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REPORT OF THE SECURITIES COMMISSION

ON AN ENQUIRY INTO

ASPECTS OF THE AFFAIRS OF

PERRY DINES CORPORATION LIMITED

(RECEIVERS APPOINTED)

Securities Commission
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Wellington.

REPORT OF THE SECURITIES COMMISSION ON AN ENQUIRY INTO
ASPECTS OF THE AFFAIRS OF PERRY DINES CORPORATION LIMITED
(RECEIVERS APPOINTED)

INTRODUCTION

1. Perry Dines Corporation Limited (Receivers Appointed) ("Perry Dines") was incorporated as a private company on 16 December 1983 and re-registered as a public company on 10 February 1984. It offered 4,500,000 ordinary shares to the public for \$1 per share (25 cents capital plus 75 cents premium) under the terms of a prospectus dated 20 February 1984 and these shares were duly allotted. After that allotment the issued and paid up capital was \$2,000,000 in 8,000,000 ordinary shares of 25 cents each, of which Dines Construction Limited held 3,499,600 shares which had been allotted at par. Under a prospectus dated 1 August 1985, Perry Dines made a further offer of 3,000,000 ordinary shares for 65 cents per share (25 cents capital plus 40 cents premium) to the existing shareholders on the basis of 3 for 8. On 27 August the directors informed shareholders at the annual general meeting of the company that they had withdrawn their approval to that prospectus. On 28 August 1985 receivers were appointed by the first debenture holder, The Bank of New Zealand ("BNZ"). The company is still in receivership.
2. On 19 September 1985 the Commission decided, pursuant to section 10 of the Securities Act 1978, to obtain evidence on the following matters:
 - (i) The circumstances and terms of the offer on or about 1 August 1985 of shares in the capital of Perry Dines under the document referred to in paragraph (ii);
 - (ii) The terms of the document referred to as "Registered Prospectus (Short Form) dated: 1 August 1985 for a renounceable offer of 3,000,000 ordinary shares of 25 cents each at a premium of 40 cents by Perry Dines

Corporation Limited to the existing holders of its ordinary shares";

- (iii) The state of facts and the basis for opinions referred to in that document;
- (iv) The circumstances of, parties to, and terms of the sales and purchases of Perry Dines shares and rights to shares in the period from 1 April 1985 to 26 August 1985.

It will be noted that the Commission's main purpose is to compare the statements made in the prospectus dated 1 August 1985 with the state of affairs as at that date. The terms of reference did not include an enquiry into the immediate causes of the collapse.

3. The Commission held a public meeting at its offices in Wellington on Friday, 22 November 1985. Evidence was taken from:

Mr R.I. Thompson,
Receiver,
Perry Dines.

Mr Bruce Hancox,
Chief Executive,
Brierley Investments Limited.

Sir George Chapman,
Past Chairman,
Perry Dines,
and formerly a director of its subsidiaries.

Mr M.G. Dines,
Managing Director,
Perry Dines.

Mr K.W. Irwin,
Director,
Perry Dines.

Mr R.A. Peacocke,
Director,
Perry Dines.

Mr C.M. Lobb,
Partner,
Jarden & Co.,
Members of the New Zealand Stock Exchange.

Mr T.G. Huppert,
Executive,
Brierley Investments Limited.

Mr R.B.W. Gill,
Executive Director,
New Zealand Stock Exchange.

Mr R.J. Cowley,
Audit Partner,
Touche Ross & Co.,
Wellington.

Mr G.R. Mitchell,
Audit Partner,
Touche Ross & Co.,
Wellington.

Information had previously been obtained from the Perry Dines Share Registrar (BNZ Share Registry), Investment Nominees Limited (a nominee company of Harcourt Longuet Hume & Co., sharebrokers, Wellington), and Firenze Nominees Limited (a nominee company of Francis Allison Symes & Co., also sharebrokers, of Wellington).

4. Counsel appeared for witnesses as follows:

Mr J.W.S. Mooney, for Mr Thompson

Mr T.J. Broadmore and Mr S.L. Franks,
for Mr Dines, Mr Irwin and Mr Peacocke

Mr W.M. Wilson, for Mr Lobb

and,

Mr W.F. Brown, for Mr Cowley and Mr Mitchell

5. The Registrar of Companies, Mr K.F.P. McCormack, attended for part of the meeting and made a statement to the Commission about his policy in relation to section 9A of the Companies Act 1955 (which empowers the Registrar to inspect the records of a company).

6. The Commission has discussed with the Registrar of Companies the procedures for registering a prospectus and for verifying registration.
7. A draft of this report was prepared for consideration by the Commission and those who had given evidence. A copy of the draft was sent to each witness and counsel on 21 April, 1986. Each witness and counsel has had the opportunity to comment upon that draft. Some have made extensive comments. The Commission has considered the comments and believes that all parties have had an adequate opportunity to present their evidence and their views to the Commission.

STATEMENT OF FACTS

8. In 1984 and part of 1985, the Directors of Perry Dines were Sir George Chapman of Heretaunga, Chartered Accountant, Chairman; Michael G. Dines of New Plymouth, Managing Director; Kerry W. Irwin of New Plymouth, Solicitor; and Robert A. Peacocke of Hamilton, Engineer.
9. In the first prospectus issued by Perry Dines dated 20 February 1984, the company said "it was well placed to pursue a wide range of construction activities, especially those projects requiring a high degree of engineering expertise". There was a summary of major work completed and in progress, which emphasised the company's experience with pipeline engineering for the petroleum and gas industries. In its first annual report, issued on 31 July 1984, the Directors announced that:-

"Tax paid trading profit before extraordinary items [for the year ended 31 March 1984] topped by 8% the result forecast in the pre-float prospectus. Earnings were \$1,160,000 compared with the \$1,078,000 forecast. ... This result was particularly pleasing to directors as turnover was 9.1% lower at \$13,216,000 through contracts starting later than programmed in the financial year."

