

*John O'Grady**

CO-OPERATIVE BUILDING SOCIETY OF SOUTH AUSTRALIA LTD V AUSTRALIAN SECURITIES COMMISSION

The law does not always lend itself to being categorised into a particular area to the mutual exclusion of all other areas of law. This case¹ is an interesting example of the interaction of property law with corporate law.

THE FACTS

The case involved the sale of strata titled units in the Westend Apartment complex in Adelaide.

Contracts of sale of each unit in the strata scheme required each purchaser to accept the provisions of a Management and Letting Agreement made between the owner of the property and the management company. The owner was a substantial shareholder in the management company and was the beneficiary of a unit trust of which the management company was the trustee.

Under the relevant Management and Letting Agreement, Westend Pty Ltd ("Westend") was appointed as the manager and letting agent of the whole complex for a period of 10 years. The Agreement also provided that purchasers were to surrender their rights of occupation and allow Westend to lease their apartments as fully furnished, serviced apartments. Further, the agreement provided for Westend to collect rental income on a consolidated basis as trustee and distribute it to purchasers based on the proportionate share, net of certain specified expenses relating to the strata-titled complex. In addition, the Management and Letting Agreement required purchasers to obtain a similar covenant with any subsequent purchaser, to comply with the terms of that agreement.

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1 *Co-Operative Building Society of South Australia Ltd v Australian Securities Commission* (1993) 11 ACLC 262.

THE COURT'S FINDINGS

The Court held that the purchasers' interests were "prescribed interests" under the *Corporations Law*.

This effectively means that:

- (1) the offerer (usually the owner of the unit) must be a public corporation within the meaning of s9 of the *Corporations Law*;
- (2) there must be an approved trust deed under s1065 of the *Corporations Law*;
- (3) an approved trustee must be appointed under s1066 of the *Corporations Law*; and
- (4) the company must also register a Statement under the *Corporations Law*, and otherwise comply with the prospectus provisions of the *Corporations Law*.

Jenkinson J found that it was an implied term of each contract of sale that Westend warranted that all previous contracts of sale, and all future contracts of sale of units in the complex would include the same terms.² This implied term granted the purchaser a right to participate in the profits of the scheme; in the absence of such a term, the scheme and common enterprise would not exist.

The owner, in its submission to the Court, said that the scheme did not constitute a "prescribed interest" under the *Corporations Law*, and relied on a decision of the Supreme Court of Western Australia which found that the contractual imposition of a management agreement on all unit holders was not sufficient to make their interests "prescribed interests" under the *Corporations Law*.³

This argument was not accepted by the Court, which found that there were additional factors indicating a "business undertaking or scheme".

2 *Co-Operative Building Society of South Australia Ltd v Australian Securities Commission* (1993) 11 ACLC 262 at 271

3 *Maunder-Hartigan v Hamilton* (1984) 2 ACLC 438.

In reaching this conclusion, Jenkinson J said:

In my opinion, there are other circumstances not present in *Maunder-Hartigan v Hamilton* which in this proceeding indicate the elements of the "business undertaking or scheme" in the profits and assets of which the purchaser of a unit is offered an interest, and indicate also what the "closely connected operations" are which constitute a "common enterprise" by contributing to the overall purpose that unites them.

His honour pointed to a particular provision of the Management and Letting Agreement which declared that the Manager shall receive Gross Revenue "as trustee for and on behalf of the Owner and the Other Owners".

The beneficial ownership of the Gross Revenue is "subject to the right of the Manager to pay therefrom the Operating Expenses, the Management Fee and the Management Incentive Fee".⁴

The Court also found that "the purchaser [was] led to expect profits in relation to the common enterprise from the efforts of a third party, namely, Westend".⁵

Furthermore, Jenkinson J found that the contract being offered, and the scheme to which the contract was designed to give effect, constituted in substance a right to participate in an "investment contract" within the meaning of that term as used in the definition of "prescribed interest". Contrary to the submission made by the owner, the Court also held that the right of a purchaser to participate in those profits was not a right or interest which was derived primarily from the purchaser's interest in the trust. In summary, the Federal Court found that the arrangements pointed to a "business undertaking or scheme" and a "common enterprise" in which the owner, Westend and the purchaser's of the units shared.

EMERGING TRENDS AS A RESULT OF THE CASE

Since *Co-op Building Society v ASC*, at least one property development of a similar structure has been marketed by means of a prospectus, and more

4 *Co-Op Building Society v ASC* at 270.

5 At 271.

are currently in progress. The trend emerging as a result of this case is for developers to turn the legal requirement of the prospectus into a positive marketing tool.

Another trend emerging as a result of acceptance by developers of the need to have a prospectus has been that developers and their legal advisers have the opportunity to use the scope offered by the *Corporations Law* to create highly refined structures, tailor-made to the particular circumstances.

More sophisticated versions of the original scheme are emerging. For example, a development currently on offer via a registered prospectus has the following features:

- (1) The purchase of each Strata Unit includes an interest in the form of a 10 year lease to the Manager, a company established to manage the complex.
- (2) The lease provides for a bank-guaranteed rental of 6% per annum of the purchase price for the first 2 years. After that period, the rental is determined by reference to the operating surplus of the complex and unit owners may subsequently elect to terminate the lease upon giving appropriate notice.
- (3) The Manager has entered into a 10 year agreement with an Operating Company to operate the day-to-day activities of the complex.
- (4) The purchaser of a unit is also required to purchase "B" class redeemable preference shares in the Manager equal to the number of unit points which attach to the unit being purchased.
- (5) After the expiry of the 2 year guaranteed rental period, the unit owners will have control of the Manager and the right to appoint 3 directors.

CONCLUSION

The Westend case represents a landmark decision where a strata scheme is marketed as part of a legal structure which is in the nature of a "business undertaking or scheme" or "common enterprise". Now that it has been generally accepted, it seems likely that more sophisticated versions of the original concept will emerge in many strata-titled developments in the future in order to take full advantage of the flexibility and sophistication available under the *Corporations Law*.