

# LegalTalk

Electronic Bulletin  
of Australian Legal  
Developments

Issue 30: December 2008

PRICEWATERHOUSECOOPERS 



## New Cartel Legislation

On 27 October 2008, the Assistant Treasurer and Minister for Competition Policy and Consumer Affairs released the final version of the *Trade Practices Amendment (Cartel Conduct and Other Measures) Bill 2008*. The Bill will introduce criminal penalties for cartel behaviour, bringing Australia in line with the United States and the United Kingdom. The proposed changes to amend the *Trade Practices Act 1974* are expected to be introduced into Parliament in its current session. The criminal penalties will be in addition to the existing civil penalties. The civil prohibitions have also been amended to parallel the new criminal offences.

### Current civil regime

Under the existing laws, corporations who engage in cartel behaviour face fines of up to \$10 million or three times the value of the illegal benefit gained from the cartel, or where that cannot be ascertained, 10 per cent of the corporate group's annual turnover in the preceding twelve months, whichever is greater.

An individual who is found to have engaged in cartel behaviour currently faces a maximum fine of \$500,000 per offence.

### New criminal penalties

Under the proposed changes, the maximum penalty for an individual found guilty of cartel conduct will be a 10-year jail term or a fine of \$220,000. The penalty for a corporation will be the same as the fines that currently apply to corporations.

### Elements of the new criminal offences

The final Bill makes it an offence for a corporation to make or give effect to a contract, arrangement or understanding between competitors that contains a provision to fix prices, restrict outputs, divide or share markets, or rig bids. The government has decided that the offences should not include the words 'with the intention of dishonestly obtaining a benefit', which were included in the Exposure Draft released in January this year. Submissions made to Government indicated that this subjective 'dishonesty' test would confuse juries and make it more difficult to bring successful criminal prosecutions for cartel conduct. Of all the countries which have criminalised cartel conduct (including the United States, United Kingdom, Canada, France, Germany, Ireland and Japan), only the United Kingdom has retained a dishonesty test. There has only been one successful prosecution in the United Kingdom.

Instead of the 'dishonesty' test, the final Bill applies fault elements under the Commonwealth Criminal Code (intention and knowledge or belief)

## Inside this issue

New Cartel Legislation	1
'Disassociate Yourself' – cancellation and winding up of incorporated associations	3
Do your sub trusts exist at law? Common structures which should be avoided	5

to the offences. According to the Government, this will ensure that the burden of proof is high enough to catch only serious offenders but also that the fault element is not used as an escape clause.

## Parallel civil prohibitions

The Government will introduce a parallel regime of civil prohibitions on serious cartel conduct for corporations and individuals. These civil prohibitions will contain the same elements as the new criminal offences and will replace the existing civil prohibitions in the *Trade Practices Act 1974*. The differences will be that the criminal offences will require proof of the elements of the offence ‘beyond reasonable doubt’, and that certain ‘fault’ elements will be automatically applied under the Commonwealth Criminal Code.

To minimise double jeopardy concerns, the Government will also enable civil proceedings to be postponed until criminal proceedings are completed. If the defendant is convicted, the civil proceedings will be terminated.

## Cartel provisions

The final Bill has changed the tests for determining whether a

provision of a contract, arrangement or understanding qualifies as a cartel provision and is prohibited. The amendments bring the tests in line with the tests that apply under the existing civil prohibitions in the *Trade Practices Act 1974*, upon which the new cartel prohibitions have been modelled.

For a breach involving price-fixing, the test now provides that the provision must have had the purpose, effect or likely effect of directly or indirectly fixing prices. For a breach comprising other forms of serious cartel conduct (output restrictions, market sharing or bid rigging), the test now provides that the provision must have had the purpose of directly or indirectly restricting outputs, sharing markets or rigging bids.

## Civil or criminal?

Under the new legislation, the Australian Competition and Consumer Commission (ACCC), in conjunction with the Director of Public Prosecutions, will be required to decide at an early stage whether to pursue a criminal or civil case. A criminal charge will provide the ACCC with greater powers, including the power to arrange for the Australian Federal Police to intercept telephone

calls between suspected cartel participants, if the ACCC can obtain a warrant from the Australian Federal Court. However, a criminal charge means that the ACCC will have to prove their case to a jury ‘beyond reasonable doubt’, a higher burden of proof than the civil ‘balance of probabilities’ standard.

## Joint venture exemption

The final Bill contains specific exemptions for joint ventures to both the civil prohibitions and the criminal offences. If a cartel provision is for the purposes of a joint venture and the joint venture is for the production and/or supply of goods or services, then it is not caught by the proposed new cartel laws. The reference to a joint venture is a reference to an activity in trade or commerce that is carried on:

- (i) jointly by two or more persons who are party to the contract, whether or not in a partnership or
- (ii) by a body corporate formed by the parties to the contract for the purpose of enabling those parties to carry on that activity jointly, by means of their joint control or their ownership of shares in the capital of that body corporate.

