 November 2007;
      4. the US Federal Reserve and government introduced a number of measures and packages to stabilise the market.

Given the significant exposure of CNP to the state of the US economy with its recent US$5 billion acquisition of New Plan, the probability of at least some of the guarantees being crystallised, all else being equal, was likely to have increased over the period from 18 September 2007 to 14 December 2007. At the same time, the chance of refinancing A$2.61 billion worth of short-term debt at reasonable rates was likely to have declined significantly.

#### Second Question

If Centro had lodged with ASX on 18 September 2007 the Notional Amended CNP annual report, in Mr Lonergan’s view, the CNP omitted matters would have been relevant to the assessment of the value of CNP Stapled Securities by users of the annual financial statements who were considering whether to buy, sell or hold those securities in the period from 18 September 2007 to 14 December 2007.

#### Third Question

If Centro had lodged with ASX on 18 September 2007 the Notional Amended CNP annual report, in Mr Lonergan’s view, the CNP omitted matters would have been likely to significantly influence users of the financial statements who were considering whether to buy, sell or hold CNP Stapled Securities in the period from 18 September 2007 to 14 December 2007 in deciding whether to acquire or dispose of those securities.

#### Fourth Question

If Centro had lodged with ASX on 18 September 2007 the Notional Amended CER annual report, in Mr Lonergan’s view, users of the annual financial statements and reports of CER in the period from 18 September 2007 to 14 December 2007 would have been made aware of the following significant matters:

* + - 1. CER’s short-term refinancing risks had increased very significantly over the six month period from 31 December 2006 to 30 June 2007.

As can be seen from CER’s financial indicators below, over the period from 31 December 2006 to 30 June 2007:

* + - * 1. CER’s net current asset deficit increased very significantly from a surplus of A$15 million to a deficit of A$630 million
        2. CER’s total debt funding remained unchanged but the short-term funding portion increased from 0% as at 31 December 2006 to 41% as at 30 June 2007.

|  |  |  |  |
| --- | --- | --- | --- |
|  | **30 Jun 07**  **Adjusted**  **$m** | **31 Dec 06**  **Reported**  **$m** | **30 Jun 06**  **Reported**  **$m** |
| Current assets | 55 | 52 | 35 |
| Current liabilities | (685) | (36) | (46) |
| **Net current assets** | (630) | 15 | (11) |
|  |  |  |  |
| Current assets/current liabilities (%) | 8 | 142 | 76 |
|  |  |  |  |
| Current interest bearing liabilities | (598) | - | - |
| Non-current interest bearing liabilities | (846) | (1,420) | (1,260) |
| **Total interest bearing liabilities** | (1,444) | (1,420) | (1260) |
|  |  |  |  |
| Current interest bearing liabilities / total interest bearing liabilities (%) | 41 | - | - |
|  |  |  |  |

1. CER’s short-term refinancing risk must have increased during the 18 September 2007 to 14 December 2007 period due to the continued deterioration of the credit crisis in the US.

Similar to CNP, CER had significant exposure to the US market conditions. CER derived around 50% of its 2007 earnings from the US. CER’s US assets accounted for 57% of its total assets.

Most of the CER short-term debts due to be repaid/refinanced within 12 months were originally obtained from the domestic Australian market. However, this does not mean that CER would automatically be able to rollover or obtain new debt funding from domestic financiers at reasonable costs.

In deciding whether to rollover existing debt or lend to CER when these short-term debts fall due, lenders would have regard to CER’s ability to generate future earnings (as well as the volatility of these future earnings) and the underlying determinant of that ability (in particular, the strength of both Australian and US consumer spending).

As the US market conditions became worse, CER’s ability to generate earnings from the US market is likely to have been adversely affected and the volatility of such future earnings is likely to have increased.

#### Fifth Question

If Centro had lodged with ASX on 18 September 2007 the Notional Amended CER annual report, the CER omitted matters would have been relevant to an assessment of the value of CER Stapled Securities by users of the annual financial statements who were considering whether to buy, sell or hold those securities in the period from 18 September 2007 to 14 December 2007.

#### Sixth Question

If Centro had lodged with ASX on 18 September 2007 the Notional Amended CER annual report, the CER omitted matters would have influenced users of the financial statements who were considering whether to buy, sell or hold CER Stapled Securities in the period from 18 September 2007 to 14 December 2007 in deciding whether to acquire or dispose of those securities.