10. At a board meeting on 12 November 1984 the Directors of Perry Dines "decided provisionally that a cash issue of 1 : 5 be implemented". The Managing Director was asked "to approach Jardens with the decision and to ask them to underwrite this float".
11. On 3 December 1984 Perry Dines authorised Jarden and Co. to distribute a Financing Plan to financial institutions. Perry Dines were seeking to raise a total of \$4,300,000 of which the major portion was to restructure existing debt and the balance to provide new facilities.
12. On 25 January 1985 Perry Dines, following the appointment of BNZ as their new bankers, finalised documentation for revised financing facilities, giving to BNZ security by way of a registered first ranking debenture charge.
13. By notice dated 1 April 1985 the Registrar of Companies authorised accountants Mr J.F. Managh and Mr T.H. Davies to undertake an inspection of Perry Dines and associated companies under section 9A of the Companies Act 1955. Mr Managh and Mr Davies commenced the inspection on 2 April 1985. They reported to the Registrar on 23 April. We have examined this report.
14. On 13 June 1985, Perry Dines executed a second debenture over its assets in favour of Jarden Securities Limited and a deed of priority limiting the extent of the priority of the BNZ as first debenture holder to \$5,000,000. This limit was subsequently extended to \$6,000,000.
15. By letter dated 20 June 1985 the Registrar of Companies informed Perry Dines that it appeared to him "that the group financial position is not at all sound. It appears, moreover, that there are also some reservations as to the solvency of the group". He asked Sir George Chapman and Messrs. Dines, Irwin and Peacocke to meet him on 2 July with other designated officers of the company, and to answer 8 specific questions in the meantime.

16. On 24 June 1985 the directors approved the accounts for the financial year to 31 March 1985. Sir George Chapman received the board papers but did not attend this meeting.
17. By letter dated 26 June 1985 Sir George Chapman informed Mr Dines as Managing Director of Perry Dines that he wished to retire from the board "effective as at 30 June 1985".
18. On 2 July 1985, the company auditors, Touche Ross & Co., signed their audit report in respect of the accounts to 31 March 1985. On the same day, Perry Dines reported to the Exchange that Sir George Chapman had retired from the Board.
19. Also on 2 July 1985, the Perry Dines board at a meeting held in Wellington attended by Messrs. Dines, Peacocke and Irwin, directors, and Mr. Gyde, secretary, resolved as follows:

"THAT the Company issue a Prospectus for a renounceable offer of three million ordinary shares at 25¢ each at a premium of 40¢ each on the following basis:

- (a) That the issue be fully underwritten by Jarden & Co.
- (b) That the offer be restricted to the existing holders of the ordinary shares of the Company as registered at 5.00 p.m. on 31 July 1985.
- (c) That the offer give each shareholder the right to subscribe for further shares in its capital under this issue in the rate of three new ordinary shares for every eight ordinary shares which are held at 5.00 p.m. on 31 July 1985.
- (d) That payment of 65¢ per ordinary share is made in full on application no later than 29 August 1985.
- (e) The new shares will not participate in the final dividend payable in August 1985 but will in all other respects rank pari passu with existing ordinary shares.
- (f) Shareholders will be able to accept the offer either in full or in part.

(g) Shareholders will have the right to renounce their rights to ordinary shares not applied for in favour of any person."

20. Also on 2 July the directors of Perry Dines, and Sir George Chapman, met with the Registrar of Companies to discuss the situation referred to in the Registrar's letter of 20 June 1985 (see para 15). We heard evidence about this meeting. We have discussed the evidence with the Registrar. The directors, and Sir George, told the Registrar in no uncertain terms that they rejected his reservations about the solvency of Perry Dines. The Registrar was concerned with the legal test of insolvency, which refers to the ability to pay debts as they fall due. It was clear that the company had deferred payment of creditors. The directors agreed that the company had difficulties, but they asserted that the difficulties were being overcome. They referred to a programme for the realisation of assets (including a headquarters building in New Plymouth, and an aeroplane) and a restructuring of the company's finances (which included substantial borrowings and financial leases). They referred to their proposals for an underwritten cash issue of shares.

We paid particular attention to the evidence of Sir George Chapman. He told us that:-

"... I had no reason to believe, and did not believe that there was any possibility of the company collapsing. On the contrary, I had every reason to believe that the company was at that time in a position to continue as a going concern ...".

He gave reasons in support of that view. He also said the budget tabled in June 1985 -

"showed a significant reduction in the level of the company's creditors since 31 March 1985 which confirmed to my mind that the recovery programme was working."

He confirmed these views in his evidence about the prospectus:-

"I played no part in formulating the terms of the document, but I consider that under the heading of 'Prospects and Forecasts' the prospectus gave an accurate summary of the company's difficulties and the steps that had been taken to remedy them. All I am able to say is that the statements contained in the prospectus would have been accurate as at 25 June 1985 - that is, the date I actually tendered my resignation - but I am not in a position to say whether the position was still the same on 1 August 1985."

Mr Dines told us:-

"... we were all aware that the whole structure was quite fragile and each part depended on the other parts ... I am sure the Registrar was also aware that it was an integrated attempt to structure something for the future, the cash issue being part of it";

and later on in the course of his evidence:-

"The cash issue was based on the budget ... there was no feeling that we had that that statement was incorrect ... the information we had, we felt, was consistent with the statement we had made."

At the meeting, the Directors referred to a budget they had considered on 24 June 1985 which forecast a profit for the year ending 31 March 1986 of \$739,000.

The Registrar emphasised that the responsibility for the operations of the company rested with the Directors.

The Directors and Sir George left the meeting with the impression that the Registrar was satisfied with their statements and proposals.