## Partnerships and unincorporated structures

Partnerships and any other unincorporated businesses which do not fit within the joint venture exemptions may be caught by the proposed civil and criminal prohibitions. While the *Trade Practices Act 1974* is primarily based on the corporations power, section 6(2) provides an alternative based on the trade and commerce power and the territories power. Professionals are subject to the provisions in Part IV of the *Trade Practices Act 1974* (including the proposed new cartel provisions, when passed) if:

- their conduct is in, or in relation to, trade or commerce between Australia and other countries
- their conduct is in or across Australian state or territory boundaries or within Australian territories, or
- they supply services to the Commonwealth or its authorities and instrumentalities.

Section 6(3) extends the *Trade Practices Act 1974* to individuals to the extent that it is possible to do so based on the post and telegraph power. However, as a result of the uniform *Competition*

*Policy Reform Acts* passed by all states and territories, the provisions in Part IV of the *Trade Practices Act 1974* (including the proposed new cartel provisions, when passed) are applicable to individuals in any event. Individual partners, sole traders and the individuals who comprise an unincorporated business need to carefully consider any ‘joint venture’ that involves competitors.

## Conclusion

As well as having the harshest anti-cartel laws in the world alongside the United States, the removal of ‘dishonesty’ as the mental element for criminal cartel conduct reflects how gravely the Australian Government regards this kind of conduct. The possibility of criminal sanctions for company executives will be more of a deterrent for businesses that may otherwise rationalise corporate fines for cartel conduct as the ‘cost’ of doing such business.

For further information please contact your usual PricewaterhouseCoopers adviser or:



**Michael Daniel, Partner**  
Phone: +61 (2) 8266 6618  
michael.daniel@au.pwc.com

# ‘Disassociate Yourself’ – cancellation and winding up of incorporated associations

## What are incorporated associations?

There are over 39,000 registered incorporated associations in NSW, typically involved in areas such as charity, sport, education or community services. There are incorporated associations registered in NSW dealing with everything from UFO research to social policy.

Incorporated associations are normally very small bodies. According to the New South Wales government, approximately 60% of incorporated associations in New South Wales have a turnover of less than \$100,000, and only 2% have a turnover of more than \$500,000.

In general, an incorporated association is not permitted to trade or make a pecuniary gain for its members. There are exceptions to this rule, for example trading for charitable purposes or reasonable remuneration of employees.

Under the *Associations Incorporations Act 1984 (NSW)* (“the Act”), an incorporated association must have at least five members but there is no upper limit of members.

Reporting requirements for incorporated associations include annual lodgments with the Office of Fair Trading. While reporting requirements for not-for-profit organisations appear to be quite onerous, incorporation provides the following important advantages for members:

- limited liability for members of the association
- the entity continues to exist despite changes in membership
- incorporation gives the organisation ‘legal personality’ which means that the organisation can enter into agreements, including buying and selling land.

Also, some grants stipulate that in order for the organisation to be eligible to be granted money, the association must be incorporated.

## NSW Government review of the Associations Incorporations Act

The NSW Government is reviewing the incorporated associations legislation in

order to keep the legislation in line with current practices and other state and territory legislation. A draft exposure bill was released earlier in the year, for which public submissions closed in April. The proposed changes were wide-ranging, from imposing statutory duties of diligence and honesty on members, to eradicating the need for a separate public officer and secretary.

One of the drivers for legislative review is that a number of incorporated associations are no longer operating but are still registered. In fact, the model rules for incorporated associations do not provide for winding up or cancellation. Under the Act, there are three different methods of cancelling or winding up an incorporated association.

## 1. Cancellation of Incorporation

Before the new Associations Incorporation Act takes effect, the Government has enacted the *Associations Incorporation Amendment (Cancellation of Incorporation) Act* to simplify the requirements for cancellation of incorporation.

The amendments widen the powers of the Director-General of the Office of Fair Trading to cancel incorporation of an incorporated association. The Act already set out grounds upon which the Director-General will cancel registration, but the new grounds for the Director-General include:

- the association does not have at least five members
- the association has not lodged financial statements for the past three years
- the association does not have a public officer.

The Director-General must give notice to the incorporated association that it is to be cancelled, and the grounds upon which the association is cancelled, as well as giving the association and its members a chance to make submissions about the proposed cancellation.

## 2. Voluntary winding up

Under section 50(1) of the Act, the members of the association can agree to wind up the association voluntarily, by special resolution. The incorporated association should also make a statement indicating how any property will be distributed.