1. I will consider later certain criticisms made by the directors in relation to these conclusions. However, at the outset I say that it is legitimate to consider the position (and make an assessment as to what may occur at a later time) as at September 2007. This task of evaluation can be undertaken (putting aside financial press and broker and analyst reports) by reference to documentation emanating from Centro or before the directors up to and including 6 September, or at the latest 18 September 2007. This is effectively what Mr Lonergan has done, putting aside some press clippings and brokers’ analysis.
2. In my view, the opinions of Mr Lonergan, which I accept, can be supported on the basis of this material which is all admissible before the Court.
3. The appropriate way in which to view the guarantees is to assess them in the aggregate as a class of ‘contingent liability’, as Mr Lonergan concludes.
4. One of the most significant matters to recall is that the four guarantees were granted in connection with the increase and the extension of the US$2.6 billion bridge facility of Super LLC and the extension of the US$350 million revolving credit facility of Centro NP LLC. The increase and the extension of the bridge facility was partly required due to the volatility in the US credit markets and the substantial increase in credit spreads.
5. It was presented to the board of CPL and CPT on 2 August 2007 that:
   * + 1. there was a significant deterioration of the global debt markets;
       2. Centro had US$2.8 billion worth of bridge facilities to finance prior to 31 December 2007;
       3. Centro US CMBS margins were anticipated to widen significantly from 50 bps to 85 to 90 bps; and
       4. market evidence suggested a limited CMBS market at any price.
6. Again, I accept that the directors were confident about the future, based upon experience and information being supplied to them, but this does not mean that there was no risk. Undoubtedly, standing back, the cumulative impact of the guarantees should have been seen as potentially having serious impact, even without the benefit of hindsight. As Mr Lonergan stressed, the test is basically disclosure unless the possibility of any outflow settlement is remote.
7. In my view, the question of disclosure of the guarantees is relatively straight forward. There is always a risk that a guarantee will be called upon. In the case of very large amounts guaranteed as here, unless the risk was remote or seriously unlikely, the existence of the guarantee should be disclosed. As I indicated, this was the view of Mr Lonergan, which was not displaced under cross-examination.
8. Mr Cougle thought that based upon the ‘magnitude’ of the guarantees they should have been disclosed, although he said this on the basis of the information he had before him in the witness box. Mr Fekete, when asked about the guarantees, and being told of the in magnified - not being just for $30 million, but “for billions” - was of the view that *prima facie* they should be disclosed.
9. The guaranteed amounts were due in December 2007, being very short-terms debts. The question was whether the primary debtor, Super LLC, was going to have $2.6 billion available to repay JP Morgan and the other banks. It does not really impact upon this issue what the value of the business of the primary debtor was. If the amount was not paid in a timely manner, the guarantee could be called upon.
10. The directors knew that the debt was to be repaid through CMBS issues which were intended to be made in the US market in the period from August to December 2007. There was certainly a risk as at August 2007, (which was certainly not remote), that repayment through the CMBS issues may not be able to be obtained. Undoubtedly the Board was, as I have said, being given positive signals, but the directors were aware of some problems with US CMBS transactions and their availability or demand.
11. However, and this is the important factor, there was a chance, a possibility, that if the markets did not recover, or the banks did not come to Centro’s assistance to extend existing facilities, Super LLC would need support.
12. Whether this may have previously been the position expected by Super LLC in any event, namely that it would be supported, or even the position that the directors took that they would support Super LLC, entering into the guarantee involved legal obligations and potential liabilities. I do not accept that by entering into the guarantees nothing really changed, even from the commercial point of view. Entering into the guarantees changes the risk, and takes away the option of not supporting Super LLC.
13. On this analysis, property values, the refinancing risks, the extent of the credit crisis in the US, the availability of debt funding, the ability to generate earnings in the US market, market conditions and/or liquidity are not of any real significance in determining the issue before the Court.
14. I now turn to the submissions of the directors on the likelihood of the guarantees being called.
15. Mr Lonergan accepted in cross-examination that, in order to determine whether a post balance date guarantee is material, it is necessary to consider the likelihood of a call being made on the guarantee. He also accepted that materiality is a question of judgment. None of these concessions changed his views.
16. It was submitted by the non-executive directors that in order to evaluate the likelihood of Super LLC defaulting on its obligations (thereby exposing CNP to the possibility of a call being made on the guarantees), it is simply not enough to refer to the gearing level of the underlying assets, while dismissing intangible assets (principally goodwill, reflecting the value of the services business) and failing to make any serious attempt to understand the detail of the New Plan business, the state of the US commercial property market in the relevant period, or the value of the assets of the primary debtor.
17. Mr Lonergan accepted that he had no expertise in the US commercial real estate market and that if the primary debtor’s assets were of sufficient value, a call on the guarantees was unlikely in any event. I observe that this is not to say such a call was remote. It was submitted that Mr Lonergan’s analysis not only assumes that CNP would be required to meet a call in the order of US$3 billion (rather than some lesser amount), but also that CNP would not have the benefit of any offsetting value in the underlying assets of New Plan. These are commercial matters to consider.
18. In considering the materiality of the guarantees and how the non-executive directors may reasonably have perceived them at the time, I accept that the commercial context is relevant. Mr Scott explained in his evidence that he considered the guarantees from a commercial point of view and did not consider that they would add to the net liabilities or place the group at risk. Mr Scott considered that the guarantees related to debt for which CNP and CER were effectively responsible in any event given that they related to the debts of the US joint venture vehicle. I do not accept this for the reasons I have already stated – entering into legal objections alters the risk. Mr Scott believed that the likelihood of a call being made on the guarantees was remote, not least because the loans were secured by substantial assets of the US joint venture borrower. Further (and in terms of how the market may have responded to the guarantees) Mr Scott’s evidence was that the “look through” gearing presented to the market took up the joint venture debt. It may also be noted that the guarantees were in respect of a bridging facility and there is no evidence to suggest that, in the remaining period of the bridging loan, there was any real prospect of circumstances changing such as to make a call more likely.
19. I do not consider that this ‘commercial perspective’, after considering the magnitude of the sums involved, detracts from the opinion of Mr Lonergan. I do not doubt Mr Scott holds the views he expressed in evidence. However, I prefer the approach of Mr Lonergan, supported, by Mr Cougle and Mr Fekete, who emphasised the magnitude of the potential exposure.
20. The directors pointed out that CNP did account for the investment in New Plan using the equity method. When a reporting entity “equity accounts” for its investment in another entity in the way that CNP accounted for its investment in New Plan, it includes a single line showing the net value of its investment in its associate after the liabilities of the associate are deducted from the assets of the associate.
21. When CNP equity accounted for its investment in New Plan, the net value of its investment as reported in its financial statements was $1.28 billion. It was submitted that CNP enjoyed a “buffer” before any call on the guarantees would take its investment in New Plan into a negative position. PwC also confirmed in its report to the BARMC on 2 August 2007 that there was additional “head room” of some $110 million. I will assume from the difference between the purchase consideration disclosed in the accounts ($955 million) and the carrying value in the accounts of New Plan at 30 June 2007 ($1.28 billion) that the value of CNP’s investment in the New Plan business increased by some $350 million after April 2007.
22. Therefore, it was submitted by the directors that where the liabilities of Super LLC as the primary debtor are reflected in the balance sheet of the guarantor through equity accounting, there is substantial “head room”. The Board had been told in respect of earlier guarantees given upon the initial investment in New Plan that a call on the guarantees was unlikely. PwC had not raised any issues. Management had assured the board it was conscious of the need to disclose material post balance date events and was monitoring the situation. Therefore, it was submitted that there were no circumstances which should have alerted the board of CNP to the fact (if it be so) that the accounts were deficient in failing to refer explicitly to the giving of the guarantees.
23. I do not accept that these submissions impact upon the views of Mr Lonergan. Without specific disclosure of the guarantees the users of the accounts would have no knowledge of their potential impact. Further, Mr Lonergan pointed out the guarantees committed CNP to a greater potential loss than the liabilities equity accounted.
24. In my view, based upon Mr Lonergan’s analysis, the entry into the guarantees was a material event occurring after the balance date, and was a matter or circumstance that may “significantly affect” CNP’s operations in future financial years for the purposes of s 299. Similarly, in those circumstances, information regarding the entry into the guarantees was a matter that the members of CNP reasonably required to make an informed assessment of the operations, financial position, business strategies and prospects for future financial years of CNP.
25. It was then submitted that even if the entry into the guarantees was “significant” for the purpose of s 299 or was information that was reasonably required by members of CNP under s 299A, it does not follow that the non-executive directors have breached their obligations under s 180 or s 344. The directors’ obligation was to take reasonable steps to ensure that the company fulfilled that obligation. As such, it was submitted, the directors were reasonably entitled to rely on management to form a view regarding events after 30 June 2007, their likely impact on the company’s affairs in future years and whether those events required mention in the directors’ report. The directors were also reasonably entitled to rely on PwC, having had access to records of events after 30 June 2007 (including entry into the guarantees) to ensure that the directors’ report complied with the Act.
26. It was submitted by the directors that Mr Lonergan sought to draw a distinction between “material” for the purposes of AASB 110 and “significant” for the purposes of the statute so as to justify his view that guarantee number 2 was material but not significant. It was said that if Mr Lonergan’s evidence was accepted, the determination of what must be disclosed as material under AASB 110 and what must be disclosed as significant under ss 299 and 299A involves fine distinctions between the meaning of the words “material” and “significant”, such that the same instrument may be material but not significant. Given this, and also the need to assess the likelihood of a call being made on the guarantees before reaching a conclusion on materiality, the directors were entitled to rely on those expert in accounting (management and the auditors) to get it right.
27. Further, it was submitted that it is notoriously much easier to consider and comment on what is in a document than it is to comb the universe of one’s knowledge to identify what is not referred to. It was said that the whole of the allegations concerning the guarantees was that, as the non-executive directors knew they had been entered into, they necessarily failed in their duties because they did not notice that they were not referred to in the full financial statements. Having been assured by management that they were aware of the need to disclose post balance date events, and having retained PwC to audit the accounts (which process involves checking for post balance date events ), it was submitted that the directors cannot be said to have failed in their duties simply because they did not notice an omission that escaped the attention of those whose core function it was to ensure compliance with accounting standards, (which necessarily entailed making appropriate post balance date disclosures).
28. The directors pointed to the audit files of PwC containing a work paper “Review of Minutes post year end”. This work paper records that it was completed by Amy Marshall on 18 September 2007 and reviewed by Brad Duggan on 19 September 2007. The work paper states that PwC reviewed minuted [sic] of board meetings held between July 2007 and the “September 2007”. The work paper states that areas of “audit significance” noted from the review of the minutes are set out in the work paper with a comment on how they impact the audit. The work paper contains express reference to the four guarantees given in connection with the refinancing of the US New Plan bridge loan, with the following notation in the “Impact on Audit Work” column: “Has been disclosed in the financial report”.
29. It was further submitted that notwithstanding that PwC was clearly aware of the guarantees, and although ASIC conducted s 19 examinations of numerous PwC personnel, ASIC did not ask them why it was that PwC decided that the matter of the guarantees had been adequately dealt with in the financial report. In view of the fact that CNP equity accounted for its investment in Super LLC and the fact that there was a buffer of over a billion dollars before any call on the guarantees would cause any loss to CNP, it may well be that PwC considered that the status of the New Plan investment had been adequately covered and no further disclosure was required by AASB 110.
30. The directors submitted that it would be unsafe to reach any conclusion on the *Briginshaw* standard that the guarantees were required to be disclosed or, if disclosure was required, that they breached their duties of care and diligence or their duty under s 344. Without understanding the reasoning of the auditors retained by Centro to audit the financial statements, which led them to conclude no further disclosures were required, it cannot be said that the directors necessarily failed in their duties merely because they failed to detect an omission from the accounts. It was submitted that, in any event, as Mr Hullah opined, a reasonable director could have formed the view that the guarantees did not need to be disclosed because the borrowings which had been guaranteed were already included in the financial statements of companies, which had been equity accounted for in CPL’s accounts.
31. The difficulty with this analysis, accepting that the guarantees needed to be disclosed (as I have found), is that the non-executive directors failed to turn their mind to the omission and solely relied upon advice. No non-executive director gave evidence, for instance, that because of the equity accounting treatment in CPL’s accounts, no further disclosure was required. No non-executive director gave evidence that he gave any consideration or proper consideration to the issue of disclosure. Mr Scott also failed to give any consideration to the disclosure of the guarantees as a post balance date event. He undoubtedly *assumed* a number of things, and had a particular mindset, perhaps now formulated by him with the benefit of hindsight. However, he did not consider, or raise the appropriate question, regarding the guarantees. Just because Mr Scott (as with the other directors) was in receipt of general assurances from management and PwC in determining post balance date disclosure, this does not excuse the failure to specifically raise the non-disclosure in view of Mr Scott’s specific knowledge of the guarantees. All that ASIC’s case requires in the circumstances was that each director, aware of the need to disclose post balance date events, and being aware of the guarantees magnitude, make the appropriate enquiries with management.
32. In my view, each director failed to exercise the requisite degree of care and diligence, and failed to take all reasonable steps to comply with the Act in relation to the disclosure of the guarantees as alleged in the amended statement of claim.

