

"The Scrip"

The official newsletter of the New Zealand Shareholders' Association Incorporated

April 2008

WHORDITORS

The courts are a place where the parties air their dirty laundry in front of a judge, and in the best traditions of English justice, anybody can go along and watch.

Mostly it is as boring as watching paint dry, but over the last couple of weeks lawyer Clive Bradbury turned it into a great show. He humiliated himself, exposed his client as a Hypocrite, flushed out that the board of a major company misled its shareholders as did the companies auditors, by act or omission, and brought into sharp relief the conflicts of interest of auditors that shareholders trust with an important governance function.

Clive Bradbury and his partner Gary Muir were lawyers to Westpac for over 15 years. As you would imagine this was lucrative. Muir designed the forestry scheme known as "Trinity" which was held to be tax avoidance. Westpac terminated the relationship with Bradbury once his involvement in the Trinity deal became publicly known and Bradbury then issued proceedings for damages.

I kid you not, an advisor, sues his client for sacking him! Great marketing Clive!

Now of course as we all know Westpac and the other banks have been involved in structured finance deals, in effect to strip income out of NZ and minimise the tax paid in NZ. The IRD considers this to be avoidance. I would never criticise a taxpayer for trying to minimise the mafia skim, that would make me a hypocrite, but for Westpac to sack Bradbury because he did such work for others (he may well have done such work for Westpac too) does make Westpac hypocrites.

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We can debate good corporate governance until we are blue in the face, but one tenant of good governance is “say what you do and do what you say.” I believe that hypocrisy is one of the ultimate governance sins.

In 2004 Westpac had its first ever, and I bet last ever AGM in NZ.

I asked the Chairman why the contingent liability from the tax audit of these arrangements were not recorded in the accounts and further if the auditors PWC had had any involvement in the design or execution of the transaction. The Chairman arranged for another to answer the question and it was confirmed that on advice they considered their position to be strong and thus no provision was made. Whose advice? The auditors or the architects or the implementers,no matter, we now know they are the same people.

The auditors managed to avoid the question and by omission mislead shareholders, leaving the meeting with the impression that they were not involved.

It now transpires that PWC were involved in the transaction and obviously also audited the same transaction and determined that no provision was required. The debt is now over \$800m.

Footnote: *Mathew Underwood has pointed out that this is a very live issue, as the “regulator,” NZX itself, has neither disclosed nor provided for the Access Brokerage claims because it feels that any claim is unlikely to succeed. However the court has just reopened the possibility of a successful claim by BNZ against NZX and other parties. Watch this space for another whorditor story!*

CLIPPING THE RIGHT TICKET

Inevitably when companies have a bad run, eventually the board will seek to replace management, usually way after they should have. A recent example of a CEO who remained on, considerably beyond his use by date, would be Evan Davies of Sky City.

When a new guard is marshalled in, the new team usually wants a share of the improvements that it effects, and the board is then challenged to find a way to do this. They usually then come up with a share option plan. These plans take many forms but usually involve the creation of new equity for the management team. The rationale for these plans used to be that turning managers into owners would mean that they would behave like owners. History has shown this to be bunkum and this line is now rarely used.

The latest lines used to justify the grant of equity or options to management is that the share price is an accurate measure for pricing the worth of an enterprise, which it should be if a market is rational and well informed, reflect the improving economic performance of the business. There are two big assumptions behind this model. Firstly, that shareholders accurately and rationally disseminate information, and secondly that they actually have relevant and accurate information. The first is called “efficient market theory” and the later is called information symmetry, ie that the owners or the

market have the same information as management. The later of course is never true, management have total information whilst shareholders have the information that management wants to give them, in the form chosen by management. This is called information asymmetry. Private equity as a business model works better than listed markets for many reasons but the major one is that this information mismatch is minimized.

Some enlightened directors accept that markets are not efficient, which I suspect most active shareholders already know, so they now have a new line to justify share options. This line is probably the shallowest thinking I have encountered. They argue that fixing the business is not enough, shareholders have to rate management in order for them to be effective and this rating is the share price. Thus boards now want to reward management for not only operating the business well, but for convincing shareholders that they are doing so.

Think about this for a moment, which is easier, doing a job well, or engaging PR firms to convince others that you are doing it well? Which is easier? Telling the unbridled truth, or embellishing it ever so slightly with PR dross?