The Act imports provisions from the *Corporations Act (2001) Cth* for the procedure for voluntary winding up. Accordingly, like corporations regulated by the Corporations Act, incorporated associations may be wound up by members' voluntary winding up, where a solvency declaration can be made by the members. A solvency declaration is where the members state that the incorporated association will be able to pay its debts and liabilities.

## 3. Winding up by a court

Section 51(1) of the Act sets out when the Court may order a winding up, including, for example, if an incorporated association has traded or secured pecuniary gain for its members, or engaged in activities inconsistent with its statement of objects.

An application to the Court for winding up may be made by a member or creditor of the incorporated association, or by the Director-General (section 51(2)). Section 51(3) then goes on to state that the Corporations Act provisions in relation to winding up apply to incorporated associations.

### 'Unable to Pay its Debts'

Perhaps the most important reason the Court may order a winding up of an incorporated association is when an incorporated association is "unable to pay its debts" (section 51(1)(c)).

The Corporations Act contains a simple procedure for determining whether a company can pay its debts. If a company is served with a statutory demand which it does not challenge and does not pay, there is a presumption that the company cannot pay its debts as and when they fall due.

While it may be expected that the statutory demand method of proving that an incorporated association is unable to pay its debts would be open to creditors of incorporated associations, this is not the case. Put simply, the Supreme Court of New South Wales has held that only the *Associations Incorporation Act*

can set out when a Court can order a winding up, and an incorporated association not responding to a statutory demand is not one of those instances. Accordingly, any application to the Court by a creditor on the basis that a statutory demand has not been paid will be dismissed by the Court.

## Conclusion

Despite the number of incorporated associations in New South Wales, their cancellation or winding up is not always well understood.

Only the *Associations Incorporation Act* can set out when a Court can order a winding up, and an incorporated association not responding to a statutory demand is not one of those instances.

For further information please contact your usual PricewaterhouseCoopers adviser or:



**Michael Daniel, Partner**  
Phone: +61 (2) 8266 6618  
michael.daniel@au.pwc.com

# Do your sub trusts exist at law? Common structures which should be avoided

## Introduction

Trusts are increasingly popular in structuring investments and projects to manage risks, as flow-through vehicles for tax purposes, and for flexibility of the distribution of trust income and the transfer of interests.

However, the use of trusts for business and investment purposes is governed by complex and at times ambiguous laws. One aspect of trust law which can bring unintended commercial consequences if not properly managed is the operation of the doctrine of merger and the consequential extinguishment of trusts.

## Merger and the extinguishment of trusts

A trustee of a trust can be a beneficiary of that trust, provided it is not the sole beneficiary. Where the trustee of a trust is also the sole beneficiary of that trust, the trustee will be holding both the legal and equitable interest in the trust property and the two interests

merge at law and any purported trust is extinguished.<sup>1</sup>

The reason for this result is the common law doctrine of merger, which provides that when a lesser legal estate (such as a beneficial interest, or that of a beneficiary of a trust) becomes vested in an entity who holds a greater estate in the same right (such as the legal interest, or that held by a trustee of a trust), the lesser estate merges into the greater and is extinguished. In other words, an entity that holds a legal interest in property cannot be regarded as holding both the legal and equitable interests in that property. In such circumstances, the entity's beneficial ownership is inherent in the legal ownership and there is no need to postulate a separate equitable ownership.<sup>2</sup>

Another reason for extinguishment of a beneficiary's equitable interest is based on the impossibility of a supposed sole trustee being subject to any obligation to himself or herself as a sole beneficiary.<sup>3</sup> In other words, a person cannot owe the equitable

obligations of a trustee to himself or herself alone.

## Situations where extinguishment of a trust may arise

Consider the situation where two trusts are established for a new venture, a head trust and a subsidiary trust (sub trust). For convenience, the same corporate entity (Company A) is appointed as trustee of both the head trust and the sub trust. In its capacity as trustee for the head trust, Company A is also the sole beneficiary of the sub trust (see diagram 1).

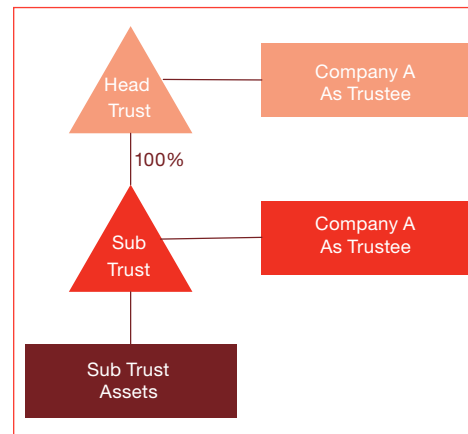


Diagram 1

As discussed above, where both the trustee and the sole beneficiary of the sub trust is the same entity (being Company A, albeit in different

capacities), the legal and equitable interests over the sub trust property would merge, causing the sub trust to collapse and the sub trust property to vest in Company A in its capacity as trustee of the head trust (see diagram 2). This may have profound and unintended consequences for the ownership of trust property and the legality and validity of any dealings with the trust property of the merged sub trust.