# SECTION 295A LETTER

1. I now turn to the operation of s 295A.
2. ASIC contends that the so called management representation letter, when construed, does not comply with the requirements of s 295A. The central representation was as follows:

*We acknowledge the directors’ and management’s responsibility for ensuring:*

*(a) the accuracy of the financial records and the financial report prepared by them; and*

*(b) that the financial report is drawn up:*

*(i) to give a true and fair view of the entity’s financial position as at 30 June 2007 and of its performance, as represented by the results of its operations and cash flows, for the year ended on that date;*

*(ii) in accordance with the Corporations Act 2001; and*

*(ii) to comply with the Australian Accounting Standards, the Australian equivalents to International Financial Reporting Standards (IFRS) as in Note 1 of the Financial Statements, or other authoritative pronouncements of the Australian Accounting Standards Board, Australian Accounting Interpretations of the Corporations Act 2001.*

1. Section 295A of the Act came into effect from 1 July 2004. By subs (1), a directors’ declaration under subs 295(4) must be made only after the CEO and CFO have given the directors a declaration under subs 295A(2). The declaration must state whether in the person’s opinion the matters referred to in subs 295A(2) are correct and must be in the form specified in subs 295A(3). Sub-section 295A(8) states that nothing in s 295A derogates from the responsibility that a director has for ensuring that financial statements comply with the Act.
2. The directors’ declaration is required by subs 295(4)(e) to include a statement that the directors have been given the declarations required by subs 295A.
3. As a matter of construction of the letter and of s 295A, the letter is not a declaration of the opinion of the CEO and CFO as to the matters specified in s 295A(2)(a), (b) and (d) (there were no matters prescribed under paragraph (d)), and therefore does not satisfy the requirements of the section, for the following reasons:
   * + 1. although it is addressed to the directors of CNP and CER (and other entities) as well as to the auditors, it is in its content and form a representation letter to the auditors. This characterisation can be seen throughout the letter starting with paragraph (1), which, to the best of the knowledge and belief of the signatories, having made appropriate enquiries of other officials in the group, confirms the “following representations given to you in connection with your audit...”. The content and expression of the representations that follow are all directed to satisfying the auditors’ requirements;
       2. it acknowledges the directors’ and management’s responsibility for ensuring the accuracy of the financial records and the financial report prepared from them. It does not, as s 295A(2)(a) requires, declare whether in the opinion of the CEO and CFO the financial records of the company, etc, for the financial year have been properly maintained in accordance with s 286;
       3. it acknowledges the directors’ and management’s responsibility for ensuring that the financial report is drawn up to comply with the accounting standards. It does not, as s 295A(2)(b) requires, declare whether in the opinion of the CEO and CFO the financial statements and notes (referred to in s 295(3)(b)) for the financial year comply with the accounting standards; and
       4. it acknowledges the directors’ and management’s responsibility for ensuring that the “financial report” is drawn up to give a true and fair view of the entity’s financial position as at 30 June 2007. It does not, as s 295A(2)(c) requires, declare whether in the opinion of the CEO and CFO the financial statements and notes (referred to in s 295(3)(b)) for the financial year give a true and fair view of the financial position and performance of the consolidated entity (s 297 (b)).
4. This is not a case where substantial compliance, at least at this stage of the proceeding, is in issue, because as Dawson J pointed out in *Hunter Resources Ltd v Melville* (1988) 164 CLR 234, at 249 when discussing the statutory provision in that proceeding:

*… substantial compliance with the relevant statutory requirement was not possible. Either there was compliance or there was not.*

See *Project Blue Sky Inc v Australian Broadcasting Authority* (1998) 194 CLR 355 at 390.