21. On 5 July 1985 Perry Dines notified the New Zealand Stock Exchange of:-

- (i) the results of the year ended 31 March 1985, showing a profit of about \$1 million;

- (ii) the directors' recommendation of a final tax free dividend of 3 cents per share; and
 - (iii) the decision to make a fully-underwritten cash issue of three new shares for every eight shares held at 65 cents per share.
22. On 12 July 1985 Perry Dines and Jarden & Co. signed an underwriting agreement in respect of the issue. In an undated letter signed, it appears, shortly before the date of the underwriting agreement Mr Dines agreed to sub-underwrite 400,000 shares.
23. On 24 July 1985 Dines Construction Limited sold, and Portfolio Management Limited, a subsidiary of Brierley Investments Limited ("Brierley"), bought, 1,450,000 Perry Dines ordinary shares at 30 cents each. This transaction was not explicitly reported to the New Zealand Stock Exchange (see para 28 below). On the same day, sales on the Exchange were reported at 68 cents and 70 cents.
24. On 29 July 1985 the New Zealand Stock Exchange, having considered a draft of the prospectus, informed the District Registrar of Companies at New Plymouth, pursuant to r.23(2) Securities Regulations 1983, that:-
- "the securities being offered have been accepted for listing and will be quoted upon completion of allotment procedures".
- Shares were quoted ex rights from 29 July 1985.
25. On 1 August 1985 Perry Dines wrote a letter to the District Registrar of Companies at New Plymouth enclosing a short form prospectus, a copy of the company's accounts to 31 March 1985 and a cheque for \$50, being the filing fee. This letter was received by the District Registrar on 6 August and a receipt for the filing fee was then issued to the company.

26. On 1 August 1985 the Exchange commenced quotation of the rights. Between that date and 26 August there was some trading in the rights.
27. On 6 August 1985, Perry Dines sent the prospectus, letters of entitlement and 1985 annual report to all shareholders.
28. Also on 6 August, Brierley Investments Limited informed the Stock Exchange that it had:-

"purchased by private treaty and on market transactions 2,139,700 ordinary shares in Perry Dines Corporation. Total consideration for the shares was \$1,015,698 giving an average price of 47.5 cents per share. B.I.L. now owns 19.45% of the issued share capital of Perry Dines Corporation, and will be considering making an application to the Commerce Commission to increase their shareholding beyond 20%.

"...B.I.L.'s decision to take a substantial stake in Perry Dines Corporation is consistent with Brierley's philosophy of identifying and assisting companies to achieve their growth potential, both locally and overseas.

"...Brierleys will be seeking board representation and would be nominating Mr Tomas G. Huppert to represent them on the board."

Brierley had purchased shares at various prices before the purchase mentioned in para. 23. We refer to these transactions in para. 73.

29. On 7 August 1985, the Perry Dines board resolved that Mr T.G. Huppert be appointed a director of Perry Dines and its subsidiaries. Mr. Huppert and Mr. M. Chennells of the Brierley organisation were present at the meeting and participated in the discussion. A number of meetings and discussions ensued. We have taken evidence about them only for the purpose of examining the state of affairs as at 1 August 1985 (the date of the prospectus) and the

state of knowledge of the directors as at that date. Otherwise, they are not relevant to our terms of reference (paragraph 2).

30. On 26 August the directors of Perry Dines requested the Exchange to suspend trading in the company's ordinary shares and cash issue rights, and trading of shares and rights was forthwith suspended.
31. At the annual general meeting of Perry Dines on 27 August 1985 the directors reported that they had withdrawn their approval to the prospectus and their recommendation for a final dividend for the year ending 31 March 1985.
32. On 28 August 1985 the directors informed the Exchange that they had invited the first debenture holder, BNZ, to appoint a receiver to the company and all subsidiaries, that BNZ had agreed to this and had subsequently appointed Mr R.I. Thompson and Mr T.A. Scoular of Coopers & Lybrand, Chartered Accountants, Wellington, as receivers, and that the directors had retired from all managerial positions in the company.
33. On 29 August, solicitors acting for the directors of Perry Dines requested the Securities Commission to suspend, pursuant to s.44(2) Securities Act 1978, the registration of the prospectus. The Commission met on 30 August, heard counsel, and resolved accordingly.
34. On 30 August 1985 the receivers informed the Exchange that, at the request of the directors, the Securities Commission had suspended registration of the prospectus and that the receivers would arrange as soon as possible for the subscriptions received from the public to be refunded to subscribers. The money was refunded.
35. On 2 September the Registrar of Companies issued a press release stating that:

"the prospectus, although delivered to the District Registrar of Companies, New Plymouth was not in fact approved and registered. No certificate of registration has been issued in terms of the Securities Act".

COMMENT - THE SECURITIES ACT 1978

36. A cash offer to existing shareholders is an offer of securities to the public for subscription under the Securities Act 1978 (s.3(3)). Perry Dines was required to register and distribute a prospectus before making the offer (s.33(1)). Regulation 4 of the Securities Regulations 1983 provides for the use of a "short form prospectus" accompanied by a copy of the accounts laid before the members in general meeting where the offer is limited to persons who already hold similar securities, whether or not the offer is renounceable in favour of any other person. The Securities Act (Short Form Prospectus) Exemption Notice 1984, S.R. 1984/184 (which has been superseded by the Securities Act (Short Form Prospectus) Exemption Notice 1985, S.R. 1985/308) provides for the distribution of audited accounts "which give a true and fair view of the state of affairs and results" of the company in lieu of accounts which have been laid before members of the issuer in general meeting. The exemption notices enable the prospectus to be circulated before the annual meeting with the annual report and the notice of meeting - a procedure more convenient and less costly than deferring the distribution of the prospectus until after the meeting.
37. The Directors of Perry Dines distributed, with the letters of entitlement, two documents in respect of the offer they had announced to the Stock Exchange on 5 July (para. 21), viz:-
- (i) A copy of the Annual Report for the year ended 31 March 1985;

(ii) A "Short Form" Prospectus.

We have taken evidence about these documents, and make the following comments about them.

THE 1985 ANNUAL REPORT

38. The financial statements for the year ended 31 March 1985 contained the information required by the Companies Act 1955. The auditors expressed the opinion that they were "properly drawn up so as to give, using the historical cost method as modified by the revaluation of land and buildings, a true and fair view of the state of the company's affairs as at 31 March 1985". The company did not present current cost accounts, and the auditors noted that fact.
39. The consolidated accounts showed assets at \$26 million, current liabilities at \$13 million, other liabilities at \$6.4 million, and shareholders' funds at \$6.7 million. Group profit was shown at \$1.017 million. The accounts are reproduced in Appendix B to this report.
40. The accounts included a "Statement of Changes in Financial Position" during the year for Perry Dines and its subsidiaries as follows:-

"FUNDS WERE PROVIDED		\$000
<u>From Operations</u>		
Profit before Extraordinary items		1,017
Less: Extraordinary items		<u>31</u>
		986
Less Prior Period Adjustments		<u>96</u>
		890
Add: Items not affecting the movement of funds:-		
Depreciation	1,006	
Movement in Deferred Taxation Accounts	<u>124</u>	
		<u>1,130</u>
		2,020
<u>From Other Sources</u>		
Increase in Long Term Debt		6,039
Decrease in Working Capital		<u>691</u>
		<u>\$8,750</u>
FUNDS WERE APPLIED TO		
Net Purchase of Fixed Assets & Goodwill		7,525
Purchase of Investments		25
Petroleum Mining Exploration Expenditure	1,620	
Less: Non-Recourse Loan	<u>(900)</u>	
		720
Payment of Dividend		<u>480</u>
		<u>\$8,750"</u>

This statement was incomplete insofar as it did not comply with SSAP No. 10 because it did not include a statement of changes in working capital.

