SUPREME COURT OF QUEENSLAND

CITATION:	*Cannon Street P/L & Ors v Karedis & Ors* [2004] QSC 104
PARTIES:	**CANNON STREET PTY LIMITED** **(ACN 001 302 085)** (first plaintiff) **MARGARET ELIZABETH KELLY** (second plaintiff) **TIMOTHY CHRISTOPHER KELLY** (third plaintiff) **v** **THEO KAREDIS** (first defendant) **GREGORY KAREDIS** (second defendant) **PESUTU PTY LTD** **(ACN 002 276 208)** (third defendant) **GTK RETAILING PTY LTD** **(ACN 002 031 414)** (fourth defendant)
FILE NO:	BS11302/03
DIVISION:	Trial Division
PROCEEDING:	Trial
ORIGINATING COURT:	Supreme Court
DELIVERED ON:	30 April 2004
DELIVERED AT:	Brisbane
HEARING DATE:	29, 30, 31 March and 1, 2, and 14 April 2004
JUDGE:	Muir J
ORDER:	**That the defendants have judgment in the action with costs, including reserved costs to be assessed on the standard basis.**
CATCHWORDS:	CONTRACT – GENERAL CONTRACTUAL PRINCIPLES – MATTERS NOT GIVING RISE TO BINDING CONTRACT– STATEMENTS OF INTENTION, NEGOTIATIONS – CONSIDERATION – NECESSITY FOR CONSIDERATION – where discussions took place between the parties concerning an option for the plaintiff director to increase his shareholding in the company and also concerning a requirement that there be unanimity on all board decisions – whether there was a binding option agreement –

whether there was a binding agreement requiring unanimity on all board decisions - whether the parties intended to be bound – whether there was valuable consideration to support these agreements – whether any option agreement was discharged or terminated by a later inconsistent agreement

CORPORATIONS – MANAGEMENT AND ADMINISTRATION – DIRECTORS - FIDUCIARY POSITION – (CTH) CORPORATIONS ACT 2001 s 201 – where the defendant directors had been negotiating the sale of the company – whether the defendant directors breached their fiduciary duties

DERIVATIVE ACTION – LEAVE TO COMMENCE – GOOD FAITH – BEST INTERESTS OF THE COMPANY– (CTH) CORPORATIONS ACT 2001 s 237 – where the plaintiff director pursuant to s 237(2) of the Corporations Act 2001 sought to bring proceedings on behalf of the company under s 236 – whether the plaintiff was acting in good faith and in the best interests of the company – meaning of good faith – considerations applicable to a determination of good faith

Corporations Act 2001, s 102(1)(a), s 237

Australian Broadcasting Corporation v XIVth Commonwealth Games Ltd [1988] 18 NSWLR 40
B Seppelt & Sons Ltd v Commissioner for Main Roads (1975) 1 BPR 9147
Bellamy v Debenham (1890) 45 Ch D 481
Brambles Holdings Limited v Bathurst City Council [2001] NSWCA 61
Brogden v Metropolitan Railway Co (1877) 2 App Cas 666
Cannock Chase DC v Kelly [1978] 1 WLR 1
Central Estates (Belgravia) Ltd v Woolgar [1971] 3 All ER 647
GR Securities v Baulkham Hills Private Hospital Pty Ltd (1986) 40 NSWLR 631,
Harlowe's Nominees Pty Ltd v Woodside (Lakes Entrance) Oil Co NL (1967-1968) 121 CLR 483
Integrated Computer Services Pty Ltd v Digital Equipment Corp (Aust) Pty Ltd (1988) 5 BPR 97326,
J J Savage & Sons Pty Ltd v Blakeney (1969-1970) 119 CLR 345
Masters v Cameron (1954) 91 CLR 353,
Meates v Attorney-General [1983] NZLR 308,
Mills v Mills (1937-1938) 60 CLR 150,
Ngurli Ltd v McCann (1953) 90 CLR 425
Pagnan S.p.A v Feed Products Ltd [1987] 2 Ll Rep 601,
Perry v Suffields [1916] 2 Ch 187,
Richard Brady Franks Ltd v Price (1937) 58 CLR 112

Department of Education, Employment, Training and Youth Affairs v Price (1997) 152 ALR 127
Smith v Morrison, Smith v Chief Land Registrar [1974] 1 All ER 957
Storer v Manchester City Council [1974] 1 WLR 1403,
Swansson v R A Pratt Properties Pty Ltd (2002) 42 ACSR 313
Tallerman & Co Pty Ltd v Nathan's Merchandise (Victoria) Pty Ltd (1956-1957) 98 CLR 93
Thorby v Goldberg (1964) 112 CLR 597,
United Dominions Corporation (Jamaica) v Shoucair [1969] 1 AC 340
Vroon BV v Foster's Brewing Group [1991] 2 VR 32,
Williams v Spautz (1992) 174 CLR 509

COUNSEL: P O'Shea QC and I Perkins for the plaintiffs
N Hutley SC and D Clothier for the defendants

SOLICITORS: Mallesons Stephen Jaques for the plaintiffs
Clayton Utz for the defendants

The parties

[1] Mr Timothy Kelly, the third plaintiff in these proceedings, is the controller of the first plaintiff, Cannon Street Pty Limited and the beneficial owner of all of its shares. The second plaintiff, Mrs Margaret Kelly, his mother, holds her shares in Cannon Street in trust for her son. Mr Kelly, together with Mr Theo Karedis (the first defendant) and Mr Gregory Karedis (the second defendant) are the directors of The Grape Management Pty Ltd ("TGM"). TGM holds all of the shares in Hotel Wickham Investments Pty ltd ("HWI"). Where it is unnecessary to distinguish between those companies they will be referred to collectively as "The Grape".

[2] The companies carry on the business of liquor merchants through approximately 14 retail outlets under the "The Grape" name. They also own and operate a number of hotels in Queensland.

[3] In about 1992, Mr Kelly conceived the notion of setting up The Grape business and enlisted the financial support of a number of investors including Mr Clive Kitchen. The plaintiffs, Mr Kitchen and those investors, in some cases through companies, became the initial shareholders of TGM and HWI. It is convenient for present purposes to refer to them all (with the exception of the plaintiffs) as "the "A" Class shareholders" and to such investors, excluding the plaintiffs, as "the majority "A" Class shareholders".

[4] Mr Kelly is the beneficial owner of 7.7% of the shares in TGM. The balance is held equally by Pesutu Pty Ltd, a company controlled by Mr T Karedis, and GTK Retailing Pty Ltd, a company controlled by Mr G Karedis.

[5] Mr T Karedis is the founder and former chief executive officer of a group of companies which carried on the "Theo's" business of wholesale retail liquor suppliers and hotel operators in New South Wales and the Australian Capital Territory. Mr G Karedis is Mr T Karedis's son.

The plaintiffs' claims

[6] Cannon Street and Mrs Kelly claim –

(a) a declaration that they have an option to purchase from Pesutu and GTK 12.3% of the issued share capital in TGM for the sum of $2.6 million;

(b) a declaration that in order to be validly passed, any resolution proposed at a meeting of shareholders of TGM or HWI must be passed unanimously.

[7] Mr Kelly claims –

(a) a declaration that in order to be validly passed, any resolution proposed at a meeting of directors of TGM or HWI concerning the sale of the business of either company must be passed unanimously;

(b) an order permanently restraining the implementation of a resolution for the adoption of a sale process for the sale of the business of TGM and HWI purportedly passed by a majority of directors of each of TGM and HWI on 10 November 2003

[8] All plaintiffs seek leave pursuant to s 237 of the *Corporations Act* 2001 to bring proceedings, on behalf of and in the name of TGM and HWI, against the first and second defendants, for an order permanently restraining the implementation of the 10 November resolution.

[9] The claims for declaratory relief are not supported by the constitutions of TGM and HWI, but are based on oral agreements alleged to have been entered into between Mr Kelly on behalf of the plaintiffs and the Karedises on behalf of the defendants.

[10] The option agreement is alleged to have been entered into in the course of discussions in January and February 2002 and confirmed in a meeting on 27 February 2002. The agreement that resolutions of directors and shareholders of The Grape would be passed only by unanimous vote is alleged to have been entered into in that meeting also.

The defendants' contentions

[11] It is denied that the words alleged to constitute the agreements were said and that there was any intention by the parties to be legally bound. Additionally, it is alleged that neither agreement is supported by valuable consideration.

[12] In the case of the unanimity agreement, it is alleged that it was void for uncertainty as essential terms had not been resolved. Alternatively, it is alleged that, if there was an option agreement, it was discharged by an agreement entitled "Authority to Agent" entered into on 9 March 2002 at Coolum.

[13] In the further alternative, it is alleged that if there was an option agreement it lapsed due to effluxion of time.

[14] The defendants oppose the making of an order under s 237 of the *Corporations Act* on the grounds that –

(a) The plaintiffs are not acting in good faith – Mr Kelly wishes "to secure to himself benefits as a consequence of his dealings with Woolworths Ltd";

(b) It is not established that it is in the best interests of The Grape that the plaintiffs be granted the leave which they seek.

Historical narrative

[15] In 1999, Pesutu and GTK each acquired "B" Class shares in the capital of GTK and HWI. The purchase gave them fifty percent of the issued shares which were then divided into "A" Class shares, "B" Class shares and an "A" Class management share held by Mr Kitchen, the chairman and managing director of both companies.

[16] In 2000, and 2001, Mr Kelly had had a falling out with Mr Kitchen and sought to persuade Mr T and Mr G Karedis that Mr Kitchen should be removed as managing director. The Karedises were reluctant to take action initially but Mr Kelly, armed with advice from Mr Loel, a solicitor, persisted in his move against Mr Kitchen. Mr Kelly eventually succeeded in having Mr Kitchen removed as managing director and himself appointed acting managing director in his place. On 5 September 2001, Mr T Karedis was appointed chairman.

[17] In September and October 2001, allegations were made by the Majority "A" Class shareholders that Mr Kelly's appointment as managing director was invalid and that he was in breach of duties owed to the "A" Class shareholders. In October, Calabro and Partners delivered a report which concluded that Mr Kitchen had breached his duties to The Grape in various respects. The Grape threatened to bring legal proceedings against Mr Kitchen.