1. It follows that Mr Healey and Mr Scott, acting in accordance with the appropriate delegation of the board, as given at the board meetings on 6 September 2007, signed the declaration for the purposes of s 295(1)(c) of the Act in contravention of s 295A of the Act.
2. However, s 295A of the Act is not a corporation (or scheme) civil penalty provision within the meaning of Part 19.4B of the Act. For ASIC to obtain relief with respect to the contravention of s 295A, it must establish that Mr Scott and the other directors should not have approved the accounts because of the absence of a s 295A declaration, and that by approving the accounts they breached s 180(1) and s 344(1) of the Act.
3. A finding of a contravention of s 295A is therefore a necessary, but not sufficient condition, in respect of the obtaining of a declaration for contravention against the directors in this proceeding.
4. In his affidavit at paras 51, 146 and 147 Mr Scott set out his understanding with respect to the management representation letter and its compliance with s 295A in the following terms:

*[51] In doing so I believe that it satisfied the section 295A requirement. It had been prepared by the chief accountant with I believe PwC input (and with the use of a precedent prepared by PwC). I also thought, that the group’s solicitors, Freehills had reviewed and had input into it (although I cannot recall from where this belief originated). Certainly I regarded the letter and providing for the section 295A declaration, and I believe that the directors and other senior Centro executives (who either signed such a letter such as Nenna and Belcher or who were present when it was tabled, such as Hourigan and Hutchinson) both of whom were former solicitors believed this also. It is referred to in the annual report.*

*[146] I knew that the management representation letter went to both the directors and the auditors. I believe I was guided by the auditors, PwC, the group’s accounting staff, and group’s in-house and external lawyers about what the management representation letter should contain. I took these management representation letters seriously, and they evolved over the years. The gravity which I attached to such letters was the subject of some merriment at the board. I believe that this was because I was thought by some to be over diligent about them.*

*[147] I considered that the management representation letters amounted to a declaration that the financial reports had been drawn in accordance with the Corporations Act, and knew the declaration was included in the annual report texts. That is what I thought I was representing. I thought the statement complied with section 295A. Certainly, the form of the letter was never raised with me as being in any way deficient in terms of its statutory requirements.*

1. The evidence of Mr Belcher who prepared the letter was that the aim was to comply with the relevant provisions of the Act. As indicated from the above evidence, Mr Scott who signed the letter believed that the letter complied with the requirements of s 295A. He also believed that the group’s solicitors had vetted the letter. There was no suggestion that Mr Scott did not hold the necessary opinion required by s 295A at the time of signing the letter. Mr Belcher said that he would not have signed the letter if he did not think that the accounts complied with the Act or accounting standards.
2. The Centro management representation letters were prepared by Mr Belcher using a PwC precedent with involvement from PwC. Draft management representation letters were included in the BARMC packs for the August and September BARMC meetings which were provided to PwC. Mr Cougle, Mr Cronin and Mr Fekete of PwC attended those BARMC meetings at which the draft management representation letters for the Appendix 4Es and the final accounts were tabled and signed. At no time did PwC or Moore Stephens raise any issue with regards to the Centro management representation letters.
3. During the trial, both Mr Hall and Mr Cooper (of the BARMC) gave evidence to the effect that they believed the management representation letters complied with the Act. Mr Cooper’s evidence was that he expected management, including Centro’s general counsel John Hutchinson to “get it right”. Mr Hutchinson had previously been a partner of Freehills. He had also attended the August 2007 BARMC meeting at which the Appendix 4E management representation letter was tabled and signed. Indeed, at that meeting, he presented the internal audit report to the BARMC. The equivalent letter for the final accounts was in the same form. Ms Hourigan, the legally qualified Centro company secretary, was present at both meetings.
4. I accept that the non-executive directors were entitled to place trust in PwC, Moore Stephens, the CFO, Mr Hutchinson, Mr Belcher and Ms Hourigan to ensure that the management representation letter provided to them complied with s 295A of the Act. Each of those people had expertise in the field and by their receipt of draft letters and attendance at BARMC meetings had ample opportunity to detect and inform the directors that the letters did not expressly provide for the opinion required by the section. The question of any possible non-compliance with s 295A was plainly not an issue.
5. It was submitted by the directors that in order to detect the shortcoming which ASIC allege in this proceeding, the non-executive director would have had to look up s 295A themselves, scrutinise its terms, and construe and compare the contents of the draft management representation letters provided to them. It was submitted that the notion of a non-executive director of a large and complex publicly listed corporation undertaking such a process has a complete air of unreality; That this sort of work is the exclusive domain of the financial accountants and general counsel who are employed to ensure that the material which they present to the Board is correct.
6. The requirements of s 295A are succinct and clear. A simple reading of the provision would have indicated what was required. Even a general understanding of s 295A would indicate to a director that a declaration of opinion is required, and not merely an acknowledgement. The management representation letter is not simply a declaration of opinion, and has a different character.
7. The directors had a responsibility to receive the declarations, and declare themselves that they have been given the declarations required by s 295A. No director gave evidence that he himself read or familiarised himself with s 295A of the Act. Mr Scott assumed a state of affairs, and relied upon others. The other directors did the same. In receiving the management representation letter, each director failed to read it properly or at all to ensure compliance with s 295A, before approving the financial statements.
8. I do not accept, as I have endeavoured to explain in relation to other matters, that ensuring compliance with s 295A is the ‘exclusive domain’ of the financial accountants and general counsel. The approach I take may come close to placing a burden on each director akin to each director having not only to take reasonable steps to secure compliance with the Act, but actually complying with the Act. If this is the practical result, it arises out of the nature of the requirements in s 295A and 295(4), and the operation of s 344(1). I do not regard this obligation as onerous.
9. In my view, the directors did not take all reasonable steps to secure compliance with s 295A of the Act, and by approving the financial statements breached s 180(1) and s 344(1).