When boards ask shareholders permission for management to clip the ticket on the transformation of a business, make sure that they are clipping that ticket and that ticket alone. In this regard share options are not the best alternative. A bonus plan based on increasing profits, cash flow, economic value added, or improvements in the enterprise value based on a rational formula, are more sensible options for giving management a share of what is within their control.

As the market begins to soften, management will see the opportunity to be given options on the cheap, below the intrinsic value of the business. Thus they can gain a reward based on improving market sentiment regardless of the performance of the underlying business unit.

Over the next 18 months shareholders must be vigilant, as I suspect we will be asked at a number of shareholder meetings to approve ill-conceived reward plans that will reward market activity rather than performance.

With the exception of small, cash-strapped start ups, all reward plans involving the granting of new shares to management should be voted against. The only exception to this would be a reward plan that pays cash, but at the option of either party the resultant cash reward can be used to buy shares, purchased on market assuming there is enough liquidity to do so.

Bruce Sheppard

Another footnote: Des Hunt feels we should all monitor this and draw NZSA board's attention to any short term bonuses awarded in the current downturn. Professor Stiglitz drew our attention to the part played by "banker greed and staff bonuses" in accelerating the already risky lending practices. We will be advocating for long as well as short term performance bonuses.

A GREATER RANGE OF DIRECTORS – INCLUDING WOMEN

It is of concern to the NZ Shareholders Association that we do not see a greater range of directors with a high degree of knowledge and experience “including woman” being appointed to our public companies. When compared to other countries we are overly represented by lawyers and accountants. Often when I asked chairman, why this is occurring on their board the normal response is that they have difficulty finding any one who has the necessary experience. I find this hard to believe when you see the talent available in the work force.

It reminds me of my own experience when I was trying to work my way up the corporate ladder. The response then was I did not have the worthwhile qualifications. It was only after a number of successful years in management, sales and international marketing my opportunity came along. Even then I was lucky to have a chairman who came up the hard way who recognise my ability and gave me the opportunity to become a director. When we look at some of the companies who are doing very well, one thing that really impresses me is the management team are often quite young and the team is often made up of both sexes. Surely some of these managers one day will move on to become excellent directors.

Perhaps chairman and directors need to look at themselves and say what we need to do to seek out these people. We would certainly like to hear from any one who feels she has the experience and talent to be a director. Unless new talent is gradually introduced to the board table there is no way she will gain any experience. When I look at a number of boards there seems to be opportunities where new talent including woman directors could bring added value to the company. I come across many people who are experienced in, human relations, engineering, marketing, science etc. The number of engineers, scientists, woman directors we have on our New Zealand boards compared to our major trading partners is very low. What an advantage for a company to give a clear signal to the business community opportunities do exist at board level. Experience in other disciplines would bring another dimension to the board table. There are many market segments where the new talents view point would have a critical input. From my research woman are very much in the forefront of any purchasing decisions being made by the end consumer. Having directors with experience in a number of disciplines on the board would raise many issues which otherwise could be over looked.

We at the N Z Shareholders Association would be keen to be involved in any initiative to assist in developing opportunities for new talent to become company directors. We would also encourage those interested to become members of our association and take an active part in the activities of the Association.

Des Hunt

NZSA – MASSEY – FISHER SCHOLARSHIP

A major step in our advanced research programme

Massey University's College of Business has established a research scholarship as a joint initiative with the Shareholders' Association and Auckland-based investment fund manager Fisher Funds.

The scholarship is established in response to the shortage of independent research on matters of governance, company performance, investor rights and relations, says College of Business Pro Vice-Chancellor Professor Lawrence Rose.

Both the Shareholders' Association and Professor Rose have been widely reported for their commitment to lifting financial literacy and Professor Rose says the establishment of this scholarship is in line with that. The association is leading the initiative to establish scholarship programmes with universities, leading investment firms and philanthropic organisations to fund postgraduate students for the completion of their PhD degree.

The new scholarship with Massey University will be jointly named after Fisher and the association and is the first of the planned scholarships to be established.

The college will provide academic and pastoral supervision of the student. Fisher Funds Management will host the PhD student in its Takapuna offices, providing day-to-day guidance and support and access to the firm's technology and research facilities.

The association will establish an annual research forum and invite the participating universities, fund managers and other interested parties – including the Stock Exchange and the Securities Commission – to identify major areas of research to create an integrated annual research programme.