[18] In late November 2001, Mr Kelly was approached by two other "A" Class shareholders or their representatives and provided with a document headed "Proposal for Consideration by 'A' Class Shareholders." The document, which Mr Kelly says he was assured by the persons just mentioned was *bona fide*, was in respect of a proposed offer by Doogle Pty Ltd to acquire all of the shares in TGM and HWI for $38,250,000 and appeared to have been prepared by or with the assistance of a person with a detailed knowledge of The Grape's affairs. It assessed the advantages and disadvantages to the "A" Class shareholders of accepting or rejecting the offer and recorded the desire of some of the Majority "A" class shareholders to retire from business. It acknowledged, as was the fact, that Pesutu and GTK had pre-emptive rights under which, in the event of an offer to acquire shares in TGM and HWI, they had the right either to acquire the "A" Class shares on the same terms and conditions or to accept the offer. The Karedises considered that the offer price was too high and decided against exercising pre-emptive rights.

[19] Almost immediately after finding out about the Doogle offer, Mr Kelly decided that his interests were best served in rejecting it. His decision in that regard was communicated to other "A" Class shareholders in a memorandum dated 4 December 2001, a draft of which had been sent by him to Mr T Karedis on 30 November 2001. On 1 December, Mr Kelly sent by email to Mr G Karedis and Mr Loel a memorandum recording the contents of discussion between himself and representatives of the "A" Class shareholders.

[20] Friction continued between Mr Kelly and the majority "A" class shareholders interests. Each side engaged solicitors and the majority "A" class shareholders persisted with a threat to have Mr Kelly removed as a director of The Grape. Allegations against Mr Kelly were made to the Karedises by the majority "A" class shareholders. Mr Kelly responded to them in an email to the Karedises of 11

December 2001 in which he highlighted his own abilities and achievements and criticised the conduct of the other "A" class shareholders.

[21] On 25 January 2002, Mr Kitchen, on behalf of the majority "A" class shareholders, wrote to Mr T Karedis confirming acceptance of the Karedises' offer to acquire the majority "A" class shareholders' shares in The Grape.

[22] In late February 2002, Mr Kelly was receiving advice from Mr Evans of Price Waterhouse Coopers concerning ways in which Mr Kelly could acquire further shares in The Grape. Consequent on those discussions, Mr Evans, on 27 February, faxed to Mr Kelly a document headed "Draft for preliminary discussion purposes only". The covering letter advised –

> "Once you have discussed this matter in principle with your business partners, we will be in a better position to assess the alternatives which can be considered, and provide more prescriptive advice in relation to the transaction. In particular, at that time, we will need to discuss with you the impact of any proposal on The Grape group which we have not considered in any detail to date.
>
> As discussed with you carefully drafted documentation will need to be attended to before the arrangement can be finalised."

The evidence of the parties about their communications in relation to the Doogle offer.

[23] Mr Kelly gave the following evidence in relation to communications between himself and the Karedises after the making of the Doogle offer. He

> "was having almost nightly telephone conversations with Theo Karedis in relation to the business of The Grape and the Doogle offer. Theo Karedis kept saying to me that the future of The Grape was looking good if I stayed with the business and that the buying power of Theo's group of companies and the guarantees that could be offered by interests associated with Theo Karedis made it advantageous to maintain an investment in The Grape."

[24] He said that he decided to assist the Karedises for two reasons. The first was that Mr T Karedis did not seek to bully or persuade him to reject the Doogle offer but, instead, pointed out the benefits of his remaining in The Grape. The other reason was that, based on his discussions with Theo Karedis, he understood that he had an ability to increase his shareholding.

[25] Mr T Karedis swears that at no time did he discuss with Mr Kelly that he wanted him to reject the Doogle offer in order to assist the Karedises in acquiring those "A" Class shares not held by the plaintiffs. He also swears that Mr Kelly did not inform him that his purpose in rejecting the Doogle offer was to provide assistance to the Karedises. On the contrary, he asserts that Mr Kelly advanced other reasons for his not wanting to accept the offer.

[26] Mr G Karedis also swears that he did not ask Mr Kelly to reject the Doogle offer in order to assist the Karedises and that Mr Kelly, at no time, told him that his purpose in rejecting the offer was to provide assistance to the Karedises. He swears that he doubted the genuineness of the Doogle offer, which was never sighted by Mr Kelly or the Karedises.

[27] Various discussions and negotiations then took place between some "A" Class shareholders and Mr T Karedis, between Mr Kelly and "A" Class shareholders and between Mr Kelly and Theo and Greg Karedis. The Karedises told Mr Kelly, as was the case, that they did not wish to sell their shares in TGM and HWI. It is probable also that they told him that they did not wish to purchase the "A" Class shareholders' shares in competition with the Doogle offer because that would result in their having to pay a price they would prefer not to pay. Eventually, as is noted earlier, the majority "A" class shareholders agreed to sell their shares to Pesutu and GTK.

Mr Kelly's evidence as to the existence of the option agreement and as to the requirement of unanimity for resolutions of directors and shareholders

[28] The following account is given by Mr Kelly in his affidavit sworn on 17 March 2004.

[29] There were discussions in January and February 2002 between him and the Karedises on an almost daily basis concerning the prospect of his increasing his shareholding in TGM and the manner in which that might be accomplished. In the course of the conversations there was acceptance that the price would be that paid to Mr Kitchen's interests and also agreement as to Mr Kelly's percentage shareholding.

> "Eventually, we agreed that I would be able to increase my shareholding to 20%. I recall that I was on my mobile phone outside my garden. I recall that straight after I got off the phone I told my wife of the conversation."

[30] He attended a meeting in Mr T Karedis' office at Neutral Bay at the end of February 2002 at which the Karedises and Mr Loel, a Brisbane solicitor, were also present. It is desirable, I think, to record precisely what was sworn to by Mr Kelly and relied on as constituting the alleged option agreement or confirmation of it –

> "32 At the meeting, I raised the possibility of bringing a new independent director in as someone who is from outside and impartial, given there were three directors. Theo Karedis immediately disagreed with the proposal. He said that there should just be the three of us as directors. James Loel then spoke at the meeting after Theo's refusal of an independent director and said words to the effect of:
>
> > 'Whilst I am acting for TGM, I am also an old friend of Tim's. He has become a minority shareholder in what is essentially a company that is owned in majority and controlled by a family. If I was advising Tim, then any future board and shareholders' decisions should be unanimous so that Tim and his position will be protected.'
>
> 33 Theo Karedis said that he had no difficulty whatsoever with the concept that it would be necessary for all three to vote as one at shareholders' meetings or meetings of the board of directors. He said that I was now part of the family and that he would treat me the same way he treated Greg Karedis and we all had to agree as a family to move forward. Either Theo Karedis or James Loel asked Greg Karedis if he agreed and he said he did.

> 34 I then raised the issue of the option agreement. I said that we should discuss the funding of the option agreement. Theo said he could not fund it as he was advised by Westpac that it was not possible to do so, however, they would help me in my ability to seek finance from another source."

[31] There was further discussion about ways in which his purchase of the additional 12.3% of shares in HWI and TGM could be financed.

> "(a) Both Theo and Greg Karedis said that TGM and HWI would guarantee repayment of any finance needed by me to purchase the 12.3% of total shares pursuant to the call option;
>
> (b) Both Theo and Greg Karedis said that The Grape would pay the interest by way of dividends to me;
>
> (c) Theo Karedis also said that once I had tried all avenues to raise finance, and if I did not have any success, I was to come back to him;
>
> (d) They said that if I wanted to sell the shares controlled by me then I was to sell them to the Karedis' at a net multiple of seven times net profit and I agreed; and
>
> (e) Theo or Greg Karedis said that the option could not go on forever. Greg Karedis said they were going to have to bear the costs of holding the shares. I said I would pay the costs of holding the shares. My recollection is that it was going to be at Bank interest rates from time to time. Theo and Greg said that was okay. If I wanted to take advantage of the offer, then I would obviously have to bear the costs of doing so. I said that I would pay interest in relation to the holding costs of those shares."

[32] At the end of the meeting, he offered to have the agreement arrived at in relation to the option, the voting requirements and his remuneration package reduced to writing. Mr T Karedis responded in words to the effect that that was not necessary given that the company was a "family company" and Mr Kelly was "part of the family". He said however that he would consider any document prepared by Mr Kelly.

[33] In an affidavit filed in the proceedings on 8 December 2003, Mr Kelly, in relation to the 27 February 2002 meeting, swore –

> "15 …**Unanimity of important decisions** at Board and shareholder level was raised for the first time with the Karedis at this meeting by James Loel, who said:
>
> 'Whilst I am acting for TGM, I am also an old friend of Tim's. He had become a minority shareholder in what is essentially a company that we owned in majority and controlled by family but will also be one director with Theo and Greg Karedis being the other two directors. If I was advising Tim, if the old shareholders deed was to be

> dissolved then any future Board and shareholders decisions should be unanimous so that Tim and his position will be protected.' (emphasis added)
>
> 16 When the topic of my option to acquire up to 20% of the shares was raised, Theo Karedis made it clear to me by saying that 'his word was his bond', that he would honour his agreement to ensure that I had the right to acquire up to 20% of the paid up capital of TGM and HWI at the same price that Pesutu and GTK were to pay the outgoing "A: class shareholders. He said that if I could raise the finance to purchase the shares, TGM would meet the interest costs associated with the loan.
>
> 17 I orally accepted Theo Karedis' offer unequivocally and Greg Karedis said that he also understood and accepted the agreement.
>
> **18 Further, as to the question of unanimity of directors voting on major issues, Theo Karedis spoke to the point very clearly saying that he had no difficulty whatsoever with the concept that it would be necessary for all three to vote as one at shareholders' meetings or meetings of the Board of Directors on important issues such as repayment of loans, issue of further shares, sale of assets or shares and other issues that were specifically raised.** Both he and Greg Karedis in James Loel's and my presence accepted this proposition unequivocally. (emphasis added)
>
> 19 There was also a discussion about the ways in which I could raise the finance needed to purchase the additional 12.3% of shares in HWI and TGM. Both Theo Karedis and Greg Karedis orally agreed that Pesutu and GTK would guarantee any finance from the ANZ Bank needed by me to purchase the 12.3% of total shares pursuant to the call option. Theo Karedis said that Pesutu and GTK would guarantee the loans but that 'The Grape' would pay the interest. Theo Karedis also said that once I had tried all avenues to raise finance, and if I did not have any success, I was to come back to him and he would arrange the finance through his bank, which was Westpac."