# CONSEQUENCES OF OMISSIONS

1. I should make mention of the foreseeable consequences arising from the omissions in the financial statements.
2. It was reasonably foreseeable in August and September 2007 that -
   * + 1. the subsequent discovery and correction of a significant error in the classification of current liabilities in the accounts of CPL and CPT could lead to harm to the interests of CPL, CPTM and/or CPT;
       2. a failure to make the required disclosure in the CPL and CPT accounts of significant guarantees undertaken subsequent to the balance date could lead to harm to the interests of CPL, CPTM and/or CPT.
3. The reputation of CNP and CER as well managed and well governed entities was crucial to the maintenance of confidence in them in the financial market. The reputation of the entities was inevitably a matter of concern to the directors. The occurrence of breaches of the Act had the potential to damage the reputation of the entities in the financial market.
4. Further, the revelation that CNP and CER had erred by not disclosing substantial on balance sheet debt liabilities, and that CNP had erred in not disclosing that it had guaranteed substantial off balance sheet liabilities of the US joint venture vehicle, was itself likely to lead to a loss of confidence, regardless of the fact that these also involved contraventions of the Act.
5. A loss of confidence in the management of CNP and CER on the part of investors and other participants in the financial market is itself calculated to affect the market price of the securities of the entities, and therefore the interests of security holders and lenders.
6. The concern of the management that ‘credit issues’, meaning the availability of financial credit, might affect the reputation of the entities, and therefore their standing in the financial market, is shown by an email exchange between Mr Nenna and Mr Scott on 11 July 2007, in which Mr Nenna updates Mr Scott on meetings with relationship banks and particularly concerning the take-out of the JP Morgan bridge facility. Scott responds:

*We need to keep on top of it and ‘listen to the noises’ but not overreact to them. If you want my assistance please do not hesitate to ask as the equity analysts are not being at all kind to us and are trying to beat up stories at the drop of a hat (real or imagined!). I think that any ‘noise’ on credit issues will be reacted to very badly. We will have to keep Phillipa informed as she will have to respond promptly, positively and aggressively to any bad rumours, especially till our gearing is lowered.*

1. Mr Lonergan in his third report referred to the importance of the omitted information to users of the accounts, particularly with respect to the assessment of the value of the securities which were quoted and traded on the ASX. Litigation by shareholders, including class actions, had by 2007 become increasingly common in circumstances where the share price of an entity had declined and there was information which had not been previously disclosed, which might have influenced the price had it been earlier disclosed.
2. It was apparent in 2007 that an error in the accounts of a large publicly listed entity such as CNP or CER, or a failure by either of them to disclose a significant matter, could result in litigation against them. In addition, because they were publicly listed, such an error or failure could also well attract the attention of ASIC and be investigated.

# OTHER MATTERS

## No Case Submission

1. In the course of the proceeding, the directors made an no case submission.
2. I make mention of a ruling I made on the no case submissions of the directors in relation to putting the defendants to their election. I deferred the ruling until the completion and consideration of the no case submission heard during the trial.
3. The no-case submission was rejected. I do, however, make mention that I approached the task upon the basis of the broad principles usefully enumerated by Kaye J in *Oakley and Anor v Insurance Manufacturers of Australia Pty Ltd* [2008] VSC 68 at [3]:

*[3] In my view the authorities, to which I shall shortly refer, establish the following broad principles which should apply to the application which is before me:*

*1. Where a no case submission is made in a trial by jury, the role of the judge is to determine whether, on the view of the evidence most favourable to the party against whom such a submission has been made (“the respondent party”), the jury could (not would) find in favour of the respondent party.*

*2. The test which is applicable, where a judge is sitting without a jury, is less stringent. In such a case the judge may uphold a no case submission, notwithstanding that the evidence, on the view most favourable to the respondent party, could support a judgment in favour of the respondent party.*

*3. In such a case the judge may perform an assessment of the quality of the evidence which has been called on behalf of the respondent party. In some cases, such an assessment may involve the judge evaluating the credit of witnesses from whom such evidence has been called.*

*4. In determining a no case submission, the judge is entitled to draw inferences from the evidence.*

*5. On a no case submission, the judge cannot draw an inference against the party making the submission (“the moving party”) based upon the absence of evidence from that party.*

*6. Although the judge, sitting alone, may assess the quality of the evidence in determining a no case submission, nonetheless the test which is to be applied by the judge, at that stage, is different to the test which the judge would apply in determining the ultimate outcome of the case, at the conclusion of a trial. Notwithstanding that the judge, in determining the no case submission, may assess the quality of the evidence, nonetheless the test remains whether, on the evidence so assessed, the judge “could” (not would) find for the respondent party on the evidence so far led. In such a case, the judge would only find against the respondent party if the evidence, so far adduced, is so unsatisfactory or inherently unreliable or equivocal that he were to conclude that he could not be reasonably satisfied of the case made by the respondent party on the evidence thus far adduced.*

1. I consider these propositions consistent with authority and the decision of the Full Court of the Federal Court in *Rasomen Pty Ltd v Shell Co of Australia* (1997) 75 FCR 216.
2. Whilst deferring the ruling until the completion and consideration of the no case submission, I ruled that the defendants should not be put to their election.
3. The Court has a broad discretion not to put the moving party to its election (or, alternatively, to refuse to hear the no case submission at all) – see *Protean (Holdings) Ltd v American Home Assurance Co* [1985] VR 187at 237; *Rasomen* at 223; *Compaq Computer Australia Pty Ltd v Merry* (1998) 157 ALR 1at 7; *Tru Floor Service Pty Ltd v Jenkins (No 2)* (2006) 232 ALR 532at 537-8; and *ACCC v Amcor* at [62].
4. Considerations relevant to the exercise of the discretion include the following:
   * + 1. A departure from the general rule can seldom be justified unless adherence to the rule would not serve the ends of justice or convenience – see: *Protean* at 238 (citing *Sampson v Richards* [1949] VLR 6); *Jones v Peters* [1948] VLR 331; and *ACCC v Amcor* at [62]);
       2. The Court will have regard to all the circumstances of the case, including the nature of the case, the stage it has reached, the issues involved and the evidence given – see: *Protean* at 238; *William H Muller & Co v Ebbw Vale Steel, Iron & Coal Ltd* [1936] 2 All ER 1363 at 1365-6 (quoted with approval in *Rasomen* at 223); and *ACCC v Amcor* at [62]).
       3. Regard should be had to whether, in all the circumstances of the case, putting the party to its election will result in the most efficient resolution of the proceeding – the Court will consider whether putting a party to its election will lead to the party unnecessarily leading the remainder of its evidence or, conversely, whether not putting the party to its election may result in a real risk that the Court will be required to consider the same evidence twice – see: *William H Muller* (quoted with approval in *Rasomen at* 223); *Compaq Computer* at 9; *Tru Floor* at 540 (paras [27] and [28]); *Australian Competition and Consumer Commission v Leahy Petroleum Pty* [2009] FCA 1678at [92]; and *ACCC v Amcor* at [71] and [72].
       4. Departure from the general rule may be justified where the case alleges fraud or dishonesty – in those circumstances it would normally be wrong to permit a defendant to be cross-examined where there really is no evidence against him/her of fraud – see *Union Bank of Australia v Puddy* [1949] VLR 242 at 245-6 (quoted in *Tru Floor* at 538); *Protean* at 215 and 236; *Compaq Computer* at 7 and 9; *Tru Floor* at 540 (paras [28] and [29]).
       5. Similarly, in *ACCC v Amcor*, Sackville J considered that defendants accused of serious breaches of the *Trade Practice Act 1974* (Cth) which would render them liable to substantial civil penalties (and also cause potential loss of business reputation), and that the allegations were analogous to a fraud case, were reasons why the defendants should not be put to their election: see *ACCC v Amcor* at [67]-[68].
       6. Justice Davies in *Trade Practices Commission v George Weston Foods Ltd (No 2)* (1980) 43 FLR 55*,* rejected the fact that the proceeding was a civil penalty proceeding as a ground for not putting the defendants to their election. He nevertheless took into account as a matter to be considered that the allegation is one that calls for a standard of proof consistent with the seriousness of the allegations made.
5. In the end, I considered the case to be such that the interests of justice required the directors to be permitted to make a no case submission without being put to their election.
6. I was particularly mindful of the considerations that led Sackville J in *ACCC v Amcor* to a similar view.
7. As was the position taken by Sackville J, I took the view that this was a case in which serious allegations of contraventions of the Act had been made against each of the defendants. If the allegations were to be established, the directors would be exposed to pecuniary penalties. Adverse findings might well have serious consequences in terms of loss of business reputation.
8. The authorities recognise that a departure from the general rule is often justified where fraud is alleged against the moving party. In *The Union Bank of Australia Ltd v Puddy*, Fullagar J said (at 246) that where fraud is alleged:

*… it may often be wrong to suggest that a party should submit himself to cross-examination before it is seen that there is really some evidence against him.*

See also *Protean*, at 215, per Young CJ; at 236, per Fullagar J; and *Compaq*, at 7.

1. Whilst fraud is not alleged in this proceeding, in my opinion it is analogous to a fraud case by reason of the very serious allegations that have been made against each of the directors: see *George Weston*, at 61; *Trade Practices Commission v Nicholas Enterprises Pty Ltd* [1978] ATPR 40-097 (Fisher J), at 17,958.
2. It was also apparent from the contentions advanced by the directors that the no case submission could be addressed by me without having to assess the credit of any of the witnesses.
3. Finally, all directors sought to put a no case submission. This was not a case where only some of the defendants wished to make the submission. If that had been the position, there would have been difficulties in entertaining the submission without requiring those directors wishing to advance it not to call evidence.
4. Another issue arose because application was also made by the directors under s 31A of the *Federal Court of Australia Act* 1976 (Cth). I proceeded on the basis that whether application was made in reliance on the summary judgment power in s 31A or pursuant to the power in O 35 r 1 of the Federal Court Rules, the party making the application should as a general rule, be put to its election not to call evidence. This is because:
   * + 1. putting the moving party to its election is the general rule of practice;
       2. the practice is for the benefit of the court in relation to the just and convenient disposition of the proceeding, and is to be departed from by reference to that consideration;
       3. section 31A is a discretionary power and expressly does not limit any of the other powers of the Court (s 31A(4));
       4. there is no reason why the practice should not apply to an application under s 31A where that application is one which is, in substance, a no case application.
5. I should also say that s 31A is an appropriate source of power for summary judgment, even though a trial has commenced. Nothing said in *Spencer v The Commonwealth* (2010) 241 CLR 118 precludes s 31A being such a source of power in the appropriate circumstances. It may not be appropriate to exercise the power during a trial, and it may be rare for the occasion for its exercise to arise, but this does not deny the power existing.
6. A Court may, for example, dismiss a claim after hearing some evidence, without undertaking the further steps and delays of a full hearing. This would still be summary judgment.
7. Undoubtedly, s 31A was designed to deal with cases that were not fit for trial at all (see Lord Woolf in *Swain v Hillman* [2001] 1 All ER 91, at 95). However, there may well be situations where the ‘unmeritorious’ nature of a case becomes apparent just after a trial commences. I see no reason to preclude s 31A from being available in such circumstances. Its terms are not limited to interlocutory applications or to pre-trial situations.

## Mr Rich

1. The subject of an email sent to Mr Purdon (a senior investigator at ASIC), on behalf of Mr Stephen Rich (an analyst at UBS), was raised during the course of the trial.
2. The email was a response to questions posed to Mr Rich by Mr Purdon during the course of ASIC’s investigations into the Centro group (prior to the commencement by ASIC of this proceeding), relating to what impact the omissions alleged in this proceeding, would have on the market.
3. The relevant questions and answers contained in the response email from Mr Rich were as follows:

*1. When CNP announced the New Plan acquisition on 28 February 2007, did he understand that the deal was being partly financed by short-term debt?*

*I believe the market was made aware that there was a bridging finance component.*

*2. On 7 May 2007, CNP made a presentation titled “Transactions Implement Business Model”. Page 22 of the presentation indicated that the US$3.7bn purchase price will be funded by a US$1.2bn loan from banks and US$2.06 in committed financing. Did he understand that all of this funding was short-term bridging finance? If not, would this have made a difference to this assessment of the price or value of CNP?*

*I’m not sure whether I was aware at the time that all of this funding was short term bridging finance. However, my thoughts on the deal were fairly negative, so further knowledge would simply have made me more bearish, but I’m not sure it would have affected my valuation of the stock (I was at Deutsche Bank at the time).*

*3. When Centro released its Appendix 4E of 9 August 2007, the on-balance sheet interest bearing liabilities was shown wholly as non-current. However, when Centro released its Annual Report on 18 September 2007, the on-balance sheet interest bearing liabilities were now classified $A1,096,936,000 as current and the rest as non-current. Did he note this at the time? If yes, did this impact on his assessment of the price or value of the CNP shares?*

*I do not recall noticing the shift in treatment immediately, but I believe it was subsequently brought to my attention, I cannot recall the exact date. I believe this information would have been worthy of consideration in terms of calculating a fair value of securities. However, it is unlikely we would have immediately changed our valuation or Price Target. More likely to factor into our next re-assessment of value.*

*4. If, on 9 August 2009, CNP had announced at its presentation of its annual financial results, that it had in excess of A$4.8bn worth of interest bearing liabilities that were maturing in less than 6 months but CNP was very confident that this debt could be repaid or re-financed before maturity, would that have affected his assessment of the price or value of CNP at the time? If so, why?*

*Having recently moved from Deutsche Bank, I was in the process of working with Simon Garing to transition coverage and merge our views on the name. As credit markets had begun to tighten we were interested in the level of short term expiries. At the time, we were much more accepting of company confidence that we would be today. As such, we probably would have accepted the company’s confidence and not altered our valuation but would have been increasingly wary of other expiring facilities that may have provided lead indicators of any further financial difficulty.*