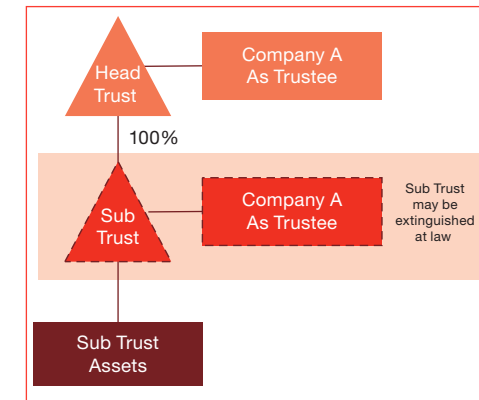


Diagram 2

## The intention that there should be no merger

Despite the rigidity of the common law, *“in equity there would be no merger if the relevant persons intended, or the circumstances raised a presumption of intention, that there should be no merger.”*<sup>4</sup> The equitable rule now

prevails in legislation derived from the *Judicature Act 1873* (UK). In particular, section 10 of the *Conveyancing Act 1919* (NSW) states:

*“There shall not, after the commencement of this Act, be held or deemed to be any merger by operation of law only of any estate, the beneficial interest in which would not be deemed to be merged or extinguished in equity...”*

Under the equitable rule, the sub trust in the scenario above may be saved from merger and extinguishment by establishing the requisite intention for the creation and existence of a separate sub trust.

## Establishing the requisite intention

Establishing intention is a construction of fact and must be determined on a case by case basis.

An example where the requisite intention may be established is where it is contemplated that additional units in the sub trust will be issued to third parties in the future. One commercial reason for separating trusts in such a structure may be to enable future investors to invest in the activities of the sub trust in isolation from the rest of the structure

(ie without exposure to or interest in the activities of the head trust or any other sub trusts). Another reason may be the possible incentivisation of the management team of the sub trust business through the issue of units in the sub trust to those persons.

In this scenario, the equitable rule protects the sub trust from extinguishment during the initial period when the trustee entity, in its capacity as trustee of the head trust, is also the sole unit holder of the sub trust. If the intention is clearly for potential investors to subscribe for additional units in the sub trust, then there is strong argument for the intention of no merger, otherwise, the commercial advantages of setting up the sub trust would potentially be defeated by the operation of the doctrine of merger.

## Conclusion

The doctrine of merger can have material unintended consequences on the assets held by sub trusts in certain circumstances. It may also affect the validity of the dealings in relation to sub trust property by the trustee.

Unless there are clear commercial reasons for appointing the same entity as the trustee of a head trust and a sub trust, it is prudent not to do so.

Where such a structure has already been established, careful analysis of the overall business or investment structure and the material facts on a case by case basis will be necessary to determine whether requisite intention can reasonably be established under equity in order to determine whether the sub trust exists at law. Alternatively, a reorganisation of the trustee arrangements may be necessary.

1. *DKLR Holding Co (No 2) Pty Ltd v Commissioner of Stamp Duties (NSW)* (1982) 149 CLR at 463-4 and 474
2. *DKLR Holding Co (No 2) Pty Ltd v Commissioner of Stamp Duties (NSW)* (1982) 149 CLR at 463-4 and 474
3. *Ford's Principles of the Law of Trusts* at [5013]
4. *Brogue Tableau Pty Ltd v Binningup Nominees Pty Ltd & Ors* [2006] WASC 63 at 51

## LegalTalk

### Editor

Elly Parker  
Phone: +61 3 8603 6273  
elly.parker@au.pwc.com

### Sydney

Tower 2, 201 Sussex Street  
Sydney NSW 2000  
DX 77 Sydney  
Phone: + 61 2 8266 0000  
Facsimile: + 61 2 8266 9999

### Melbourne

Freshwater Place,  
2 Southbank Boulevard  
Southbank, VIC 3006  
DX 77 Melbourne  
Phone: + 61 3 8603 1000  
Facsimile: + 61 3 8613 5555

© 2008 PricewaterhouseCoopers Legal. All rights reserved. PricewaterhouseCoopers refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

The information in this publication is provided for general guidance on matters of interest only. It should not be used as a substitute for consultation with professional legal or other advisers. Before making any decision or taking any action, you should consult with your regular PricewaterhouseCoopers Legal professional.

No warranty is given to the correctness of the information contained in this publication and no liability is accepted by the firm for any statement or opinion, or for any error or omission.

For further information please contact your usual PricewaterhouseCoopers adviser or:



**John Cannings, Partner**  
Phone: +61 (2) 8266 6410  
john.cannings@au.pwc.com