41. For our purposes we have restated this, and other data in the report, as follows:-

During the year, additional funds were required to finance:-		\$000
increase in debtors and work in progress		6,736
increase in stocks		1,768
acquisitions of fixed assets and goodwill		7,556
acquisitions of investments		25
mining exploration		<u>720</u>
		<u>16,805</u>

Funds were raised from:-

Profit before tax, 1,140, add depreciation, 1,006, less tax provision, 967, less dividend paid, 240	939
Reduction of cash deposits	619
Increase in creditors	2,721
Increase in bank overdraft	2,326
Bills payable	3,200
Finance Leases	2,786
Mortgages	1,310
Term Loans	2,904
	<u>16,805</u>

A note showing how these items were derived is included in Appendix C. The accounts (Appendix B) disclosed the interest-bearing nature of the increased obligations (Note 2 page 23, Note 12 page 26, Note 13 page 26, Note 14 page 27).

42. Another restatement, prepared by Mr Alan J. Robb, which gives more details about operations, has been published (National Business Review, 21 October 1985). It is as follows:-

Perry Dines Corporation

Cash Flow Statement (Year Ended March 31, 1985)

<u>Sources of Cash</u>	<u>\$ Million</u>	<u>\$ Million</u>
From operations -		
Revenue	33.726	
Less increase in debtors	6.736	
		26.990
Expenses before tax	32.586	
Less depreciation	1.006	
	31.580	
Plus increase in inventory	1.768	
	33.348	
Less increase in creditors	2.762	
	30.586	
Less increase in bills payable	3.200	
		27.386

Cash surplus (deficit) from operations	(0.396)
Tax paid	1.149
Tax paid cash surplus (deficit) from operations	(1.545)
Increase in long term liabilities (excluding finance leases capitalised)	4.214
Increase in bank overdraft (net)	2.945
	5.614
<u>Uses of Cash</u>	
Purchase of fixed assets	4.629
Payment of dividend	0.240
Expenditure on Mining exploration	1.620
less non-recourse loan	0.900
	0.720
Increase in investments	0.025
	5.614

43. It is a matter of presentation. The facts were available in the Perry Dines report but we do not care for the format. We will ask the New Zealand Society of Accountants to consider this matter in their review of Statement of Standard Accounting Practice No. 10 "Statement of Changes in Financial Position". We will also include the subject of statements of the sources and uses of funds and cash flow statements in the terms of reference for our Review of the Law and Practice of Financial Reporting, which we intend to open for public enquiry later in the year.
44. The balance sheets of the group showed a decline in the equity ratio from 52.84% as at 31 March 1984 to 26.00% as at 31 March 1985. This change was expressly disclosed on page 30 of the Annual Report.
45. There was no reference in the annual report to the fact that during the year and at the time the accounts were approved by Directors, Sir George Chapman was Chairman of the Company. The company notified the Stock Exchange

promptly of Sir George's resignation. Nevertheless it came as a surprise to some shareholders to learn, when they received their 1985 annual report early in August, that he was no longer Chairman. Two shareholders expressed their misgivings to the Commission on this matter. Both said that they would not have invested in the company in the first place had they not known that Sir George, an experienced chartered accountant, was willing to serve on the board. His service was, they considered, an important matter. Although it is not required by law, we consider that the annual report of a listed company should name all directors who have served in the period under review, and if any have ceased to be directors before the report is printed, state the fact.

THE PROSPECTUS - PROSPECTS & FORECASTS/DIRECTORS' STATEMENT

46. The prospectus, dated 1 August 1985, included the following statements:-

"The Company expects the 1986 year turnover to be less than this years record. While after tax profit is projected to be similar to that achieved this year the Company's ability to secure work in the volatile heavy construction market will play a significant part in this year's result".

The Directors' Statement read:

"The Directors of the Company state that after due enquiry by them in relation to the period from 1 April 1985 to 1 August 1985, there have not, in their opinion, arisen any circumstances that materially adversely affect the trading of [sic] profitability of the Perry Dines Group, the value of its assets or the ability of the Perry Dines Group to pay its liabilities due within the next 12 months".

Of course the prospectus should be read as a whole - a copy is attached as Appendix A.

47. There is no record in the Perry Dines Board minutes of any consideration of those statements. The Commission has therefore examined the evidence relating to the period from the commencement of the new financial year on 1 April 1985 to the date of the prospectus, 1 August 1985, to ascertain whether in our view the directors had made an informed judgment on the affairs of the company as at 1 August 1985 which would justify the terms of the prospectus. The directors (Messrs. Dines, Irwin and Peacocke) said they were very much engaged in "hands on management" of the Company's affairs. Our opinion is that as at 1 August they had not made such a judgment, and that neither statement should have been made.
48. The cash position of Perry Dines had been a matter of concern to the directors for some time. The minutes of the board meeting on 16 April 1985 include the following report:-

"The Secretary reported that the cash position of the Company was still extremely tight but that the planned realisation of assets, namely:

1. Sale of the Aircraft
2. Sale and Lease-back of Nelson
3. Sale and Lease-back of the Head Office Building
4. Sale of Surplus Project Plant
5. Sale of Kennedy Equipment Limited and its Stock

would release in total an amount of \$5.59 Million gross which would be used to repay approximately \$4.47 Million of borrowings and the other \$1.1 Million being used to supplement Working Capital. This programme was planned to be completed by 31 July and it was noted that the major item, i.e. Sale of the Head Office Building would be among the last of the realisations and that in the meantime the tight cash position would continue. Accordingly arrangements had been made with the Bank of New Zealand to run the Overdraft into excess, on prior notice to the Bank, of up to \$250,000. Since this

would be at excess rates of up to 29% the facility would be used sparingly but provided a good fallback position to meet emergency requirements."