Joint press release – Kevin McCaffrey

COMPANY MEETINGS

SANDFORD.

Held on 30 January 2008.

The Auckland Fish market seems a popular venue for Sanford meetings. It was another scorching January day and the temporary marquee made for maximum discomfort and a quick conclusion in temperatures that outside in the shade would have been approaching the 30s. Your representative did not on this occasion receive

a copy of the annual report nor did he have the opportunity to download a copy before the meeting. With the passing of the new legislation there is now small opportunity for the investor as opposed to the shareholder to review accounts before a meeting. Even shareholders are now left out of the loop if they fail to complete the request for an annual report in time. Fortunately the share registrar at the door had spare copies available but it is not a safe assumption to presume that even a copy of the agenda will be available to those who failed to turn up with their copy.

The questions from the floor soon came to an end. Whether this was the result of the stifling heat or the quality of the response was difficult to tell. However I intend to approach this summary in a quite different manner than usual as there were matters mentioned by the chairman that ought to receive a wider audience. There are, I am sure, long-standing shareholders who will disagree with what I am about to say and whose expectations differ but I will comment nevertheless.

Profitability

The chairman was unable to cheer shareholders at the meeting, indeed the strengthening exchange rate two things seem inevitable, a further steep reduction in profits comes with a challenge to the 22cps dividend that has remained unchanged for the last 4 years. The only positive factor is that the results for this year will be underpinned by a large one-off gain from the rearrangement of the Canadian operations.

As the Chairman stated at the meeting and in the Annual report, profits are unsatisfactory and basically unacceptable. Just how unsatisfactory can be gauged by the fact that profitability based on continuing ordinary business is now a miserable 2.4% on average shareholders funds. For those of us who prefer to use results based on capital employed, the figure is slightly higher at 3%. One shareholder had the audacity to tell the meeting that it was impossible to glean from the report just where the company was making its profits. The chairman glibly pointed out that the Board were in receipt of management accounts that delivered this information. This is a reminder that the 2007 accounts are the last financial statements before International Financial Reporting Standards (IFRS) are introduced. It becomes patently clear why Sanford, usually so advanced on reporting, are reluctant to use IFRS: segment reporting will require disclosure of farming as well as fishing results and this will be a huge positive step in understanding the finances of this group. This was an excellent question from a NZSA member and with the admission that management accounts provide the information sought, next years accounts will be interesting.

Board representation

The Board is to be congratulated in advising members at the meeting that Mr Paul Norling is to be appointed a director. This allowed a shareholder (another NZSA member) to ask that Mr Norling address members, which he duly did.

Exchange rate fluctuations

A shareholder sought further information on the exchange rate and asked the chairman to spell out Company policy. The chairman responded with a comment that did not address policy so much as advise members present that the company had

benefited hugely from hedging in the past. This question might bear repeating next year when a more specific question might force a policy statement from the Board. Such a statement would not go amiss in the annual report.

Oliver Saint

PGG WRIGHTSON & NZ FARMING SYSTEMS URUGUAY

We had a very enlightening and interesting talk by the Chairman of PGG Wrightson, Craig Norgate, at our February meeting, and it was clear that in Craig we have a Chairman who really understands his business.

Members benefited from an interesting film showing the growing farming business in Uruguay – a great reason to attend a meeting in person!

PGG Wrightson has posted a NPATA of \$34.6 million for the six months to 31 December 2007, compared with \$20.6 million for the December 2006 half year.

Craig said the result reflected improved underlying performance in most of the business, offsetting the impact of poor sheep prices, and a strong return from the establishment of NZ Farming Systems Uruguay Limited (NZFSU). "This is an excellent result in challenging operating conditions, with dry weather, exchange rates and poor returns to sheep and beef farmers being of particular concern".

The interim dividend has been increased from 4 to 5 cents per share, fully imputed. Under the Distribution Plan introduced in 2007, dividends are paid in the form of bonus shares and shareholders have the right to require the group to buy them back.