[34] In cross-examination Mr Kelly gave this evidence when alerted to differences in the content of paragraph 18 of his first affidavit and paragraphs 32 and 33 of the second affidavit –

> "… when James Loel mentioned about unanimity and those specific things, Theo said that he had no problem with that."

He identified Mr Loel's words as those appearing in paragraph 32 of his second affidavit. He further said –

> "Mr Loel did refer to major issues … all important board decisions … important things at board meetings" (were to be the subject of a unanimous vote) … but agreement at the end was on all board decisions."

[35] He maintained that he said words to the effect "I want unanimity on all board decisions" and that in response Mr T Karedis said "That he doesn't have a problem because that's the way they work as a family". Later, he conceded the possibility that after Mr Loel had spoken the words quoted above, Mr T Karedis had said "I've got no problem with that", that he then said "I want unanimity on all decisions" and that nothing further was said.

[36] In relation to the way in which the acquisition was to be financed, Mr Kelly said, in cross-examination, that –

> "We then discussed various ways or mechanics that we could do that and we agreed that I would go and look for the moneys from banks up in Queensland … we agreed that there'd be dividends to be paid that would – which would be paid in equal – equal to our shareholding – 20% and 80% – and that the 20% would be paid to me and their 80% would be put aside, and that whatever I wanted to do with that dividend was not to fund whatever interests that I needed to pay on the loan. … he also said that if I didn't have any luck with the banks, to come back to him and that he would help me. … we agreed that they would help to provide the funding thereof, but they couldn't do it through Westpac."[1]

"Various options were canvassed at the meeting" and it was agreed that if Mr Kelly wished to sell his shares then the Karedises would pay a price based upon seven times the earnings of The Grape before interest and income tax.

Evidence of James Loel as to the existence of the option and unanimity agreements

[37] In late 2001/early 2002, Mr Loel acted as the solicitor for TGM and HWI. He also acted for Pesutu and GTK in their acquisition from the majority "A" class shareholders of their shares in TGM and HWI. Prior to the Neutral Bay meeting he was informed by Mr Kelly in the course of a number of discussions he had with him between late January and early February 2002 that Mr T Karedis –

> "… had agreed on behalf of Pesutu and GTK to grant him an option to buy 12.3% of the shares in TGM and HWI, and that voting at meetings was to be unanimous."

[38] Exhibited to his principal affidavit is a copy of a handwritten diary note which he swears to have made during such a telephone conversation.. It states –

> "put + call option
> Quorum – 3 hands <u>all unanimous</u>
> <u>Helen + Theo</u>
> Very appreciative of legal advice given"

In cross-examination he said that the diary note recorded Mr Kelly's words, and that despite the use of the words "put + call option" he understood Mr Kelly to be intending to convey that the option was "a straight option to purchase up to 20% of the shareholding".

[39] He explained that the latter part of the note recorded Mr Kelly's recounting that Mr T Karedis had said that he and his wife were appreciative of the legal advice given

---

1 Transcript 104.

by Mr Loel in relation to the dispute with Kitchen. Another undated diary note exhibited to the affidavit is said by Mr Loel to be in respect of a conversation between him and Mr Kelly after the above diary note but before the Neutral Bay meeting. It records –

> "for management agreement – 2-3 measures that increase shareholder wealth
>
> FOR KELLYS CALL OPTION
> _____
>
> ① structures say that its tax effective.
> Somehow gain must be capital?
> ② assignable by TK not Pesutu
> ③ no dilution ie. 12 x % on current equivalent of X shares."

On his instructions an employed solicitor in Frews, the firm in which Mr Loel was then working as a consultant, prepared a draft option agreement which he provided to Mr Loel with a memorandum dated 7 February 2002.

[40] The same solicitor gave Mr Loel another memorandum dated 11 February 2002 dealing with proposed amendments to the constitution of TGM. On it Mr Loel wrote "right of veto. All directors + shareholders unanimous." He swore that the note was made at about the date of the memorandum.

[41] Mr Loel and Mr Kelly flew down to Sydney together for the Neutral Bay meeting which Mr Loel understood had been called to discuss the draft share sale deed and other matters relating to the acquisition of "A" Class shares by Pesutu and GTK. The meeting, which was harmonious, took an hour or less. There was no disagreement on anything and most of it was concerned with Mr Kelly's management package, option to purchase shares and voting rights rather than with the matters for which the meeting had been convened.

[42] In relation to the option, Mr Kelly said that he wanted to formalise it, to which Mr T Karedis responded –

> "Look Tim, my word is my bond, I will honour my agreement to make sure that you have the right to buy up to 20% of the companies at the same price we are paying Kitchen."

[43] He felt awkward about raising the issue of voting rights, but did so by saying words to the effect –

> "I can't be advising anyone but it appears to me that post settlement Tim is going to be in an elephant and flea situation".

Mr T Karedis responded –

> "Look Tim we have been this far together, we have worked together, you are part of the family now and we don't treat family like that."

In response Mr Kelly said words to the effect –

> "I would need resolutions at the directors' and shareholders' meetings to be unanimous."

Mr T Karedis responded in words to the effect –

"I don't have a problem with that."

[44] Consultancy fees were not discussed and he recalls no discussion of funding Mr Kelly's borrowing through dividends. There was discussion about how Mr Kelly was "to pay any interest bill. If Tim couldn't get the ANZ … to fund the purchase he should come back to Theo who would introduce him to Westpac and consider guaranteeing". He does not recall discussion of "what particular decisions needed to be unanimously agreed". At the conclusion of the meeting Mr Kelly said "… you won't mind if I have a written agreement prepared", to which Mr T Karedis responded with words to the effect that –

> "… he did not see this as necessary given that the company was a family company and that Tim was part of the family, but he would consider any document that Tim Kelly got prepared."

[45] I do not set much store by Mr Loel's diary notes. I doubt that he has any real recollection of the circumstances in which they were prepared or of what they purport to record. The diary note containing a reference to unanimity is most unlikely to be a record of instruction that agreement had been reached on that account. Even Mr Kelly agrees that there was no agreement about unanimity before the Neutral Bay meeting.

[46] Whilst I consider that Mr Loel attempted to give an accurate account of matters as he recalled them I do not have confidence in the accuracy of his recollection. I consider also that his recollection is likely to have been distorted by a mindset, unjustified in my view, about the nature of the dealings between the parties. It is of concern that he appears throughout to have seen himself as an adviser to and supporter of Mr Kelly, notwithstanding his fiduciary obligations to his clients, the Karedises and The Grape. That is a factor which contributes to my conclusion that, in this matter, Mr Loel's objectivity is suspect. I consider it probable also that his recollection of words used and topics discussed at the Neutral Bay meeting is sketchy – he does not recall discussion at the meeting about quite significant topics which both Mr Kelly and Mr G Karedis agree were discussed.

The evidence of Mr T Karedis concerning discussions with Mr Kelly in January/February 2002

[47] Mr Karedis had discussions with Mr Kelly, after the report of Calabro Partners was issued, concerning the acquisition by Mr Kelly of additional shares in The Grape but that no agreement was reached. Mr Kelly had told him that he wanted to get rid of Mr Kitchen "and become the boss of The Grape and stay in as a shareholder."

The evidence of Mr T Karedis concerning the Neutral Bay meeting

[48] He cannot recall any discussion about an independent director being appointed but concedes that it is possible that such a discussion took place. He does not recall unanimity of voting at board or shareholder level being discussed. His recollection is that there was such a discussion at a meeting in his unit in Surfers Paradise in January 2002 and that both he and his son had said that the voting should be "two against one".

[49] He would not have agreed to unanimous voting because he would not have accepted having anyone in a position to override or block "decisions that needed to be made to grow the business". "Greg and I were taking most of the equity and debt risks in

The Grape and I wanted to ensure that that risk was not compromised. The experience we had just been through with Mr Kitchen was still fresh in my mind and I did not want a repeat of it."

[50] There was no discussion at the meeting about an option agreement and, about honouring any such agreement. Either at this meeting or in other conversations with Mr Kelly in February 2001 he said that he would agree that Mr Kelly "could move to 20% of The Grape if he could raise the necessary finance and this had to be settled by the same time as settlement of the agreement with the "A" Class shareholders."

[51] He did not say that he would give a personal guarantee of the loan. In previous discussions Mr Kelly had said that he could not afford to pay for the additional shares and had said that he wanted the help of Mr G and Mr T Karedis in that regard. Either at this meeting or at another one close in time to it, there was discussion between Mr G Karedis and Mr Kelly "about The Grape paying interest on any loan obtained by Mr Kelly by way of dividends." He was concerned about such a proposal as he calculated that interest on a loan of $2.6 million would be about $200,000 and his assessment was that The Grape could not afford to pay such dividends. He understood also that there may have been a "bank requirement that dividends not be paid." He concedes that he may have said to Mr Kelly "Tim we don't mind helping you. We want to help you find the finance. If you've got problems come back to me".

[52] Mr Kelly said that if the Karedis family ever sold their business he wanted to sell at the same price. There was discussion about "a seven multiplier" and Mr Kelly stated his acceptance of that. There was discussion that Mr Kelly "had to buy and settle with the "A" Class shareholders." Mr Karedis did not say that it was not necessary to have a written agreement given that the company was a family company and that Mr Kelly was part of the family but he did say "put something in writing and we will look at it."

The evidence of Mr G Karedis concerning discussions with Mr Kelly in January/February 2002 and at the Neutral Bay meeting

[53] In January/February Mr Karedis had discussions with Mr Kelly about the latter's acquisition of the shares in The Grape, the additional percentage which might be acquired and the financing of the acquisition.

