Our Ref: AJ
Your Ref:

19 May 2008

Huntley Management Limited
Suite 301, 37 Bligh Street
SYDNEY NSW 2000

Attention John Knox

Dear John,

Australian Olives Project – Member management of Groves

Thank you for your email of 16 May 2008.

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Executive Summary

The Grove Agreements do permit self management. However these provisions in our view are inconsistent with the overriding obligation of the responsible entity to "operate" the scheme. For the Groves to be self managed either directly or by appointment of another manager would mean that the entities managing the Groves that form part of the scheme are "operating" the scheme at least in those respects and not your company. The provisions arguably are therefore void and unenforceable.

Alternatively you have the power pursuant to clause 28 of the Constitution to amend the Grove Agreements by the deletion of clause 5 of the Grove Agreements. If the self management of some Groves will affect the management of other members' Groves and members as a whole then in our view you can be reasonably satisfied that such an amendment would not adversely affect members' rights.

Therefore our recommendations are:

- you respond to any requests by members to self manage by informing them that to do so would be in breach of the Corporations Act, 2001 and may cause the scheme to be wound up; and,
- you enter into a Deed Poll to amend the Grove Agreements by deletion of clause 5.

There is some risk in doing so but should an issue arise you may apply to the Court for advice on whether compliance with the self management provisions will constitute a breach of the Corporations Act, 2001.

Liability limited by a scheme approved under Professional Standards Legislation (for matters conducted in NSW)

Advice

The Grove Agreement permits three forms of member election in relation to the Member's Grove.

The first is where a Member may elect to carry out its own maintenance which is limited to weeding, cultivating, fertilising and pruning (Clause 5.1). The conditions are that the Member gives at least 21 days written notice and they comply with the Grove Licence Agreement.

There is no obligation on you to reduce the fees in such event but you may do so but this is at your absolute discretion. If you wished to deter the practice you would simply not give a reduction in fees.

However if the Member does not do it properly you can rectify it and charge the member a fee for fixing it up.

The second is where a Member may elect to have their olives harvested separately (clause 5.2). This requires notice to be given 90 days before a Production Period by the Member. You then give them notice when the harvest is to take place, when the oil is available for collection and the fee payable by the Member for the harvesting. Within 7 days after that notice the Member must give you a bank cheque for the harvest fees and any other fees payable to you or any other party under the Grove Agreement or Constitution.

The third is where a Member elects to harvest and market their own olives (clause 5.3). This requires notice to be given 90 days before a Production Period by the Member. The olives are at the Member's risk from when the Member first enters the property and storage is the Member's problem. Also if the Member does not perform an adequate harvest to the extent that other Groves are affected then you may enter the Grove to make good any damage and complete the harvest in a proper manner and charge the member for the work.

The fourth is where a Member elects to manage their own Grove completely. If they do this then you are released from all liability to carry out any duties in the Agreement (clause 5.4). It is noted however that this does not release you from liability as a responsible entity to which we refer later in this letter. They can advise you in writing that they require you to supply water for which a fee is payable. However you may give 30 days notice to the Member requiring them to make good damage to their Grove or any other Grove caused by the failure by the Member to manager the Grove in a property manner r to conduct adequate maintenance or bring it up to a similar standard of other Groves. If the Member fails to comply with the notice you can do the work and charge them for it.

The above are contractual obligations. Apart from practical issues as to how this could possibly work, there are some Corporations Act issues that conflict with these contractual obligations. Unfortunately there is a paucity of authority to give any assistance in resolving the conflict discussed below and to protect yourself you may need to apply to the Court for a direction under the Trustee Act, 1925. This is because you are put in the impossible position of having to comply with contractual obligations that are in conflict with duties that you have as a responsible entity.

The first problem with the contractual obligations is that they conflict with the statutory requirement in relation to registered schemes. The responsible entity is required to operate the

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scheme ([1]). In this context The word "operate" has its ordinary meaning and is not limited to ownership or proprietorship "but rather to acts which constitute the management of or the carrying out activities which constitute the managed investment scheme." ([2]).

Any person that carries on a function that involves operation of the scheme must be an agent of the responsible entity ([3]). The management of the members' Groves is a function that forms part of the operation of the scheme. The members who self manage are not appointed as agent of the responsible entity.

We note that in a review of various schemes. ASIC required changes to be made to certain schemes where the members appointed a scheme manager to operate the scheme and not the responsible entity stating:

> " Scheme members can appoint a manager for the scheme, however this breaches the law if the manager effectively becomes 'responsible' for operating the scheme. As a result, the rights and interests of investors can be diminished, as the scheme members may not be able to rely on the RE for redress in the event of loss caused by an act or default of the manager." ([4])

It appears to us that if the members or a person appointed by them are carrying out any of the management duties in relation to the scheme such as maintenance and harvesting of the Groves they are carrying out activities that constitute "operating" the scheme. In doing so they are not the agent of the responsible entity. A person must not operate a scheme that is required to be registered unless the scheme is registered and the person operating the scheme is a public company that holds an Australian financial services licence that authorises it to operate the scheme ([5]).