Craig said that, while the operating environment remained uncertain, the group was continuing to perform well. The Board remained comfortable with the earnings guidance provided to the market in December 2007, for full-year NPATA of approximately \$60 million, consisting of:

- Earnings from operations \$39 million
- NZFSU Performance Fee (based on \$1.50 share price) \$8 million
- NZFSU share appreciation (based on \$1.50 share price) \$9 million
- Capital gains/one-offs \$5 million

Craig said the initial return from NZFSU reflected the value created by the timely establishment of the company, ahead of a substantial increase in international dairy prices. This had been extended by an accelerated programme of land acquisition and farm development to take advantage of the favourable conditions.

Outlook

Craig said the businesses within the group were continuing to execute well. "While the nature of the business means it will always be sensitive to external conditions, including seasonal weather patterns and market factors, the changes made within the group have increased our ability to achieve positive business outcomes".

"In Australia, the recent rains have been very welcome. In South America, the continuing growth of the markets and the additional stimulus from the growth of NZFSU provide a strongly positive outlook.

"We are confident that the group is positioned to perform well in its various markets and operating environments. The fundamentals for medium and long-term growth in agriculture - and thus for PGG Wrightson - remain strong".

Jacquie Staley

AWARDS 2008

"Whether tis nobler in the mind to suffer outrageous fortune or to take arms against a sea of troubles."

Through the **Beacon and Glob awards** you have the opportunity to enlist the NZSA to confront those that displease you or on a happier note, praise those that raise your spirits. For several years now the Beacon and Glob awards have enabled the association to champion excellence and deride self interest and incompetence. The NZSA executive has found the nominations put forward by Members and Branches a strong guide in their deliberations. A nomination box will again be at the AGM but meanwhile you may contact the Award convenors **Joe Turnbull** (09) 631 5071, email rjyturnbull@xtra.co.nz , and **Howard Zingel** (07) 552 5320, email howardz@xtra.co.nz. with your thoughts.

BRANCHES

Auckland

- Our first Branch meeting this year was held on 20 February. Approximately 120 – 140 people turned out to listen to Craig Norgate – MD PGG Wrightson, deliver a very informative presentation about his company and in particular about its business developments in the dairy industry in South America.
- Following on from Craig's presentation, we introduced a new feature to the Branch meeting called 'Members' Forum'. The aim is to provide time after the formal meeting has ended, for members to raise and discuss any issue that is of concern to them in a low key, non-threatening atmosphere. The first Forum was hosted by Des Hunt and Noel Thompson and a large number of those present at the official meeting, stayed on to take part in the Forum. Various topics were discussed and the event was well received by everyone. The Forum should be a regular feature of future Branch meetings as long as we have volunteers to sit in

the 'hot seat'.

- Our next Branch meeting is scheduled for 16 April and we are pleased that Carmel Fisher – MD Fisher Funds Management, has agreed to give us a presentation on the Company investment strategies and what has been learned over the last 20 years. Tim Brown from Infratil Limited was scheduled to be our April speaker, and will now speak to us later in the year.
- The speaker for our 4 June meeting has just been confirmed as John Palmer – Chairman – Air New Zealand.
- Our committee meetings have been well attended and we are pleased to have an additional member, Uli Sperber, to help share the load.
- The Auckland committee supports the idea of a conference for branches in May 2008. After discussion with our members, it was felt that some issues that should be considered are:
 - Succession planning – where are the people that can assist and eventually take over reins from current executives?
 - Where are we heading as an organization?
 - Communication – currently a two way street with one way traffic

Ken Cook

Bay of Plenty

2008 opened with record attendances at two monthly discussion group meetings. In February Hamish Coleman of ABN AMRO Craigs gave us his view on the ever changing investment outlook and his view on share picks for the coming year. He was followed by David Higson who gave a thorough presentation on his experiences when investing in Australian shares. The meeting closed with an impromptu discussion on shares and markets as raised from the floor of the meeting.

In February Andrew von Dadelszen, licensed sharebroker spoke on Portfolio Investment Entities (PIE)s. This showed that we all have some learning to do in this area. The discussion widened to take in FDRs the current investing scene. Second up was Russell Brown, the convenor of the Equal Shares Investment Club which arose out of our branch and already has its membership closed at twenty members. The clubs prime objectives are to provide an educational opportunity for its members.

In March the members of our committee met the Hamilton committee in Matamata for a discussion on matters of common interest.

Next month, April, our branch will be visiting ABN AMRO
Craig's when the theme will be, Company Analysis.