[54] At the commencement of the Neutral Bay meeting Mr Loel "said they had no particular agenda … but thought it was important that we look at how we go forward in the future." Mr Loel referred to Mr Kelly's wanting to increase his share in The Grape. There was then discussion about ways in which that might be financed. Mr Karedis suggested that a dividend could be paid to the three shareholders and that the Karedis' interests could leave in their dividends as a loan. Mr T Karedis responded that he did not want to lend the business any more money.

[55] There was then a suggestion by Mr Kelly about payment of a consultancy fee of $200,000. Mr Kelly said he was speaking to the banks at the moment and Mr Karedis said that they were "still speaking to Westpac about them providing a loan to Mr Kelly".

[56] Mr Loel raised the possibility of the appointment of a fourth director and that was rejected by the Karedises. Mr Loel asked what would happen in the event that Mr Kelly purchased 20% of the business and the Karedis' interests wanted to sell it. Mr Kelly said that he wanted to make sure "that The Grape got the same earnings multiple as the NSW business" and Mr Karedis responded that he had no problem with that. Mr Kelly said that if the business was to be sold it should be by unanimous decision. Mr G Karedis did not agree with that proposition and after some discussion said that if the Karedis' interests wanted to sell for less than a price arrived at on a seven PE multiplier they would have to buy Mr Kelly's shares at a 7 PE multiplier.

[57] Mr Kelly asserted that decisions should be unanimous. Mr T Karedis "said that would never work … we have already discussed it in Surfers and if any two of us agree and the other one disagrees, the third has to go with the other two". Mr Loel said that there should be some decisions which should be unanimous and Mr G Karedis agreed that "the budgets at the beginning of each financial year, capital expenditure and shareholder loans could be … we should go away and look at the shareholders' agreement to find some other examples". Mr Karedis, having had the experience of Mr Kitchen asserting that he would block all decisions of the board, did not wish to repeat it having regard to the Karedis interests' increased shareholding and debt exposure.

[58] At the conclusion of the meeting. Mr Kelly said that he would write notes on what was discussed. Mr T Karedis said that would be good and "we would consider it from there". Although there was discussion about the acquisition of shares by Mr Kelly from the "A" Class shareholders, there was no discussion of any option. On a number of occasions, including at the meeting, Mr Karedis heard his father say to Mr Kelly "if you can afford it, you're welcome to increase your stake by buying the shares". There was no discussion of the provision of any guarantee by Mr T Karedis. Mr T Karedis did say that once Mr Kelly tried all avenues to raise finance he was to come back to him and "we would try through Westpac". Mr Kelly said that he would go away and "document the meeting", not that he would "document the agreement". Mr T Karedis said he would consider any document Mr Kelly prepared.

Mr Kelly's evidence concerning the meeting at Coolum on 9 March 2002

[59] Mr Kelly met with the Karedises at the Coolum Hyatt on 9 March 2002 and requested that Pesutu and GTK execute a document entitled "Authority to Agent" which he produced. He informed the Karedises that the document recorded that they were acquiring 12.3% of the issued share capital of TGM and HWI as his agent and that the document would have the effect of avoiding double stamp duty. The Karedises said that they agreed and that "it was pursuant to our agreement on (the) increased shareholding".

[60] After that, Mr T Karedis asked how Mr Kelly was going to raise the necessary finance. Mr Kelly responded that he had commenced discussions with the ANZ and that the ANZ required a shareholders' agreement. Mr Karedis said that he did not consider there was a need for a written shareholders' agreement but he would agree to it if it was absolutely necessary. He said he was prepared to give a personal guarantee for Mr Kelly's loan, that he had never done that before and it would only be given as a last resort.

[61] The Authority to Agent was addressed to GTK and Pesutu by Mrs Kelly, as principal. It authorised the addressees to act as her agent for the purpose of acquiring shares constituting 12.3% of the total issued share capital of TGM at a price of $8.42 per share. It provided an indemnity by the principal against all claims and expenses incurred by the agents acting in accordance with the authority. Clause 4 provided –

> "GTK and Pesutu would execute a transfer of the subject shares in favour of Mr Kelly when required to do so. Mr Kelly agreed to pay all money payable under the contract for the purchase of the 'subject shares' and to indemnify GTK and Pesutu against any claims and expenses they may incur as a result of acting on his behalf under the authority."

Clause 5 provided –

> "All money payable under the contract for the purchase of the Property, including any deposit will be paid by the Principal."

[62] A copy of the document had been sent by email to Mr Kelly by Mr Cahill's solicitor on 8 March. In the email, Mr Cahill advised that the appointment was unconditional and that if the principal could not obtain finance she would nevertheless have a contractual obligation to pay for the shares.

Mr T Karedis' evidence concerning the meeting at Coolum on 9 March 2002

[63] Mr Kelly, when presenting the Authority to Agent document for signature, said that it was an agency agreement, it was very simple and that he did not want to reveal to other shareholders that he was increasing his stake in The Grape. He referred to its stamp duty benefits. Mr Karedis asked how Mr Kelly's financing was coming along, saying "we needed to settle soon". He said that he wanted to help Mr Kelly get his finance and would personally guarantee him so he could speed up and get the loan for settlement. Mr Kelly said he appreciated that. Mr G Karedis said "Theo what are you doing?", to which Mr Karedis responded that it was his money. Mr G Karedis then had a telephone discussion concerning the document over the telephone with a representative of Price Waterhouse Coopers.

Mr G Karedis' evidence concerning the meeting at Coolum on 8 March 2002

[64] Mr Kelly said that he had not been able to obtain approvals for finance as he didn't have any assets that he could borrow against. In response to an inquiry about why he wanted the Authority to Agent signed, Mr Kelly explained that he still had an exposure of Mr Kitchen who wanted to pursue him. He had been told that Mr Kitchen was out to get him and that he didn't want to be seen as one of the buyers. Mr Kelly further said by way of explanation that if the Karedises signed the share sale deed he would have to buy the shares off them and he would then have to pay two lots of stamp duty. Mr Karedis said that "this was all too hard and that he should consider an option.". Mr Kelly responded that he had been a 7% shareholder since he invested and wanted people to know he was a 20% shareholder when they dealt with him.

[65] Mr Karedis said that he did not understand how Mr Kelly could afford to pay the interest and that an option would be preferable. Mr Karedis then spoke to Mr Evans of Price Waterhouse Coopers over the telephone about the matter and gave the telephone to Mr Kelly to speak to Mr Evans. Mr Kelly said that all he had to do

was to get funding by settlement. Mr T Karedis said that "he had not done this before but that he would personally guarantee Mr Kelly." That offer was queried by Mr G Karedis and the document was later signed concerning the Coolum meeting. I do not accept that the Karedises spoke words indicating acceptance by them that the Authority to Agent was pursuant to an agreement in relation to Mr Kelly's increased shareholding. The Karedises and Mr Kelly would have regarded the Authority to Agent instrument as a document designed to implement the shared desire of the parties that Mr Kelly increase his shareholding to 20% when he could afford to do so.

Findings in relation to the Coolum meeting

[66] Mr Kelly pointed out the stamp duty benefits of entering into the agreement. The Karedises had no difficulty with that aspect of the matter. Mr Karedis stated a willingness to stand guarantor for Mr Kelly's obligations as a last resort. That offer was queried by Mr G Karedis but affirmed by Mr T Karedis. Discussion with Mr Evans took place as the Karedises report. As Mr G Karedis asserts, Mr Kelly stated a desire that his participation as purchaser be kept from the other "A" class shareholders.

[67] I am not persuaded, on the balance of probabilities, that any emphasis was placed on speed or timing as Mr T Karedis' evidence suggests.

[68] Nothing was said to suggest that the Authority to Agent would not take effect in accordance with its terms. All three men regarded it as giving rise to contractual obligations.

Credibility generally

[69] None of Mr Kelly, Mr T Karedis and Mr G Karedis kept diary notes of critical conversations and dealings. It is thus not surprising that their recollections were shown to be faulty in some respects.

[70] Of these three witnesses, Mr T Karedis' recollection of the detail of conversations and events was the most limited. That is as one would expect as, in relation to The Grape, he left matters of detail and day to day business affairs to his son and, in appropriate cases, others.

[71] A vigorous attack was made on Mr Kelly's credibility in cross-examination and in addresses. Whilst the attack revealed errors and inconsistencies in Mr Kelly's recollection, I am not persuaded that, as the defendants' counsel urged, Mr Kelly's evidence should be treated as entirely tainted and lacking in credibility. I think it probable that he has a genuine belief in the existence of the agreements for which he contends but as I mention elsewhere, I do not accept that his evidence in relation to critical conversations is completely accurate. I consider also that in relation to the critical aspects of this case he is unable to be entirely objective and recalls matters through the prism of his own self interest.

[72] Mr G Karedis emerged from cross-examination largely unscathed. Whilst I do not consider his recollection to be completely reliable, or his approach entirely objective, I regard his evidence to be more reliable generally than that of Mr Kelly and Mr T Karedis.

Dealings between the parties between 9 March 2002 and 26 March 2002

[73] The evidence does not disclose, in detail, what communications took place between the parties in relation to Mr Kelly's proposed share acquisition between 9 March 2002 and 26 March 2002, the date of settlement under the share sale deed. Mr G Karedis swears that just prior to settlement Mr Kelly telephoned him and informed him that he would be unable to obtain finance in time for settlement. On being asked what he wanted to do now, Mr Kelly said that he would have to buy the shares from Mr G Karedis. Mr G Karedis responded that he had spoken to Westpac and had been told, in effect, that they would not lend money on the security of shares in The Grape but suggested that Mr Kelly speak to the ANZ as they had a first mortgage over The Grape's assets. Mr Kelly denies that this conversation took place.

[74] On 13 March Mr Cahill sent Mr Kelly an email to which was attached an "issues paper" concerning matters "which should be covered in the shareholder's agreement and also in (sic) clarifying status of your existing shareholding". Paragraph 1(c) and (d) stated -

> "(c) It is proposed that Tim will purchase an additional 12.3% shares in The Grape to bring the total Kelly family holding up to 20%. The share price is approximately $2.63 million. **Agreements for this acquisition were signed over the weekend of 9/10 March 2002.**
>
> (d) It is proposed that the purchase price of $2.63 million will be borrowed on an interest only basis (probably from Suncorp Metway). The Grape will guarantee the interest payments and will pay these directly to Suncorp Metway as an expense payment fringe benefit (which should not be subject to FBT – otherwise deductible rule). (Emphasis added)

Mr Cahill's reference to "Agreements for this acquisition" is to the "Authority to Agent" document.