At the next board meeting on 27 May 1985, the board received a cash flow projection for the ensuing four months. The secretary is minuted as saying that:

"the tight position would continue until all the Asset Realisation Programme had been completed and that the amount allocated in the Cash Flow for payment to Creditors was the minimum amount which could be sustained and that it was imperative that this Flow be maintained in order to avoid strong action from the Creditors".

The Managing Director reported that Perry Dines Limited had "a serious work shortage ... All overhead staff have been progressively laid-off or transferred to Nelson. The outlook for heavy engineering does not look good with what appears to be a two year lull between major projects".

49. At the board meeting on 24 June 1985 (which Sir George Chapman did not attend), the Perry Dines board approved a budget for the year to end on 31 March 1986, showing forecasts of:-

Consolidated revenue \$23.2 million.
Consolidated profit before interest,
depreciation and corporate costs \$5.1 million.
Profit before tax \$1.3 million.
Provision for tax \$605,000.
Net profit after tax \$739,000.

The minutes also record, as a matter of regular reporting, a "Tender Summary" showing that, within the previous month Perry Dines had submitted 28 tenders for \$8 million, of which only 3 amounting to \$760,397 had succeeded.

50. The board met again on 2 July 1985 to approve the terms of the cash issue. Sir George Chapman, who had then resigned, was not present. The minutes, which consist

merely of resolutions apparently prepared in advance, contain no record of any discussion about trading prospects or trading performance to date for the year against budget, and there was no record of any discussion about the appropriateness of the terms of issue. The directors, with Sir George, met the Registrar on the same day. There were no further board meetings before the release of the prospectus.

51. The board next met on 7 August 1985, the day after the prospectus had been mailed to shareholders. Mr Huppert and Mr Chennells of Brierley by invitation of the directors were in attendance.

The "Tender Summary" recorded that in June and July, 41 tenders for work amounting to \$21,298,049 had been presented, of which only 7, amounting to \$475,008, had been accepted, while 12, amounting to \$17,184,445, were "under discussion". One of the 12 was a tender for \$13 million for work on the Glenbrook site of New Zealand Steel Limited, which was described as "the only field project of magnitude under consideration in the foreseeable future". The Managing Director reported that Perry Dines Limited, the principal subsidiary, was "suffering from serious shortage of major field work".

The minutes also record that settlement of major claims was late and in dispute, and that there were unbudgeted prior year claims by sub-contractors. The result of Perry Dines Limited for the period April to June 1985 was a loss of \$38,000 against a budgeted profit of \$277,000. Pio Pio Quarries Limited recorded a loss of \$48,000 for the quarter, somewhat better than budget, Egmont Plant Hire Limited recorded a loss of \$80,000 compared to a budget of \$3,000 profit. Anchor Dorman (New Plymouth) Limited recorded a loss of \$281,000 against a budgeted loss of \$328,000. Anchor Dorman Limited recorded a profit of

\$185,000 compared with a budget of \$197,000. No consolidated figures were recorded in the minutes. For the quarter ending June 1985 there appeared to be a loss of \$262,000 compared with a budgeted profit of \$99,000 according to the figures recorded in the minutes.

Mr. Dines told us that the directors also received at that meeting a set of accounts as at 30 June 1985. The minutes do not refer to them. Mr. Dines said he knew part of the figures on 5th August, and that the staff had worked through the night prior to the board meeting to present the accounts to the board on the 7th. The set consisted of a "Statement of Income for the three months to 30 June 1985" and a balance sheet as at that date for Perry Dines alone, and a "Consolidated Profit and Loss Account for the three months ended 30 June 1985" and a "Consolidated Balance Sheet as at 30 June 1985" for Perry Dines and its subsidiaries. The Consolidated Profit and Loss Account showed revenue \$3,584,153, expenses \$3,910,839 (including depreciation \$331,315), resulting in a loss of \$326,686.

The secretary reported at the meeting that almost all facilities were drawn down fully and that interest rates continued to climb. It was also clear that the asset realisation programme was well behind schedule.

52. The statement of prospects and forecasts in the prospectus projected a result "similar" to that achieved in the 1984/85 financial year - a projection which was not justified on the basis of the budget and information relating to the period from 31 March 1985 to 1 August 1985. The result for the first quarter of the year to which a budgeted profit of \$99,000 applied, showed a loss of \$262,000 or \$326,686. The claim to similarity for the full year must be seen, in our opinion, as untenable. To their credit, shortly after learning on 16 August of the failure of Perry Dines' tender for work at Glenbrook, the

directors recognised the position, and decided to withdraw the prospectus.

53. Counsel for the directors said that the interest and participation of the Brierley organisation was regarded as an encouraging sign. They also argued that the directors were dealing with a "dynamic situation which confronts all directors dealing with a crisis". With respect, that is not the picture portrayed in the prospectus. The state of affairs reported to the board on 7 August did not develop within the previous week. It had in fact been maturing for a long time and had become acute before 1 August. Unremunerative assets had not been sold as planned, interest-bearing commitments had increased, and the prospects of remunerative work being obtained had become remote. On that basis, the statements quoted in paragraph 46 should not have been made, and the prospectus should not have been issued.
54. The case exemplifies the importance of a substantial equity base, especially for companies which solicit confidence in their ability to carry out major commitments. Counsel for the directors submitted to us that in the heavy engineering contracting industry, losses resulting from low utilisation of plant during times of low work load may be compensated by extraordinary profits in times of high work load. That submission emphasises the necessity for a strong equity base.
55. A company with a weak equity base may invite the public to strengthen it by taking up shares, but the law requires that the weakness be displayed in the invitation with a clear statement of the current position. These are not formalities. Such statements in a prospectus are amongst the most important statements that directors make to their shareholders and the public. Unlike most other statements, which usually relate to times past, the

prospectus statements are concerned with the present and the directors' expectations for the future. The Commission suggests that the terms of a prospectus should be deliberately considered at a meeting of the Board, and that each director should conscientiously ask himself whether he can make the statements in it. The minutes should record that consideration.