Lloyd Christie

Canterbury

Well, Easter is over and we are now well into 2008. Hopefully we shall see the share market recoup some of the losses experienced over the last few months. The Feltex matter is beginning to rumble again but don't hold your breath if expecting any return of your investment. Matters will take a long time to work themselves through and any decisions will probably be appealed which will protract things even further.

We shall be holding a meeting on Tuesday 20th May at the Fendalton Croquet Club with Guest Speaker Bob Parker, the Mayor of Christchurch who will have just got back from his trip to Beijing. No doubt Bob will have some interesting things to tell us about his trip and the future directions of Local Government in Christchurch.

Other things in the pipeline are a visit to the Canterbury Brewery to see how your favourite tipple is produced and the Branch AGM for which we are trying to arrange to coincide with a visit to Christchurch of Arthur Lim, Investment Manager of Macquarie Equities NZ Ltd. We may have to defer our AGM later than normal to fit in with Arthur Lim's availability.

Your present committee members have indicated their willingness to stand for election for another year. However we would welcome others who may wish to be more involved in running the affairs of the Branch. It is good fun and there is lots to learn from the discussions round the coffee table after the formalities of the meeting are over. We usually meet on the second Tuesday of each month but this can be flexible as members are sometimes otherwise engaged on the scheduled evenings. So have a think about it and if you want to know more then give me or any of our other committee members a ring to chat about it.

Finally, those shareholders of Cavotec MSL may be aware that I have been nominated to stand for the Board of Directors and would welcome the support of members in my bid for election. This can be done at the company's AGM if attending or by submitting your proxy in favour of "the Representative of the NZ Shareholders Association" and forwarding it to the Company Share Registrar.

We still have a number of Training Manuals for the four courses that we have run in previous years. These are available for purchase at \$30 each but will be discounted to \$20 each if purchasing two or more of the courses. If buying all four manuals the cost would be only \$80 which is excellent value for the information contained in these manuals. Contact me for further details.

As they say in Scotland - "Lang may your lum reek" but not to the extent of polluting the atmosphere.

Ritchie Mein

Waikato

Our first meeting of the year on March 12 was held at the Hamilton Club. The guest speaker was Derek Brewster, a sharebroker from ABN Amro Craigs, Hamilton. Derek is an enthusiastic investor and keen branch member.

The theme was “The Roller coaster that is the Sharemarket” which was very appropriate for these volatile times. His talk was very wide ranging covering many sectors of the sharemarket and the local and international economies. Derek was wary of the banking sector and the highlight of his talk for me was his prediction that the kiwi dollar would have a sharp correction by June. Derek thought any market recovery will be lead by high yielding quality companies.

The 48 attending, appreciated Derek’s willingness to share his knowledge in an entertaining and informative presentation which easily filled the allotted time.

At the beginning of our meeting Derek handed out his disclaimer disclosure forms. No doubt these disclosures are a good thing for people giving paid advice. But where is the line drawn in these more litigious times? Can a person who pays to join an organisation with the intention of getting help and advice, then sue that organisation or its officers if they inadvertently or unknowingly give false or bad advice?

Three members of the Waikato Committee met informally with the B.O.P. branch at the Horse and Jockey Inn at Matamata on 25 March. The venture proved to be a worthwhile exchange of thoughts and ideas of how each other’s branch functioned. The most concrete resolution that came of the meeting was that the two branches should help other provincial branches become established, in particular Hawkes Bay. Our next function will be an address given by Shelley Thomas, the Chairperson of the Waikato/BOP Branch of the Institute of Directors. Shelley will speak on the role of the Institute in promoting good governance.

Robert Foster

Wellington

Our first meeting for the year was hosted by Xero where CEO Rod Drury gave a comprehensive overview of the company, the rationale behind the product, progress to date and a demo of Xero.

Its a very good product, probably the slickest online accounting service anywhere. The challenge they face is selling into a relatively entrenched market - although having said that, most people seem to dislike their existing accounting systems, so it may not be such a hard sell afterall. The main selling points of the product/service are:

- No software for the end user to install, maintain or backup – you can get to it from any internet connected PC or Mac.
- Automatic daily bank statement downloads into Xero with a smart transaction matching facility.

- Online support included in the monthly subscription.

Xero are still in the development stage with new functionality being added almost weekly. They have only just started to market the product directly to the public, aiming for 1300 users by 1 April (break even is approximately 10,000 users). Work on developing the UK then Australia markets is also underway. The UK is most attractive and will be launched first due to size and the similarity of tax system.