Negotiations and communications in relation to the proposed shareholders' agreement – March to August 2002

[75] On 29 March, Mr Evans of Price Waterhouse Coopers sent his comments on the issues paper to Mr Cahill and Mr Kelly. Those comments were made after a discussion between Mr Kelly and Mr Evans. Neither those comments nor the issues paper itself referred to the existence of an option or to any agreement that voting at directors' and shareholders' meetings be unanimous.

[76] On 15 April 2002, Mr Kelly sent the draft shareholders' agreement to Mr G Karedis by email. The document was 19 pages long. It provided, amongst other things:

(a) that certain decisions by directors were required to be unanimous;
(b) that Mr Kelly was to be employed as general manager;
(c) for pre-emptive rights on the part of the other shareholder where one shareholder wished to dispose of its shares;
(d) for rights and obligations in the event of a purchase of shares in TGM or its business by a third party;

[77] On 19 April, Mr Kelly sent another email to Mr G Karedis in which he said –

> "On that shareholders agreement, Theo wants a simpler easily readable document but what I forgot to tell him was that a lot of the need for this document is driven by the ANZ in requiring this comprehensive document, so that the Credit Department would be satisfied.…."

Mr Kelly, on 29 May 2002, emailed to Mr G Karedis a three page document entitled "Summary of Provisions of Shareholder Agreement for The Grape Management Pty Ltd and related companies." It appears to be a summary of the draft shareholders' agreement referred to earlier or a later version of it.

[78] There seems to have been some discussion about the granting of an option to Mr Kelly to acquire shares as, on 3 June 2002, Mr G Karedis sent an email to Mr Kelly asking if certain advice in relation to the tax implications of a "call option to an employee" could be obtained from Price Waterhouse Coopers. He said he would need to look at the advice "if we are going to make some decisions on the shareholders' agreement this week." Also on that day Mr Kelly sent Mr G Karedis a copy of a memorandum from Price Waterhouse Coopers attaching a draft Executive Service agreement for Mr Kelly and a draft shareholders' agreement. The memorandum considered the possibility of Mr Kelly acquiring an option over shares in TGM in relation to his employment with TGM and alternatively, in relation to his dealings as a shareholder of TGM.

[79] On 4 June 2002, in an email to Mr G Karedis, Mr Kelly said –

> "I thought that a deal had been agreed to between us and that all we had to do was now put into effect a shareholder's agreement.
> The way the agreement is drafted has been considered by PWC to be the most effective way to move forward. It was on that information that I went to ANZ.
> We have an appointment with David at PWC on Friday at 2 pm. Remember that PWC acts for The Grape, not for me. So the advice is for all of us. Would you tell me you are heading with all of this?"

Mr Karedis responded –

> "I believe that we are not necessarily talking about an option but an aspect of the shareholders agreement. We are not talking about a price below the market value but at a price we paid and I thought we were taking into account the holding cost in relation to the price.
> The time aspect of being able to purchase in the future does not reflect buying in 3 years shares below market value at … of the company 3 years ago but will be a reasonable market price then. The difference will be the companys better capacity to pay the dividend. I therefore believe that there will be no CGT aspects to any such purchase and would be happy for David to demonstrate where one would exists if the price paid was arguably the market price then.
> It would be very hard to consider the previous documents sent in that form. If the aspects of those documents evolve from banks needs alternative structures would be needed to be contemplated. Either way I would like David to demonstrate a CGT liability if one existed."

[80] The Karedises sought financial advice from Beerworth & Partners, Corporate Advisers. That firm's email to Mr G Karedis of 7 June discussed the possibility of an option being provided to Mr Kelly to purchase 13% of the shares in TGM by either the Karedises or TGM. An alternative proposal was a bonus issue to Mr Kelly. Under the heading "Problem" the author of the document remarked –

> "The major problem is that Theo and Greg have become involved in Tim's financing process. … In a sense, Tim is being treated as a member of family in that Theo and Greg are trying to pre-estimate when and how he will be able to afford to exercise the option and pay for interest on his loan."

The author observed, in effect, that the draft shareholders' agreement appeared to be unduly favourable to Mr Kelly as a minority shareholder. In the summary to the document it is said –

> "However, the real reason it is difficult to find an easy solution is the unusual circumstance that Theo and Greg are prepared to provide a financing solution for Tim. This converts an arm's length transaction to a semi-family transaction."

[81] At a meeting shortly after 7 June 2002 at Price Waterhouse Coopers, Mr G Karedis asked a representative of that firm if The Grape could guarantee the payment of Mr Kelly's dividend. He was advised that that would be against the directors' fiduciary responsibilities.

[82] A plain English summary of the draft shareholders' agreement was prepared by Mr Loel and provided to Mr G Karedis by Mr Kelly in August, together with a further draft of the shareholders' agreement. It noted –

> "Board decisions are by majority other than certain restricted matters where decisions must be unanimous …"

[83] The draft conferred on Mr Kelly a right to acquire 12.3% of the shares in TGM and HWI for $2,629,696 "at a time nominated by" Mr Kelly. Mr Kelly was to borrow that sum from "a bank or other finance institution", TGM was to pay the interest on the loan and GTK and Pesutu were to guarantee Mr Kelly's obligations to the lender.

[84] Mr Kelly advised Mr G Karedis by email on 23 August that the ANZ Bank, the proposed lender, did not require a guarantee. Further advice was then given by Price Waterhouse Coopers as to how Mr Kelly's proposed acquisition could best be structured from a taxation viewpoint.

[85] The discussions about the proposed shareholders' agreement were overtaken by approaches to the Karedises by Coles and Woolworths to buy the Theo's Liquor Group. On 13 September 2002, at a meeting in the offices of Clayton Utz in Sydney attended by the Karedises, Mr Shaw of Clayton Utz and Messrs Murray and Reberger of CIBC World Markets Securities Australia Limited, Mr Kelly was informed of these developments.

[86] According to Mr Kelly, at that meeting, Mr Murray said "that CIBC knew all about the option agreement for me to move to 20% and that Theo Karedis had determined to honour that agreement and had given them more grief about the details of that option agreement than anything else".

[87] He also said that at one stage, after he and Mr T Karedis had left the meeting to go to the lavatory, Mr Karedis agreed that The Grape would not be sold until there was a final agreement on price between them. Mr Karedis denies that any such conversation took place. The plaintiffs do not assert that this conversation gave rise to a binding agreement.

[88] Mr Murray's version of the conversation at the meeting differs substantially from that of Mr Kelly. It is –

> "Theo has told me that he was agreeable to you moving to 20% of The Grape but that specific terms had not been agreed. Theo does not want you to be disadvantaged by that however and is happy for you to share in the profit as if you had 20% of The Grape.
> I then looked up at Mr Theo Karedis who said words substantially to the effect, 'yes, Tim, I'm happy for you to receive an equivalent to 20% which is what you've always wanted. I think this is a good opportunity for us to sell the business. I think the time is right to sell.' "

[89] Mr Murray denies that he said words to the effect that CIBC knew all about the option agreement and swears that he was not aware of the existence of any such agreement. He also denies using some language attributed to him by Mr Kelly. I do not accept that there was any admission by Mr Murray of the existence of the alleged option agreement. Mr Murray was a witness who was substantially independent and who appeared to be endeavouring to provide an honest recollection of events. I consider that his recollection of events is likely to be more accurate than that of Mr Kelly.

The proposed assets sale

[90] On 27 September 2002, Mr Kelly, Mr G Karedis and Mr Reberger met in Sydney with representatives of Liquorland (a Cole's subsidiary) and its financial adviser in order to discuss a prospective sale of the assets of The Grape. Further discussions took place between Mr Kelly and Mr G Karedis after that meeting concerning Mr Kelly's attitude to the proposed sale. Throughout September there were other communications concerning the value of the assets of The Grape and the sale of its business. Matters discussed included the price payable to Mr Kelly for his interests in the event of a sale, the way in which the assets sale could be best structured for income tax purposes and the impact on the business of the foreshadowed introduction of Woolworths' "Dan Murphy's" business into Queensland.

[91] The due diligence investigation then being undertaken disclosed that The Grape business had "a negative $6 million working capital". This was a concern to the Karedises as it suggested that they had paid too much for their interest in The Grape and that the achievable sale price may be less than had been previously thought. As well as the shortfall in working capital, the investigations disclosed a deterioration in the earnings of the business.

[92] On about 30 September, Mr Kelly sent a memorandum dated 25 September to the Karedises in which he expressed the opinion that the proposed sale of The Grape business was 2-3 years too early.

[93] A memorandum to the Karedises from CIBC dated 19 November 2002 entitled "'Project Spirit' – Tim Kelly briefing memo" records that the purchaser valued The

Grape at $33 million which equated to an equity of $15 million "after debt and negative working capital". It further records –

> "Theo has wanted to give Tim a 20% stake but this doesn't work for Tim at these valuations because equity value is below the last round (Tim would be $630K out of the money). Theo still wants to do the right thing with Tim."

A copy of the memorandum was sent by Mr Kelly to Mr Loel on 8 December 2002.

[94] On Monday, 25 November, Mr Kelly made contact with the Chief Executive Officer of Woolworths and had a brief meeting with him in which he broached the possibility of Woolworths acquiring an interest in The Grape.

[95] Mr Murray prepared a memorandum to the Karedises and Mr Kelly dated 26 November 2002 in which he discussed the value placed on The Grape business by the offer made by Coles and the return Mr Kelly could expect if the offer were to be accepted. Paragraph 4 of the memorandum noted that Mr T Karedis had offered to pay "a sale bonus" to Mr Kelly of $500,000. Mr Kelly's share of the sale price, on that basis, was calculated to be $1.69M.