USE OF THE SHORT FORM PROSPECTUS

56. We heard some criticism of the short form prospectus to the effect that investors were not given adequate time and information to make a decision. Each offeree must make his own decision to invest or not. The statutory policy is to require offerors to provide timely and material information. Our powers of intervention are limited to cases where the information provided is false or misleading. At the request of the directors themselves, we exercised those powers in this matter.
57. The Perry Dines shareholders received the prospectus and the annual report for the year ended 31 March 1985 by mail a day or two after 6 August 1985. They were required to have their application forms in the hands of the share registrar by 29 August. They had some 2½ weeks to make a decision.
58. Shareholders were presented with a newly issued annual report. It had not been considered or approved at a general meeting and had not been subject to analysis by the financial press and others. While it appeared to contain all essential information, it was not always easy to follow, particularly in respect of funds requirement. For those who had the time and the skill to see it, the financial statements showed that the company was very short of money.

59. The general investor would also observe that the shares had traded at around 80 cents at the beginning of the financial year, fluctuated in the range 75/80 cents through to early July, and in the period 5 July, when results for 1984/85 were announced to the Stock Exchange, to 18 July, traded down from 80 cents to 64 cents, a drop of some 20 per cent. On 26 August when trading was suspended shares stood at 65 cents ex-rights, having sold at as high as 85 cents ex-rights, in early August. Clearly there was evidence of buying support in the market, though trading was very volatile in the period 4 July to 26 August (when trading was suspended). We think that an investor influenced by share prices recorded on the Stock Exchange would have found sufficient justification for a decision to accept his entitlement. He may also have been influenced, as apparently the market was, by the Brierley announcement on 6 August that it now owned some 20% of the issued capital of the company.
60. The securities legislation does not prescribe a time within which an offer of securities must be kept open for acceptance. Listing Requirement 211 of the New Zealand Stock Exchange provides that applications are not to close for at least 15 business days after the day of mailing letters of entitlement, and renunciations are not to close for at least five more business days. These requirements were observed. We do not think any further time should be required under a mandatory rule.
61. We were more impressed by the point that the offer opened before the annual report had been considered by the shareholders in general meeting. There is no doubt about the utility of the procedure available under the Short Form Prospectus Exemption Notices, which allow the distribution of the annual report, notice of meeting, a rights issue prospectus and letters of entitlement at the same time. The obligation on the directors of Perry Dines

to face their shareholders in general meeting at a time when the cash issue was open for acceptance and rights were trading on the Stock Exchange must have been a salutary experience for the directors and an important occasion for shareholders. Accordingly, we suggest that an issue under this procedure should not close until some time, say 7 days, after the general meeting. This would enable those offerees who wish to do so to wait for discussion on the annual report at the meeting before making their decisions.

THE REGISTRAR OF COMPANIES

62. The Registrar of Companies became involved in the affairs of Perry Dines in the period under review in two ways. First, in April 1985 he undertook an inspection of the company under section 9A of the Companies Act 1955, and called on the Directors to see him about the company's affairs. Secondly, he was responsible for accepting or declining registration of the prospectus on or about 6 August 1985.

63. The Registrar has power, under s.9A Companies Act 1955 in the case of companies, and under s.67 Securities Act 1978 in the case of others who offer securities to the public, to inspect their records and take copies of them. The s.9A power is limited to that (Barr Burgess & Stewart v. Registrar of Companies (1985) 2 N.Z.C.L.C. case 96-059 (C.A.)). Under "the general power conferred on him by s.3 of the Act", he is entitled to obtain comment and advice about the state of affairs of a company (ibid. page 99-437). Amongst his powers, is one enabling him to present a petition to the High Court for an order winding up a company that is unable to pay its debts (ss.217, 218, 219 Companies Act 1955). The company, a majority of its directors and virtually every creditor each has a similar power to petition.

64. The inspection in April 1985 was handled with discretion. The fact that inspectors had visited the company at the beginning of April 1985 did not become public knowledge until after receivers had been appointed. The Registrar's letter of 20 June 1985 was delivered by hand, the terms of the Registrar's reservations were expressed carefully, and the matter appears to have remained confidential. At our hearing, we raised the question whether the inability of the company to obtain work had been contributed to by any leak of the fact of the Registrar's interest in April. From the responses to this suggestion, we are satisfied that there was no leak. There was a general impression amongst persons interested in doing business with Perry Dines that the company was in difficulties. That arose from delay in paying creditors.
65. The Registrar must think long and hard before presenting a petition to wind up a company. Such an act usually destroys any prospect of a company in difficulties making a recovery. Where he makes his reservations plain to the directors, and is met with strong assertions that the directors are moving to deal with the problem, he faces the question whether he should substitute his business judgment for theirs. His powers to apply to the Court, which are the same as those of any creditor, should be exercised only in plain cases. We have no doubt that the Registrar acted correctly in reminding the Directors of their responsibilities and refraining from moving to wind up the company.
66. As to the question of registration of the prospectus, the evidence disclosed an unsatisfactory position. The document, dated 1 August 1985, reached the District Registrar at New Plymouth on 6 August, with a cheque for the registration fee and a letter from the secretary of Perry Dines asking the Registrar to register the document. The Registrar issued a receipt for the fee, but did not

issue a certificate of registration under s.42(5) Securities Act 1978. The document, with the notification from the New Zealand Stock Exchange mentioned in paragraph 24, was placed upon the public file kept by the District Registrar in respect of Perry Dines. It was seen by solicitors who searched that file. Until the Registrar made the public statement mentioned in paragraph 35, everyone concerned, including ourselves, understood that the document had been registered. On 2 September 1985 the Registrar said it had not been registered.