The shares are very thinly traded so you can't read anything much into the price – especially at the moment.

Martin Dowse

SPECIAL OFFER TO NZSA MEMBERS

NEW ZEALAND INVESTOR.

You will soon receive a letter from Equity Investment Advisers, offering their monthly, New Zealand Investor, at a special price for the first full year. We are in discussion with this journal, and we think the large discount from shelf price will be attractive.

As our profile increases with your help, we hope to bring more attractive offers from the investment community.

MEMBERS ISSUES

NATIONAL PROPERTY TRUST

John McCarthy believes that St Lawrence is milking National Property Trust's unit holders, of unreasonably high fees, in the last six months \$7,140,000. Further, with revaluations of \$36.22m St Lawrence is entitled to convert its 20% into units diluting those held by others and their potential for future dividends. What action can we take?

We have often discussed the inequitable distributions from unit trusts, and still favour the company structure with in-house management accountable to a board of directors. There is little chance of an action against high fees succeeding because they will be approved under the trust deed.

Protest at unit holders meetings need to be well documented and publicised, showing that St Lawrence is above the market rate.

Stapling of trust units with management entities and other structures was achieved in Australia (eg Mirvac) by popular demand.

John is hoping to follow up his complaint with a letter to the Securities Commission. We do know that they are unhappy with some of the trust structures and management contracts.

We also feel that a letter to the Trustee, in this case NZ Guardian Trust, owned by Suncorp Metway in Brisbane would help to make the dissatisfaction known. The trustee, however, will simply be guided by the letter of the deed.

In today's market the trustee's fee (0.1% of assets) and the manager's fee,(0.75% of assets could both go down if the valuations go down, and so should the performance fee, that is provided the valuer is doing his job properly. So members are encouraged to keep a close watch on valuations and payments to the manager over the next two years in a slacker property market, to raise these issues with the trustee, and to recommend to the trustee that the manger be sacked if the assets are not producing an adequate return to unit holders, or that the trust be liquidated.

Footnote: John needs support with this issue, and asks that unit holders who wish to join his complaint to the Securities Commission contact him by email: jhamccarthy@xtra.co.nz, or phone/fax 06 844623, or mail 147 Ascot Ave, Taradale.

OFFERS FROM COLONIAL CAPITAL CORPORATION

Ashley Chan advises that members have been receiving offers for shares, especially those listed in Australia, from the above grand-sounding corporation. David Tweed is a leading director of this company. Mr Tweed has been banned from operating as a financial adviser (sharebroker) by the Australian Securities Commission. His practice of offering apparently high prices for shares with long settlement terms or other unrealistic valuations were found by an Australian court to be dishonest, and so members who are prompted to sell shares by letters from the above "corporation" should seek advice before signing up.

FELTEX UPDATE:

Wakefield Associates in Christchurch have decided to pursue a representative action against the Directors of Feltex, Credit Suisse Private Equity, Credit Suisse First Boston, First NZ Capital, and Forsyth Barr. The action will include all of those investors in the initial public offering who do not opt out by 14th April. The costs will be born by the named claimants, ie those who fronted with the original request for \$980.00. We have on record Garry Wakefield's opinion that no claim for subsequent costs will be born by unnamed claimants who do not opt out, but they will lose some of any settlement won to Wakefield Associates in legal fees. Ross has warned that notwithstanding the assurance received, there is a slight chance that costs might be awarded against all plaintiffs at the end of the hearing, by the Court. Before we received the latest assurance, we had some concerns about the structure of the opt out arrangements, which we have set out below ("The thinking in the Feltex Case") – but must now be read in light of this latest information.

Since the receivers sold the assets of the business to Godfrey Hurst, they have repaid \$105.5m to the ANZ Bank and the ANZ National Bank, of the \$119m claimed, leaving a balance of A\$14m, and no hope of paying unsecured creditors or shareholders.

The Liquidator's responsibilities were to investigate the claims of unsecured creditors, (no hope there,) and the events leading to the appointment of receivers by the banks. The liquidator in October considered that the directors had been "reckless" in continuing to trade without complying with their disclosure obligations. Since that time they have gained access to bank-client correspondence, and have advised shareholders of their claim requirements without which claims will be rejected. This is continuing to be a fascinating but drawn-out saga.