[96] On 29 November 2002, Mr Kelly and his solicitor met with a senior executive of Woolworths in Brisbane. Subsequent negotiations culminated in the entering into of an agreement between the Kelly interests and Woolworths on 5 December 2002. It recited, erroneously, that the Kelly interests were entitled to acquire the shares of the Karedis' interests and further that Woolworths was interested in acquiring the shares once they had been acquired by the Kelly interests. The existence of the agreement and the negotiations were not disclosed by Mr Kelly to the Karedises until after the commencement of these proceedings.

[97] Mr Murray participated in two further meetings with Mr Kelly and the Karedises, one in a restaurant in Sydney in mid-November 2002 and one in Brisbane on 4 December 2002. In the course of the later meeting Mr Murray discussed with Mr Kelly a document headed "Kelly Shareholding Analysis" in which he had valued Mr Kelly's interest in The Grape at $3.8 million. Mr T Karedis observed to Mr Kelly that the offer was a terrific one which put a value on The Grape considerably in excess of the price payable by Coles.

[98] On 28 November 2002 Mr Kelly sent an email to Mr G Karedis in which he foreshadowed an offer to purchase the Karedis' shares in TGM and HWI.

[99] On 10 December 2002 Pesutu made an offer to the plaintiffs to acquire their shares in HWI and TGM for a total price of $3.8 million.

[100] In a letter of 12 December 2002, Mr Kelly's solicitors asserted that the conduct of Pesutu and GTK had triggered the pre-emptive rights provisions in the constitution of TGM and repeated an offer by the minority shareholders to purchase the majorities' shares in TGM for $14.3 million. Pesutu and GTK, through their solicitors, denied the assertion and rejected the offer.

[101] The Karedis' solicitors forwarded to Mr Kelly's solicitors a letter on 19 December 2002 enclosing a notice for a directors' meeting of TGM to be held on 20 December together with an agenda for that meeting. The agenda included provision for consideration of a proposal by Coles to purchase the business of TGM and for the

directors to consider and discuss any other proposals to purchase the company's business. Enclosed with the letter was a copy of deeds between, inter alia, the Karedises and Liquorland, a Coles subsidiary, dated 16 December 2002 under which, in general terms, the Karedis interests were entitled to exercise an option to require Liquorland to enter into "The Grape Agreement". That agreement contemplated that a new company, TGM Newco Pty Ltd, be formed, that it would acquire the business of The Grape and that Liquorland would acquire its shares. It is unnecessary for present purposes to further analyse the content of the voluminous documentation.

[102] The meeting which the Karedises attempted to convene on 20 December was not held until much later as a result of stalling tactics by Mr Kelly. Something of a stalemate was reached with neither party being prepared to accept an offer from the other. Against that background the Karedises decided that it would be desirable for the business of TGM to be sold. On 30 September 2003 the board resolved to sell the business. Negotiations then took place concerning an appropriate sale process.

[103] Mr G Karedis had made attempts to obtain from Mr Kelly his suggestions for a process in the course of October 2003. Eventually, on 28 October 2003, Mr Kelly sent Mr G Karedis an email in which he made a number of criticisms of the timing of steps in the process put forward by the Karedises. The email asked how it was proposed to accommodate alternative offers for the sale of shares as part of the process and stated –

> "I do need to remind you that I may wish to exercise my option to move to a 20% interest in The Grape by paying you $2.6 million. We can avoid the need for further debate on the existence of this option if you are now prepared to accept that this right exists."

[104] In his email of 30 October 2003 Mr G Karedis observed that "a share sale is not for the board to consider" and that "as I have said to you in the past, you do not have any option to move to a 20% interest in The Grape." That provoked a response from Mr Kelly on 3 November that he would "only move forward on the sale process" if the option was acknowledged.

[105] At Mr Kelly's request, a board meeting to consider the asset sale proposal was adjourned to 10 November 2003. The meeting was attended by representatives of the parties legal advisers as realised by the directors. At it the sale process put forward by the Karedises was adopted by majority vote. The process contemplated –

- offers for the purchase of The Grape business to be lodged with the board and PWC Corporate Finance by 2 December 2003;
- an analysis of the bids by PWC Corporate Finance by 4 December 2003;
- facility for bidders to make revised offers by 9 December 2003;
- provision of an analysis of the revised offers by PWC Corporate Finance on 9 December 2003;
- consideration of final offers by the board on 11 December 2003 and execution of contracts on 11 December.

A minimum price of $33 million was stipulated.

Principles applicable to the determination of the existence of a binding option agreement

[106] The question of whether a binding contract resulted from negotiations between parties is to be determined by reference to the intention of the parties "disclosed by the language the parties have employed".[2]

[107] McHugh JA in *GR Securities v Baulkham Hills Private Hospital Pty Ltd*[3] expressed the question for determination this way –

> "However, the decisive issue is always the intention of the parties which must be objectively ascertained from the terms of the document when read in the light of the surrounding circumstances".

Those observations are in respect of a written agreement but, with appropriate adaptations, they apply equally to oral agreements.

[108] Where, as is the case here, a binding agreement is alleged to have come into existence after oral and/or written communications between the parties over a period of time, the communications alleged to constitute the agreement must be considered in the light of the other exchanges and not in isolation.[4] Also, the question of whether a binding agreement has been concluded is not always capable of resolution by attempting to draw out of oral or written exchanges a discrete offer and acceptance.

[109] In *Integrated Computer Services Pty Ltd v Digital Equipment Corp (Aust) Pty Ltd* [5] McHugh JA, with whose reasons Hope and Mahoney JJA agreed, said –

> "It is often difficult to fit a commercial arrangement into the common lawyers' analysis of a contractual arrangement. Commercial discussions are often too unrefined to fit easily into the slots of 'offer', 'acceptance', 'consideration' and 'intention to create a legal relationship' which are the benchmarks of the contract of classical theory. In classical theory, the typical contract is a bilateral one and consists of an exchange of promises by means of an offer and its acceptance together with an intention to create a binding legal relationship ...
>
> Moreover, in an ongoing relationship, it is not always easy to point to the precise moment when the legal criteria of a contract have been fulfilled. Agreements concerning terms and conditions which might be too uncertain or too illusory to enforce at a particular time in the relationship may by reason of the parties' subsequent conduct become sufficiently specific to give rise to legal rights and duties. In a dynamic commercial relationship new terms will be added or will supersede older terms. It is necessary therefore to look at the whole relationship and not only at what was said and done when the relationship was first formed."

---

2 *Masters v Cameron* (1954) 91 CLR 353 at 362.

3 (1986) 40 NSWLR 631.

4 Cf *Storer v Manchester City Council* [1974] 1 WLR 1403 at 1408 in *Bellamy v Debenham* (1889) 45 Ch D 481.

5 (1988) 5 BPR 97326 at 11,117-11,118.

[110] In *Vroon BV v Foster's Brewing Group*,[6] Ormiston J referred to the following passage from the judgment of Cooke J in *Meates v Attorney-General*[7] with approval –

> "I would not treat difficulties in analysing the dealings into a strict classification of offer and acceptance as necessarily decisive in this field, although any difficulty on that head is a factor telling against a contract. The acid test in the case like the present is whether, viewed as a whole and objectively from the point of view of reasonable persons on both sides, the dealings show a concluded bargain."

[111] After the Neutral Bay meeting, the parties continued to negotiate contractual terms and quite significant ones at that. That regard may be had to these dealings in order to determine whether a contract came into existence at an earlier date is well established.[8]

[112] However, parties to negotiations may, by their words and conduct, make it clear that they do intend to be bound even though there are other terms yet to be agreed,[9] provided of course, that all essential terms of their bargain are agreed.[10]

[113] And the mere fact that negotiations continue after the point at which an agreement is alleged to have come into existence does not lead, necessarily, to the conclusion that no binding agreement was reached.[11]

[114] As Cozens-Hardy MR said in *Perry v Suffields*[12] -

> "Though, when a contract is contained in letters, the whole correspondence should be looked at, yet if once a definite offer has been made and it has been accepted without qualifications, and it appears that the letters of offer and acceptance contained all the terms agreed on between the parties, the complete contract thus arrived at cannot be affected by subsequent negotiation. When once it is shown that there is a complete contract, further negotiations between the parties cannot, without the consent of both, get rid of the contract already arrived at."

[115] But the existence of continuing negotiations, particularly if they concern matters of substance, will tend suggest that no contract was formed.[13]

The alleged option agreement

[116] The option agreement is alleged in paragraph 15 of the statement of claim to have been made "in discussions between Tim Kelly and Theo Karedis during January/February 2002" and to have been confirmed in a meeting at Neutral Bay on

---

6 [1991] 2 VR 32 at 82-3.
7 [1983] NZLR 308 at 337.
8 *Brogden v Metropolitan Railway Co* (1877) 2 App Cas 666, *B Seppelt & Sons Ltd v Commissioner for Main Roads* (1975) 1 BPR 9147 and *Australian Broadcasting Corporation v XIVth Commonwealth Games Ltd* [1988] 18 NSWLR 40 and *Brambles Holdings Limited v Bathurst City Council* [2001] NSWCA 61.
9 *Storer v Manchester City Council* [1974] 1 WLR 1403 at 1408.
10 *Thorby v Goldberg* (1964) 112 CLR 597.
11 Cf *Pagnan S.p.A v Feed Products Ltd* [1987] 2 Ll Rep 601.
12 [1916] 2 Ch 187 at 192.
13 *Bellamy v Debenham* (1890) 45 Ch D 481.

27 February 2002. Words to the following effect were allegedly spoken by Mr T Karedis to Mr Kelly –

> "'Tim is now part of my family' and that they would honour his right to acquire up to 20% of the paid up capital of TGM and HWI at the same price that Pesutu and GTK were paying the outgoing "A" Class shareholders."

It is alleged also that Mr G Karedis said words to the effect that "he understood and accepted the agreement."

Did the alleged option agreement come into existence?

[117] I am unable to accept that the discussions between the parties in relation to the granting of an option were intended to give rise to a legally binding agreement. In my view, the Karedises were indicating to Mr Kelly in their discussions with him prior to the Neutral Bay discussions that when he was in a position to acquire the shares under consideration they would be prepared to sell them to him. No doubt the parties had in mind that the transaction would need to be structured in a way which would best suit the financial interests of the parties and accommodate a determination by the Karedises as to which entity or entities should provide the shares.