67. Registration is an important step in the process of issuing a prospectus. It is unlawful to make an offer of securities to the public until a prospectus has been registered (s.33 Securities Act 1978). The Registrar may refuse registration in certain cases (s.42, *ibid.*). Upon registration, the Registrar is required "forthwith" to give a certificate of registration (s.42(5)). The certificate is "conclusive evidence" that the prospectus has been registered. It is clear that the issue of the certificate is not the act of registration - it is evidence of that act. What does in fact constitute registration, where a certificate has not been issued, is perhaps open to debate. We think that the action by the Registrar's staff of placing the document on the public file is evidence of registration.
68. We have asked the Registrar to review his procedures on the point, to ensure:-
- (a) that a person who presents a document for registration will be informed promptly whether or not the document has been registered, and
 - (b) that documents presented for registration will not be placed upon the public file until they have been registered.

69. The power to decline to register a document presented for registration was introduced on the recommendation of the Macarthur Committee by the Companies Amendment Act 1973. Section 42 Securities Act 1978 applies the power to documents presented for registration as prospectuses. We think the power, and the operation of it, should be reviewed in the context of a general review of the law of incorporation.

THE TRADING OF SHARES AND RIGHTS

70. According to the 1985 annual report the 20 largest shareholders in Perry Dines at 31 March 1985 were:

	<u>Number of Shares</u>	<u>%</u>
Dines Construction Limited	3,229,300	40.37
National Bank of N.Z. (Nominees) Limited	660,000	8.25
Australian Mutual Provident Society	584,200	7.30
Colonial Mutual Life Assurance Society Ltd	358,100	4.48
Norwich Union Life Insurance	200,000	2.50
Investment Nominees Limited	163,800	2.05
The Mutual Life & Citizens Assurance Company Ltd	158,200	1.98
Commercial Union General Insurance Company Ltd	145,000	1.81
Leadenhall Superannuation Nominees Limited	120,000	1.50
The New Zealand Insurance Company Limited	100,000	1.25
V.A. Slack	40,000	0.50
Brittco Properties Limited	27,100	0.34
L.W.N. Fitch	25,000	0.31
Sir George Chapman	25,000	0.31
K.W. Irwin	25,000	0.31
M.G. Dines	24,000	0.30
J.G. Wright	22,000	0.28
R.C. Christey	21,000	0.26
B.J. Vieceli	20,200	0.25
Norwich Winterthur Insurance (N.Z.) Limited	20,000	0.25
	<hr/>	<hr/>
	5,967,900	74.60
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71. In the period from 1 April 1985 to 26 August 1985, as appears from the share register, about 2.55 million shares changed hands. We have analysed these transactions as follows:-

Transactions reported to the Exchange -	700,000 shares
Other transactions	
- At Stock Exchange prices	379,000 shares
- At different prices	1,471,000 shares
	<hr/>
Total	2,550,000 shares
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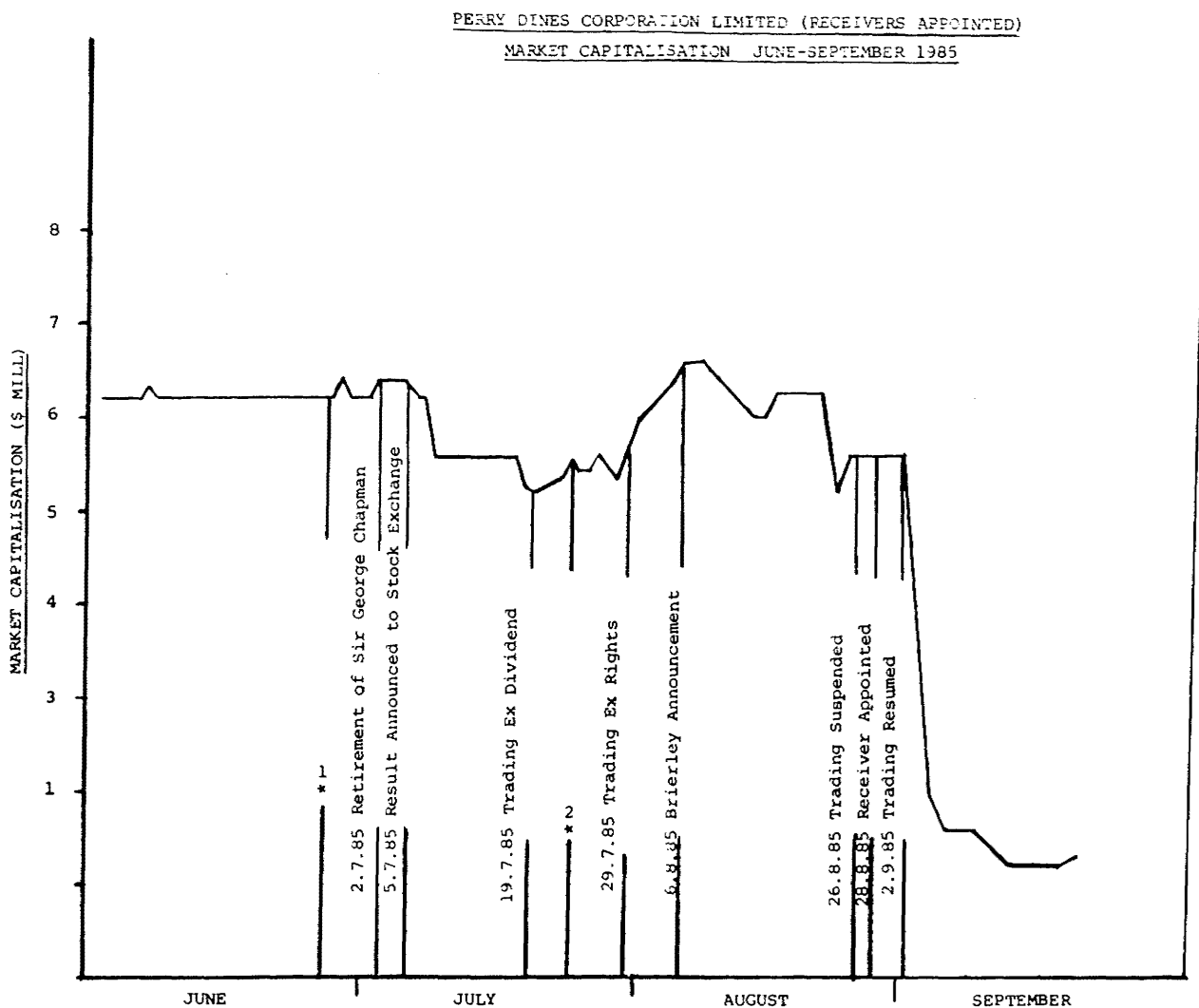
The 1,471,000 shares at prices different from contemporary prices on the Stock Exchange were comprised in 3 transactions, viz:

18 April - 1,000 shares at 88 cents per share
(Stock Exchange price 80 cents per share)
27 June - 20,200 shares at 84 cents per share
(Stock Exchange price 80 cents per share)
24 July - 1,450,000 shares at 30 cents per share
(Stock Exchange price 68 cents per share)

The transactions of 27 June and 24 July are included in the 1,957,900 shares acquired by the Brierley organisation that are referred to in para. 73.