Therefore in our view the contractual provisions conflict with the statutory provisions. Arguably the members who self manage their Groves or any person appointed by them to manage their Groves are acting in breach of the Corporations Act, 2001. Therefore the contractual provisions are not enforceable and could cause the Project to be wound up ([6]).

The second problem with the contractual obligations is that you owe certain specific duties to members. One of those duties is that you must treat all members who hold interests of the same class equally and members who hold interests of different classes fairly.

There is nothing in the Constitution that makes any interest in the respective Projects different from any other interest so this would mean there is only one class of members. This means that if you comply with the contractual obligations you are not treating members equally. The only

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[1] section 601FB(1) of the *Corporations Act, 2001*

[2] *Australian Securities and Investments Commission v Pegasus Leveraged Options Group Pty* (2002) 41 ACSR 561 at 574; *Re Lawloan Mortgages Pty Ltd* [2003] 2 Qd R 200 at 218; *Australian Securities and Investments Commission v IP Product Management* (2002) 42 ACSR 343 at 349; *Australian Securities and Investments Commission v Arafura Equities Pty Ltd* [2005] QSC 376 at [3]; *Australian Securities and Investment Commission v. Atlantic 3 Financial (Aust) Pty Ltd & Ors* [2006] QSC 132 (5 June 2006) at [19]

[3] section 601FB(2) of the *Corporations Act, 2001*

[4] ASIC IR 03/03

[5] sections 601(ED(5), 601EE(1) and 601FA of the *Corporations Act, 2001*

[6] section 601EE of the *Corporations Act, 2001*

basis on which this duty could not be breached would be if the members who make the appropriate election are considered to be members of a different class. Although the Constitution does not strictly separate interests into separate classes, it may be arguable that members who have a right to manage their own Grove by election become a separate class. The AAT has held that having different bands of investors within a mortgage trust determined by the amount invested to which band there was a different rate of return was sufficient to constitute the bands as separate classes ([7]). If they were held to be a separate class then this duty would not be breached. The position is not clear.

However notwithstanding the above. we are of the view that you have the power to amend the Grove Agreements to remove clause 5. of the Grove Agreement which contains the provisions permitting member management as discussed below.

Clause 28 give you power to amend the Grove Agreement to such extent as may be required to enable the provisions of the Grove Agreements or the Project "to be more conveniently, advantageously, profitably or economically administered or managed." The only requirement is that you must be satisfied that the amendment does not adversely affect the rights of Members.

We cannot see how the Project can be conveniently, advantageously, profitably or economically administered or managed with some Groves managed by the responsible entity and others managed by the Members. Therefore to avoid any problems we are of the view that you could amend the Grove Agreements to remove clause 5 because to do so would be "to be more conveniently, advantageously, profitably or economically administered or managed." The only issue would be whether you can be reasonably satisfied that the amendment does not adversely affect the rights of Members.

There is no doubt such an amendment does affect the rights of Growers as a whole (the section refers to "members'" not "member's") ([8]). The question is whether this affectation is adverse to members' rights. There is not much assistance in the case law. At best it seems to be accepted that the words do not have a settled meaning and operation ([9]). ASIC have in the past been of the view that the duties of a responsible entity under sections 601FC(1)(c) and (d) are relevant to the question of whether members' rights are adversely affected ([10]).

In our view it would be consistent with your duties under these sections if these amendments were made. This is because you could properly form the view that it is in the best interests of members as a whole for the amendments to be made. This is because self management would interfere with the rights of those members who did not wish to self manage making management of those member's Groves difficult. The amendment would also be treating members of the same class equally and if the self managed Groves were considered a separate class is treating them fairly.

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[7] *Equitiloan Pty Ltd and Australian Securities and Investments Commission* [2003] AATA 367 (24 April 2003)

[8] *Smith v Permanent Trustee Australia Ltd* (1992) 10 ACLC 906

[9] *Re Homemaker Retail Management Ltd* (2002) 40 ACSR 116; *Seabrook, in the matter of the Takeovers Panel & the Corporations Act 2001 (Cth)* [2002] FCA 1219 (2 October 2002)

[10] SPS 135.41

Therefore if self management by Growers of some of their Groves will interfere with the proper management of other members' Groves then in our view you could be "reasonably satisfied" that the amendment does not adversely affect the rights of members.

In that event you should amend the Grove Agreements by Deed Poll by removing clause 5.

If you were concerned about a fight with the members over this amendment it is possible for you to seek advice from the Supreme Court pursuant to section 63 of the *Trustee Act, 1925*. This is expensive and time consuming. Although you would be entitled to be indemnified for the costs of seeking the advice we would not recommend it unless you considered members may take action.

If you have any queries please do not hesitate to contact us.

Yours faithfully
Piper Alderman

Per:

Alan Jessup
Partner