[118] At the time of the alleged agreement, the Karedises were not seeking to formalise the arrangements concerning the shares. Not only had the acquisition of the "A" Class shares not held by the plaintiffs not been completed, there was no formal agreement in writing for the sale and purchase of those shares. Additionally, Mr Kelly had not established his ability to borrow the purchase price. Despite that, he was endeavouring to finalise arrangements which would give him an increased equity and a guaranteed management role. He saw the settlement of the sale of the "A" Class shares as a window of opportunity. But, the "Authority to Agent", and not an option agreement, was the instrument selected by him to implement his proposed share acquisition.

[119] It is significant that Mr Cahill made no mention of any option agreement in his email to Mr Kelly on 8 March, in the Authority to Agent or in his "issues paper" of 13 March. Price Waterhouse Coopers' comments on the issues paper did not advert to the existence of any option agreement either. Nor is there mention of an option agreement in the first draft of the shareholders' agreement. It assumes that the Kelly interests will have acquired an additional 12.3% of the shares. The Price Waterhouse Coopers' memorandum of 3 June 2002 addressed to Mr Kelly refers to the possibility of options being acquired on different bases. This document and others show that Mr Kelly was undecided about the most beneficial mechanism to be adopted to bring about his proposed share acquisition.

[120] The detailed documentation, although discussed, was never accepted by either party as being in final form and it is not suggested that it, in whole or in part, ever became embodied in a binding agreement.

[121] It is impermissible in these circumstances to single out from the parties' fluid and reasonably complex dealings those items in respect of which there was a general consensus and conclude that a binding agreement or agreements arose in relation to them. The increase in Mr Kelly's shareholding was viewed by all parties as an

integral part of an arrangement under which Mr Kelly would be the managing director and general guiding force of The Grape. Important aspects of that arrangement remained to be resolved, not least of which were the circumstances in which, and the basis on which, the Karedises could sell the assets of the Grape or require Mr Kelly to sell his shares. The financing of the acquisition and Mr Kelly's management role were other central issues. Until such matters were resolved, the parties were unlikely to have viewed their many discussions as giving rise to contractual obligations. More relevantly, the evidence does not support a finding that it was the intention of the parties objectively ascertained on or before the date of the Neutral Bay meeting, to conclude a binding agreement.

[122] The discussion at the Neutral Bay meeting must be seen in the context just described. It was not even a meeting called with a view to resolving outstanding issues in relation to share acquisitions and voting procedures. In my view, whatever was said by the Karedises in the course of the meeting concerning the proposed acquisition was likely to be representational rather than promissory and for that reason lacking in contractual force.[14]

[123] Nevertheless, discussion on those topics did take place and various possibilities were canvassed. Mr T Karedis said words to the effect that he had no difficulty with Mr Kelly's acquiring a further 12.3% of the shares in The Grape. Mr G Karedis indicated his concurrence.

[124] I do not accept, however, that Mr Kelly's or Mr Loel's recollection of what was said at the meeting in this regard is accurate. In particular, I do not accept that the conversation was as formal or as structured as their evidence suggests. There was discussion about the use of dividends as a means of enabling Mr Kelly to meet interest payments but I do not accept that any consensus was reached in that regard or as to the precise manner in which financial assistance was to be provided by the Karedises, should such assistance be necessary. No unqualified offer of a guarantee was made by Mr T Karedis at this meeting.

The effect of the "Authority to Agent"

[125] If contrary to my conclusion there had been a binding option agreement entered into, it was brought to an end by the entering into of the Authority to Agent instrument. Under it, GTK and Pesutu agreed to acquire 12.3% of the issued share capital of TGM from the majority "A" Class shareholders. It is not suggested that it was not intended to take effect in accordance with its terms.

[126] The Authority to Agent gave rise to an obligation on the part of the Kelly interests to acquire the subject shares, whereas an option agreement would have created a right on the part of the Kelly interests to acquire the shares in the event that the option was exercised. The Authority to Agent is thus inconsistent with any prior option agreement in a way which "goes to the very root of it"[15] and the entering into of the former reveals an intention, objectively ascertained, to rescind the latter.[16]

---

14 Cf *J J Savage & Sons Pty Ltd v Blakeney* (1969-1970) 119 CLR 345.

15 *Tallerman & Co Pty Ltd v Nathan's Merchandise (Victoria) Pty Ltd* (1956-1957) 98 CLR 93 at 113 per Dixon CJ and Fullager J.

16 *Tallerman & Co Pty Ltd v Nathan's Merchandise (Victoria) Pty Ltd* at 144 per Taylor J and *United Dominions Corporation (Jamaica) v Shoucair* [1969] 1 AC 340 at 348-9.

[127] If an option agreement had existed it may also have been possible to view the entering into of the Authority to Agent as the exercise of the option. That appears to accord with Mr Kelly's understanding.[17] No relief was sought in respect of the Authority to Agent, presumably because the evidence discloses that it was abandoned by the parties.

The alleged agreement in relation to voting rights

[128] For the Karedises to have agreed to give Mr Kelly a power of veto over directors' and members' decisions would have been quite remarkable. Nevertheless, there is evidence that they were prepared to accept that some major decisions be arrived at by unanimous vote. As the earlier discussion indicates, I do not accept that this was done as a *quid pro quo* for Mr Kelly's continuing support in relation "A" Class shareholders. The gesture appears to have been motivated by a combination of friendship and the desire to harness the talents of Mr Kelly in the business of The Grape. But did any such indication of willingness to confer on each of Mr Kelly and the Karedises an effective power of veto (in some circumstances at least) amount to a legally binding agreement? In my view the answer is no.

[129] The discussion in relation to voting rights, as with the option agreement, was in the context of the proposed acquisition of the majorities' "A" Class shares and the intended acquisition by Mr Kelly of a further 12.3% of TGM's issued share capital. It was anticipated that, along with the increase in Mr Kelly's shareholding, there would need to be a working out of the details of his management role. The proposed voting rights restriction was one aspect of that. There was no intention that, come what may, Mr Kelly would have a right of veto.

[130] The conduct of the parties after the meeting supports that conclusion. No memorandum or set of instructions prepared after the meeting evidences the existence of an agreement or understanding that decisions be arrived at only as a result of unanimous vote. The draft shareholders' agreements, on the contrary, provide for a majority decision except in specified respects. I regard it as probable that at the Neutral Bay meeting the Karedises indicated a willingness to accept unanimous voting in some respects but that the matter was not pursued to finality. I consider it unlikely, having regard to the way in which the topics of unanimity and increased shareholding came to be broached and to the dealings between the parties before and after the meeting that it was the intention of the parties, objectively ascertained, to conclude a legally binding agreement. My observations in relation to the alleged option agreement are generally applicable to this issue.

[131] If there had been a legally binding agreement in relation to voting rights it would have been implicit that it was subject to the acquisition by Mr Kelly of the 12.3% interest in The Grape. I accept also that no finality was reached by the parties as to the essential terms of any such agreement.

Were the alleged agreements supported by valuable consideration?

[132] I am not satisfied that either of the alleged agreements is supported by valuable consideration.

---

[17] Paragraph 48 of Mr Kelly's affidavit sworn on 17 March 2004.

[133] The plaintiffs allege that the consideration is "the assistance of [Mr] Kelly pleaded in paragraph 14 [of the statement of claim]" namely –

> "(a) by determining, on behalf of CSPC and Margaret Kelly, not to accept the offer of Doogle Pty Ltd; and
>
> (b) maintaining that decision until the signing of the share sale deed on or about 7 March 2002;
>
> (c) by assisting Pesutu and GTK obtaining together 92.3% of the total shareholding in TGM and HWI by entering into, and causing the first and second plaintiffs to enter into, the Share Sale Deed on or about 7 March 2002, and therein consenting to the transfer of the shares of the other "A" class shareholders … and waiving their pre-emptive rights."

[134] The facts do not support the conclusion that these actions by the plaintiffs were performed or offered "in exchange for an act, or the offer of an act … or the offer of a promise …".[18] Nor do the facts establish the existence of any reciprocity in the pleaded matters; that is that the alleged assistance was promised or done in exchange for a promise or promises by the Karedis' interests.[19]

[135] The plaintiffs, in engaging in the conduct under consideration, were merely pursuing their own interests. As appears from earlier discussion, Mr Kelly decided, very soon after hearing of the Doogle offer, to reject it. He considered that the desire of Mr Kitchen and the other shareholders to sell their shares created an opportunity for him to increase his shareholding and to secure the managing directorship. His conduct revealed a perception on his part that his interests were likely to be best served by an alliance with the Karedises against the other shareholders.

[136] The defendants were not aware, and could not reasonably have been aware, that the plaintiffs were engaging in such conduct or offering so to do in exchange for a promise, act or offer of an act by them or any of them.

[137] The defendants argue also that if there was consideration for either of the alleged agreements, it was past consideration. Having regard to my conclusions that there were no binding agreements and that any agreements, had they existed, would not have been supported by valuable consideration, it is unnecessary for me to consider that question.

The plaintiffs' allegations that the 10 November resolutions are in breach of the Karedis' duties as directors and not in the interests of The Grape.

[138] It is alleged that the purported resolutions of the directors of TGM and HWI at the 10 November 2003 meeting are in breach of the duties of the Karedises to act in good faith, in the best interests of the companies and to "avoid a conflict of interests" and "not to improperly use their position to gain an advantage for themselves or for someone else".[20]

[139] The plaintiffs argue that the Karedises, in determining and pursuing the sales process, are following their own personal interests in breach of their fiduciary duties. It is further alleged that they have actually preferred their personal interests

---

18 Cf Sir Owen Dixon, *Jesting Pilate* 29 ALJ at 474.

19 Cf *The Law of Contract by Treitel*, 9th ed at 63, 64, 65.

20 S 102(1)(a) of the *Corporations Act* 2001.

in satisfying their contractual arrangement with Coles to their duties to TGM and HWI. These matters, it is argued, may be inferred from –

(a) the failure of the Karedises to contact Woolworths before 10 November 2003 to gauge its level of interest;

(b) knowledge of the Karedises of clause 5(a) of the Put Option Deed entered into with Liquorland which required them not to seek out interest from another potential purchaser, such as Woolworths;

(c) failure by the Karedises to consider the benefits to the company of a public sale process;

(d) failure by the Karedises to inform Mr Kelly at the board meeting of 10 November 2003 that Coles was interested in a direct purchase of assets;

(e) framing the sales process in such a way as to ensure that, effectively, it limited participation in the process to the Karedis' interests and the Kelly interests;

(f) failure on the part of either Mr G or Mr T Karedis to disclose prior to the cross-examination of Mr G Karedis that they had decided, after becoming aware of the dealings between Mr Kelly and Woolworths, that the sales process was no longer appropriate. In this regard it should be concluded that despite realising that the sales process was indefensible, the Karedises "wished to press ahead nonetheless unless and until challenged about it in the witness box".