THE THINKING IN THE FELTEX CASE

Several members have enquired about their potential liability in a court case against the directors and issuers of the shares. This is some of Ross's thinking in replying to members. Bronwyn Smits and John McCarthy felt we should include it in The Scrip.

Tony Gavigan has stated on the ftxit website that those who do not opt out are not liable for court awarded costs (in the event that the claims fail). People can take him at his word, but I am interested in working out just how that can be the case. (Ed: We have since asked Gary Wakefield for confirmation of this and he has given it – see item above) . I have not seen a copy of the Court Order in relation to the opt out arrangement, so will assume the Court has not specifically addressed it.

The funding agreement, that investors were earlier invited to sign, deals with the issue of costs protection at clauses 8.4 to 8.7 inclusive. These provisions are worth considering in detail, as this is their protection mechanism.

The first point is that it is a matter of contract, and in effect is an indemnity. This means that in the event that the Court does make a costs award against those that signed up, the company Joint Action Funding Limited agrees to pay it.

People who do not opt out, do not have to sign the funding agreement. So it is difficult to see how they are protected. They are not a party to the contract (again, presuming the Court Order has not said otherwise).

Those who did sign the funding agreement, have the benefit of a company guarantee. The company was formed on 20 December 2007, and the sole director and shareholder is Mr Gavigan. I have seen a comment on one of the websites that this company is backed by wealthy but unnamed people.

Mr Gavigan is not giving the guarantee. Only this company is. The company is a private company. I do not have any information that would allow me to estimate whether this company could ever pay a costs award. It is irrelevant who the company is backed by. Only the company has to pay. If it has no assets, it pays nothing. If the shares are held in trust for Bill Gates and Warren Buffet, this is irrelevant. Shareholders do not have to pay one cent of the losses of the company. That is why people use the company structure. The company is liable. The shareholders are not.

That leaves investors who have signed up on the earlier deal (and note this does NOT apply to those who have signed nothing, but have also not "opted out") with this quandary - how do they know they are protected from an adverse costs award? Mr

Gavigan has publicly stated they are not exposed. The funding agreement states that if the company owned by Mr Gavigan can pay, then they are not exposed. But Mr Gavigan has not said that he will pay. The public information says that the company is backed by wealthy investors - which is irrelevant if the company itself can not pay.

If I was a Feltex IPO shareholder, my view would be (a) that if I thought the case had merit, and would recover me my money, I would fund the action directly myself (if I could afford to do so) and control what steps were taken. (b) If I did not have that view, then I would opt out. I would not have signed the earlier deal, as I would not trust a company formed a few months ago, with undisclosed assets and backing, to protect me from a costs award if things go pear shaped. I would only see the arrangement as a possible benefit, if (c) I was already convinced that the case would succeed (in which case the guarantee is not needed anyway) and could not afford to fund any claim myself.

I think all Feltex investors fit into one of (b) or (c). So the key issue for them is - is this case a winner? If so, stay in. If not, opt out.

Is the case a winner? That is a question for each shareholder to consider carefully. In doing so, they should consider all available information, including in particular the Securities Commission's own conclusions on the IPO documentation.

Only the Court will determine the ultimate question.

Shareholders have to make an informed choice in this, as in any other type of investment.

In the event that all this may be considered investment advise, I say first that as a lawyer advising in regard to proposed legal proceedings that I do not have to meet the new amendments to the Securities Markets Act, but even so say (in my capacity as a member of the Board of the NZSA):

DISCLOSURE

The New Zealand Shareholders Association generally has no idea what it is doing, The office bearers have no formal qualifications in giving investment advice, regularly lose their own money on the stock exchange, have professional qualifications and membership of professional bodies, have some insurance, can be sued, have no criminal convictions, are not bankrupt or in No Asset Procedure, are not prohibited from running a company, have no adverse findings against their respective professional capacities, have not been in receivership or liquidation or voluntary administration, have not yet been prohibited from practicing their respective professions, do not get paid (note that particularly, as you do tend to get what you pay for,) unless the NZSA itself retains us to carry out a particular project, may have shares in companies we praise or pillory (making us particularly sensitive to success, failure, genius or stupidity,) and advise on any damn thing they like, whether they have any basis for doing so or not. So don't say you weren't told.

AND THIS IS OUR DISCLOSURE FOR THE WHOLE ISSUE - AMEN