1. During the course of the trial, I thought it appropriate that Mr Lonergan should consider the views expressed by Mr Rich for the purpose of determining whether those views affect the opinions Mr Lonergan had given in his expert reports (in particular, his third report).
2. Mr Lonergan in a further affidavit dated 12 April 2011 concluded as follows:

***No impact on my opinion***

*58 Mr Rich’s comments in the Email have no impact on my opinion. My reasons why that is so include:*

*(a) they responded to questions different from questions that I was asked*

*(b) they appear to only reflect his generalised and uncertain recollections or qualified view*

*(c) they contained no supporting evidence, analysis or reasoning*

*(d) Mr Rich was not provided with information consistent with ASIC’s Amended Statement of Claim*

*(e) some of the questions put to Mr Rich are either materially incomplete (in terms of the current issues being heard) and/or inconsistent*

*(f) Mr Rich was not asked to, and did not opine on, the matters that are the subject of the Reports.*

*59 Put simply, in my view, Mr Rich was apparently not given all the relevant information, and his responses to the questions asked apparently provided only ‘general recollections’ in his responses.*

1. I do not think it necessary to comment further upon the email from Mr Rich. It was discovered by ASIC, so there is no question of it being concealed from the defendants. It was not suggested that fairness required ASIC to call Mr Rich as a witness. I agree with Mr Lonergan’s assessment of the email. Even without Mr Lonergan’s evidence, I would have made the same assessment of the contents of the email. I put no weight at all on the views of Mr Rich as expressed in the form found in the email.

## Cross-examination of the directors

1. A number of times during submissions, Senior Counsel for Mr Scott particularly, contended that a number of matters were not put to the directors, and that such matters not put could not be relied upon by ASIC.
2. I do not accept this submission. First, before each director gave evidence prior notice was clearly provided, by way of the pleadings, the opening, the evidence and in the course of the no-case submission, of ASIC’s case: see eg *Kennedy v Wallace* (2004) 142 FCR 185; (2004) FCAFC 337 at 56.
3. Secondly, in relation to the rule in *Browne v Dunn* (1893) 6 R 67, as Mason P explained in *Scalise v Bezzina* [2003] NSWCA 362 at [98] (Santow JA with Brownie AJA agreeing):

*The rule does not undermine the adversary nature of proceedings or make one party the other’s keeper. Thus, a party who proves facts sufficient to establish a cause of action or a defence upon which that party bears the onus does not have to confront the other side’s witnesses with the issue if they do not address it in their own evidence. To require this would invert that aspect of the rule grounded in what I have described as judicial economy. There is no unfairness in letting the sleeping dog lie and also invoking* Jones v Dunkel *(1959) 101 CLR 298 so long as the moving party has by pleadings or otherwise signalled the matter sought to be proved and led necessary evidence on the topic. There is no need to confront an opponent’s witnesses by cross-examination if they fail to contradict evidence earlier called by the moving party in support of an issue raised in the pleadings or otherwise….*

1. In my view, even recalling this is a civil penalty proceeding, the fact that the directors were not examined in chief on some topic, does not impose an obligation on ASIC to confront them to the extent submitted by the directors. In fact, the directors would be expected to provide evidence, which was peculiarly within their knowledge, of the extent to which they read and understood the accounts, the accounting standards and the Act: see eg *Commercial Union Assurance Co of Australasia Ltd v Ferrcom Pty Ltd* (1991) 22 NSWLR 389 (CA) at 418-419 per Handley JA; *Freeman v Health Insurance Commission* (1997) 78 FCR 91 at 98-99; *White Industries (Qld) Pty Ltd v Flower & Hart (a firm)* (1998) 156 ALR 169 at 226-229 per Goldberg J; and *Prentice v Cummins (No 6)* (2003) 203 ALR 449; [2003] FCA 1002 at [77]-[80] per Sackville J (where a witness ‘elected to give no evidence’ in respect of a particular issue).
2. I observe that in criminal cases, in such circumstances, even if described as unusual, the failure to present evidence (whether it be by calling a witness or by failing to examine a witness in chief on some topic) may call for an inference that further examination in chief on the topic may have exposed unfavourable facts: see eg *Dyers v The Queen* (2002) 210 CLR 285 at [9]-[10] and [15] per Gaudron and Hayne JJ.
3. Of course, at all times, ASIC has the onus of proving its case on all elements. No failure to call evidence, or to examine in chief more comprehensively on some topics, can fill in the gaps of any failure to prove those elements.
4. In this proceeding, as it eventuated, the evidence was relatively uncontroversial. No issue of credit arose. I did not draw inferences against the directors because of any failure to examine in chief on some topic. However, I did not draw inferences in favour of the directors where their legal representatives specifically refrained from presenting evidence peculiarly within each director’s knowledge as to what they knew, read or understood.

# REALITY CHECK

1. The directors have contended on a number of occasions that ASIC’s contentions in this proceeding lack any sense of reality, and embrace a counsel of perfection. The directors say that all the processes that could have been undertaken and all the advices that could have been obtained were in fact undertaken or obtained. They accepted that directors cannot abdicate their responsibility, but it was argued by the directors that they fulfil such responsibility by adopting processes and relying on proper advice. It was argued that ASIC in this proceeding seeks to extend the responsibility of directors well beyond reasonable financial literacy and a proper degree of engagement in the affairs of a company. The directors point to the fact that at the time, the errors were not detected by anyone in Centro’s accounting team, PwC, or by any of the directors. The directors submitted that the more the issues are scrutinised, the more difficult they seem to be.
2. I do not accept these matters are determinative in the proper consideration of the issues before me.
3. Part of ASIC’s case is that the apparent errors were so obvious that it can more readily be inferred that it was negligent for the directors to have failed to detect them. After all, each director was intelligent and sufficiently financially literate, having many years of experience analysing financial statements. Further, the year 2007 was not the first time each director had to read and understand accounts, even with the change in accounting standards.
4. Whilst there are many matters a director must focus upon, the financial statements must be regarded as one of the most important. As I have said repeatedly, a director must at least understand the terminology used in the financial statements, and in this proceeding this related to the classification of liabilities and disclosure of events occurring after the balance date.
5. It may be that in the course of this trial the directors have been able to show others had difficulties with the issues confronting the directors in 2007.
6. The first point to observe is that the directors themselves were not distracted by the various so called complicated issues raised now in this proceeding. Each director relied completely on the processes in place and their advisors. All the directors failed to see the ‘obvious errors’ because they all took the same approach in relying exclusively upon those processes and advisors. No director stood back, armed with his own knowledge, and looked at and considered for himself the financial statements.
7. The second point to make is that as far as the other persons who fell into error are concerned, the Court in this proceeding cannot adequately determine the reason for this occurring. Every person referred to by the directors as having fallen into error, had different roles to play, and had various levels of information available to them.
8. Some may well have had limited knowledge of the facts, or themselves failed to take sufficient care. Mr Nenna has acknowledged that he failed to take sufficient care. The mere fact that others (perhaps many others) fell into error does not assist in determining the key issue in this proceeding relating to the conduct of the directors.
9. The final point to observe, is that ASIC does not allege, as I have previously indicated, that the directors needed to get it right or that they needed to realise that the information available to them was ‘necessarily’ indicative of error (as the directors would frame the issue). All that is being alleged is that they should have detected the apparent error, and acted accordingly, by for instance, asking the appropriate question of management.
10. Therefore, I do consider that all that was required of the directors in this proceeding was the financial literacy to understand basic accounting conventions and proper diligence in reading the financial statements. The directors had the required accumulated knowledge of the affairs of Centro, based upon the documents placed before them and discussion at board meetings. Each director then needed to formulate his own opinion, and apply that opinion to the task of approving the financial statements.