72. In connection with our review of takeover law and practice, we have been examining the question whether prices in ordinary daily trading on the Stock Exchange indicate the value of the company. We regard the movement of share prices during the period from the beginning of June until the collapse of the company as significant in this respect. The "market capitalisation" of Perry Dines was more or less steady at \$6.40 million until 4 July, but behaved somewhat erratically until the collapse of the company was announced on 29 August, falling to the low

point of \$5.12 million on 17 July, attaining \$6.56 million more or less coincident with Brierley's announcement on 6 August of its 19.45% holding, and of course collapsing with the announcement of the appointment of receivers. Details of the share trading reported to the Stock Exchange are included in Appendix D, and the changes of "market capitalisation" are indicated by the following graph:-



OFF MARKET TRANSACTIONS (Refer to paragraph 71)

- * 1 - 27.6.85 Purchase by Brierley from B.J. Viecelli at 84 cents per share
- * 2 - 24.7.85 Purchase by Brierley from Dines Construction Ltd at 30 cents per share.

73. In the period from 1 April 1985 to 26 August 1985, the Brierley organisation acquired about 1,957,900 shares, to bring its total shareholding to 2,139,700 shares. 1,450,000 shares in the Brierley holding came from Dines Construction Limited on 24 July 1985 at 30 cents per share. The Stock Exchange prices were then 68 cents per share. Mr. Dines explained that he was concerned to induce Brierley to take an active interest in Perry Dines. The average cost of the Brierley acquisitions before the purchase from Dines Construction Limited was about 85 cents per share. Mr. Huppert of Brierleys told us that he said to Mr. Dines, "If we are going to get involved with your company, obviously our average cost at this particular point of time is too high ... we would prefer to have a lower entry cost and to that end we negotiated the price of 30 cents cum dividend ..." The result was to reduce the average cost of the Brierley holding to 47.5 cents per share. We are unable to say that any of these more or less contemporary figures - 30 cents, 47.5 cents, 68 cents per share - represented the value of Perry Dines as a whole. Obviously Mr. Huppert later thought 30 cents was too much having regard to the actual state of affairs of Perry Dines unknown to him at the time of purchase. On 24th August he informed Mr. Dines that Brierleys had reviewed their position as shareholders and were no longer willing to be represented at board level.
74. As to Dines Construction Limited, it may be noted that the shares sold by that company to Brierley at 30 cents each had been allotted to Dines Construction Limited for 25 cents each. We were told by Mr. Dines that Dines Construction Limited retained the rights to the new issue. On 25 July, Dines Construction Limited paid to Perry Dines \$380,000, and there was a further payment of \$400,000 on 9 August. We were told that there are legal questions as to the effect of these payments on which we express no opinion. Whatever the legal position may be, the fact of

payment may be taken as evidence of Mr. Dines' continuing confidence in Perry Dines at the time of payment.

75. Sir George Chapman sold his shares through the Stock Exchange soon after his resignation from the Perry Dines board and after the results for the year ended 31 March 1985 and the proposal for the cash issue had been announced. Sir George had ceased to be a director at that time, but his conduct observed the guidelines issued by the New Zealand Stock Exchange for the guidance of the directors and officers of listed companies in relation to dealings in the shares of the company (March 1982).
76. Mr M.G. Dines bought 36,200 shares and 242,766 rights during the period. The consideration for the shares was \$24,225, averaging 67 cents per share. The consideration for the rights was, on average, less than one cent each.
77. Rights traded on the exchange in the range 1 to 10 cents. Some 13,500 rights were traded on market. It appears that some rights may have been traded off market.

SUMMARY OF CONCLUSIONS

78. (a) The "Statement of Changes in Financial Position" that was included in the annual report did not comply with SSAP No. 10 and did not present information in a manner comprehensible to investors (paras. 40-43).
- (b) The annual report should include the names of directors who have served in the period under review (para. 45).
- (c) The directors who signed the prospectus dated 1 August 1985 had not made an informed judgment of the state of affairs of Perry Dines as at that date (paras. 46-55).

- (d) The statements in the prospectus mentioned in para. 46 should not have been made (paras. 46-55).
- (e) No change is proposed to the law relating to short form prospectuses at this stage, but issuers using the procedure under The Securities Act (Short Form Prospectus) Exemption Notice 1985 (S.R. 1985/308) are asked to ensure that the offer does not close until at least 7 days after the annual general meeting (paras. 56-61).
- (f) The Registrar of Companies acted correctly in deciding that he would not apply to the Court to wind up Perry Dines (paras. 62-65).
- (g) The procedure for registering prospectuses is not satisfactory. We have asked the Registrar to review his procedures (paras. 66-68).
- (h) The Registrar's power to decline to register documents should be reviewed in the context of a general review of the law of incorporation (para. 69).

FURTHER CONSIDERATION

- 79. We have decided to refer this report to the Institute of Directors, the Listed Companies Association and the New Zealand Stock Exchange for their consideration generally, and we will ask them to consider whether, in their opinion, any change to the law or practice is desirable.
- 80. We will also refer this report to the New Zealand Society of Accountants with a request to review Statement of Standard Accounting Practice No. 10, "Statement of Changes in Financial Position".

81. We have asked the Registrar of Companies to review his procedures for registration, and to issue a statement of practice on the subject.

Chairman

22 May, 1986

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