# CONCLUSION

1. In light of the above findings, there has been a failure to comply with the relevant AASB’s, and a failure to give a true and fair view, contrary to the provisions of s 296 and 297, and a failure to disclose information in the terms of s 299 and 299A so as to not comply with s 298.
2. ASIC in its submissions made an individual analysis of contraventions in relation to each director. However, ASIC’s case was based upon a central proposition concerning the duty of directors to properly read and understand the financial statements and to apply the knowledge they had or should have acquired to perform that task.
3. Based upon the evidence, which in the main was uncontroversial, each director did not take all reasonable steps to focus and consider for himself the content of the financial statements, particularly as to short-term debt and whether the guarantees should have been disclosed.
4. Each director failed to make enquiries of management, the BARMC or other directors as to proposed statements in the financial statements relating to the short-term debt and guarantees, and failed to have apparent errors corrected.
5. Each director failed to request that the directors be given declarations pursuant to s 295A of the Act which accorded with its requirements, after failing to consider the requirements of s 295A and read the management representation letter.
6. I have already found that each director knew of the current interest bearing liabilities and of the guarantees. Each director was aware of or should have been aware of the relevant accounting principles which would have alerted each director to the apparent error in the proposed financial statements. Each director could then and should have made the relevant enquiries, if they had taken all the reasonable steps required of them. The directors did not focus upon or properly consider the issues the subject of ASIC’s allegations. Each director may have had different reasons for not focusing. For instance, Mr Scott did not focus, as he was concentrating on the key risk areas and investors, and did not consider the existence of current debt liabilities as a problem. Mr Scott considered that the concern of investors at the time was with total liabilities. Mr Scott *assumed* that management and the advisors would bring to his attention any information necessary, and did not turn his mind specifically to the guarantees or to short-term debt.
7. The other directors relied solely on management and their advisors to be properly informed of information relevantly to be put into the financial statements.
8. The differences between the individual analysis of each director provided by ASIC, in my view, do not detract from the above position pertaining to each director and the findings I make. Whether, for instance, a director went through the financial statements ‘line by line’, he is not thereby taking all reasonable steps, if the director in doing so is not focussed for himself upon the task and considering for himself the statutory requirements and applying the knowledge he has of the affairs of the company.
9. The failure to notice certain omissions may well be explicable – but here the directors, in some cases on their own admission, clearly looked solely to management and external advisors. If they had acted, as Senior Counsel for ASIC suggested, as the final filter, taking care to read and understand the financial accounts, the errors may have been discovered earlier than they were.
10. In relation to each director in his capacity as a director (or officer) of each relevant entity as pleaded in the amended statement of claim and to the extent relief is sought in the amended application, I find that each director failed to take the following reasonable steps and failed to take the following steps that a reasonable person would have taken if they were in the director’s position:
11. to properly read, understand and give sufficient attention to the content of the financial statements prior to participating in the resolutions occurring on 6 September 2007 in so far as they related to:
12. the classification of liabilities as either current or non-current;
13. the disclosure of guarantees relating to Super LLC and Centro NP LLC.
14. to consider or properly consider the content of the financial statements prior to participating in the resolutions occurring on 6 September 2007 in so far as they related to:
15. the classification of liabilities as either current or non-current;
16. the disclosure of guarantees relating to Super LLC and Centro NP LLC.
17. to raise or make enquiry or adequate enquiry with management, the BARMC and other members of the Board prior to participating in the resolutions occurring on 6 September 2007:
18. the apparent failure of the financial statements to properly classify current and non-current liabilities;
19. the apparent failure of the financial statements to properly disclose the guarantees relating to Super LLC and Centro NP LLC.
20. to have the apparent failures with respect to the financial statements corrected prior to participating in the resolutions occurring on 6 September 2007;
21. prior to participating in the resolutions on 6 September 2007;
22. to take the necessary steps to ensure they had a sufficient knowledge of the requirements of s 295A;
23. to read, understand and give sufficient attention to the management representation letter provided to the directors;
24. to request that the directors be given a declaration pursuant to s 295A of the Act which accords with its requirements.
25. not participating in the resolutions occurring on 6 September 2007 prior to being given a declaration pursuant to s 295A of the Act.
26. In these circumstances, each director in relation to the allegations pleaded in the amended statement of claim and to the extent relief is sought in the amended application contravened ss 180(1), 601FD(3) and 344(1) of the Act in that:
27. each director failed to take all reasonable steps to secure compliance with each of the provisions of the Act alleged against them;
28. each director failed to take all steps that a reasonable person would take if they were in each director’s position to ensure compliance by the relevant entity with each of the provisions of the Act alleged against them;
29. each director failed to exercise the degree of care and diligence required by failing to take each of the steps I have found that each director failed to take in the course of his review of the financial statements.
30. Once the Court is satisfied that a person has contravened the above provisions, it must make a declaration of contravention (see s 1317E).
31. Section 1317E(2) provides that the declaration must specify the following:
32. the Court that made the declaration;
33. the civil penalty provision that was contravened;
34. the person who contravened the provision;
35. the conduct that constituted the contravention;
36. if the contravention is of a corporation/scheme civil penalty provision - the corporation or registered scheme to which the conduct related.
37. In relation to Mr Nenna, declarations will need to be made based on his admissions and my conclusion that the information required by s 299A of the Act needed to be included in the financial statements.
38. I will ask the parties to confer and consider appropriate declarations to accord with my findings in light of the relief sought in the amended application. The declarations will need to be made by reference to each defendant, the relevant entity, the provision contended and the conduct involved as I have described it in these reasons.
39. I propose to adjourn this proceeding to allow the parties to submit minutes so that the declarations can be made and to formulate minutes for the purposes of the hearing of relief from liability and penalty (if any) to be heard on 1 August 2011.

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| I certify that the preceding five hundred and eighty-nine (589) numbered paragraphs are a true copy of the Reasons for Judgment herein of the Honourable Justice Middleton. |

Associate:

Dated: 27 June 2011