[140] Parties other than the Karedis interests and the Kelly interests were said to be excluded from the sales process because –

(a) the timetable is abnormally short and inflexible;

(b) the process makes no allowance for potential purchasers to undertake due diligence;

(c) no party is to be approached or encouraged to participate in the process. In short, the process does not envisage the marketing of the asset to be sold.

The defendants' contentions in relation to allegations of breach of directors' duties.

[141] The following submissions are made on behalf of the defendants. Central to the plaintiffs' case is the proposition that the sale process is flawed because it fails to provide for public advertisement of the proposed sale. The question to be decided is not whether Mr Kelly's proposal, viewed objectively, is preferable to the sales process but whether the decision to adopt the sales process by the Karedises was made *bona fide* and in the best interests of TGM.

[142] The following circumstances make it impossible for lack of *bona fides* to be established –

(a) The fact that the business was for sale was notorious in the liquor industry and its sale was widely publicised;

(b) It was common knowledge that both Coles and Woolworths "were on a push to expand their retail liquor businesses" and, in consequence, were likely to pay more than others for liquor assets;

(c) Mr Kelly admits that Coles and Woolworths were the most likely purchasers of the business. Both companies had examined the business when the Theo's business was on the market and

Woolworths expressed the view that too much had been paid for the New South Wales business;

(d) Woolworths did not approach the Karedises about any intending acquisition. The Karedises did not know of Mr Kelly's dealings with Woolworths and were thus justified in thinking that Woolworths was not interested in acquiring the business. Even Mr Kelly accepted that it was reasonable for the Karedises to assume that Woolworths was not interested in the business;[21]

(e) The possibility that if the business was publicly advertised others might express interest in it was not a significant one. The defendants were only required to put in place a process which they believed to be in the best interests of TGM and they were aware that the offer TGM Newco contemplated making was likely to be a significant one determined by reference to an exceptionally high multiplier of 9.81;

(f) Although on Mr Kelly's own admission (and assertion in his email to an executive of Woolworths on 23 October 2003) The Grape business had been "put to the market in the middle of 2002", there was no evidence that anyone other than Coles and Woolworths was interested in it.

[143] Other matters relied on by the defendants to support a decision against a public sale process are –

(a) The Karedises' concerns over the impact of increased competition on the operation of The Grape, particularly from the opening of Dan Murphy stores in Queensland;

(b) Concern of the Karedises over the consequences of the re-branding of two of The Grape stores from "Theo's Liquor". Those stores contributed significantly to The Grape's turnover and revenue. The Theo's name had become the property of Coles which was intending to use it in connection with some of its own businesses;

(c) The continuing dispute with Mr Kelly, in particular as to unanimity of board decisions; and

(d) The requirement of the ANZ Bank that refinance would be offered to The Grape business only on the provision of directors' guarantees.

It is convenient to defer consideration of these matters until after considering the plaintiffs' application for leave under s 236 of the *Corporations Act*.

Application for leave to bring proceedings on behalf of TGM and HWI – the defendants' contentions.

[144] Section 237(2) of the *Corporations* Act 2001 provides that the court must grant an application by a person under s 236 to bring proceedings on behalf of a company if satisfied that –

"(a) it is probable that the company will not itself bring the proceedings, or properly take responsibility for them, or for the steps in them; and

(b) the applicant is acting in good faith; and

(c) it is in the best interests of the company that the applicant be granted leave …".

---

21 T 167/168.

[145] It is common ground that the requirements of paragraph (a) are satisfied. The defendants contend that the plaintiffs are not acting in good faith and that it is not in the best interests of TGM and HWI that leave be granted. The argument proceeds as follows. In order to act in "good faith" the plaintiffs would need to be acting for the benefit of the company and not for the benefit of themselves. Mr Kelly's purpose is not to maximise the return to TGM and HWI from the sale of the business: it is to maximise his own return. Although, in many circumstances, a shareholder's desire to obtain the highest price for himself will coincide with the desire to ensure that property of the company is sold at the best price reasonably obtainable, that is not so in this case. Mr Kelly intends to obtain a premium for his share in the subject assets and to ensure his continued management of The Grape. Mr Kelly's goal is to extract something more for himself than the other shareholders will receive.

[146] In order to demonstrate that it is in the best interests of TGM and HWI that leave be granted, it must be shown that a public sale process is likely to engender more interest in the business and is therefore likely to result in a greater price being achieved for the business. There is no evidence to support these conclusions. Mr Kelly has had ample opportunity to provide evidence that entities other than Coles and Woolworths may be interested in acquiring the subject business but has failed to do so. His allegations that there are likely to be such persons may therefore be disregarded. As for Woolworths, neither Mr Kelly nor Woolworths have chosen to disclose the extent of the interest of Woolworths in acquiring the business and the inference is open that Mr Kelly and Woolworths are using litigation in order to force the Karedises to recognise the alleged option and unanimity agreements and/or to delay a sale of the business to Coles. There is no apparent reason why Woolworths would not wish to participate in a sale process involving the Karedis interests and Woolworths was opposed to a public sale process.

The section 236 application – the plaintiffs' response.

[147] The plaintiffs' contentions may be summarised as follows. Mr Kelly has sworn to his reasons for commencing these proceedings and his evidence ought be accepted. He swears that the considerations he took into account were –

(a) his belief that there should be an open sale process that allows genuinely interested parties to obtain information about the business and of a kind recommended in a report by Mr Walker of KPMG;

(b) his belief that the Karedises are in a position of conflict of interest and duty;

(c) his belief, based on specified legal advice, that there is a good cause of action. In particular, he has legal advice to the effect that he has "a good argument related to breach of directors' duties" and to the effect "that the prospects of a claim for breach of fiduciary duty were better than even".

[148] The Woolworths' agreement is based upon the ability of the Kelly interests to exercise pre-emptive rights – the ability to exercise those rights has not arisen. Although Mr Kelly attempted to negotiate a further agreement with Woolworths in late 2003, no further agreement was reached.

[149] If Mr Kelly was determined to acquire The Grape business for himself or for Woolworths it is unlikely that he would have wanted "the fair and open process he

contends for in these proceedings". Also the evidence does not establish that Mr Kelly's motive is to prevent or delay a sale.

Mr Kelly's conduct from October 2003

[150] In attempting to demonstrate a lack of good faith on the part of Mr Kelly, much reliance was placed by the defendants on the dealings between Mr Kelly and Woolworths in the weeks leading up to 10 November. It is now proposed to examine those dealings.

[151] On 7 October 2003 one of Mr Kelly's legal advisers sent an email to Woolworths' legal advisers and to Mr Kelly entitled "TGM – draft status/strategy paper". It referred to a conference call between Mr Kelly and senior executives of Woolworths scheduled for later that day. An attachment to it was a document entitled "Sale of business – The Grape Management Pty Ltd (TGM) Preliminary Strategy Paper". It canvassed matters including: Mr Kelly's alleged option to acquire a further 13.3% of the shares in TGM; the provision of funding for action contemplated by Mr Kelly in relation to his increased shareholding; a contemplated oppression action; the prospects of an agreed approach to bidding for The Grape assets; a proposed shareholders' agreement between the Kelly interests and Woolworths; and "an Executive Service Agreement" for Mr Kelly and a payment to him of approximately $5M "at successful completion". The paper did not refer to any public, or publicly advertised, sale process. It did, however, disclose information confidential to TGM relating to dealings between TGM and Coles in respect of the Theo's name.

[152] On 23 October Mr Kelly sent by email to a senior executive of Woolworths a document entitled "Position Statement" which referred to The Grape having been "effectively put to the market by the Karedises in the middle of 2002". It set out a table of projected sales broken down into "retail", "co-operative rebates" and "pubs" categories and listed comparable figures for the preceding two years. Under the heading "Moving Forward" it stated -

> "Whilst one can debate the merits of launching a case against Karedis's for oppression of the minority shareholders etc, this course of action could be longwinded and will have huge negative ramifications for the business of the Grape and is personally very draining."

[153] It went on to comment "I think we could win the tender on a price of $37-$40m".

> "…This sale is such a good fit that Woolworths do not want to miss this opportunity.
>
> The price will be considered cheap when The Grape can move ahead unimpeded by Board disputes and with the full dynamics of the Woolworths retailing excellence."

[154] On 24 October, Mr Kelly, in an email to Mr G Karedis, informed him that he had instructed an employee or employees of TGM not to divulge certain price sensitive information to the Karedises having regard to the sale agreement with Coles and the Karedis' consequent position of conflict. On 25 October 2003, Mr G Karedis, in an email to Mr Kelly, pursued him concerning agreement on a sale process. The matter was followed up in an email on 25 October.

[155] Mr Kelly sent a lengthy email to Mr G Karedis of 28 October 2003, purportedly seeking information on the proposed sale process to enable him to seek advice. It does not advocate that the sale be advertised publicly. Mr Karedis gave a detailed response to that email in an email of 30 October.

[156] In an email of 31 October 2003 from a representative of Mr Kelly's solicitors to representatives of Woolworths the author stated –

> "Email from Tim Kelly to Greg Karedis follows for your comments. This email is actually what is consistent with the strategy of what Tom[22] and Tim canvassed in their meeting on Thursday. The essence of the strategy and this email is to get the Karedis' agreement to Tim's entitlement to go to 20% and to see if we can get them to agree on unanimity and a completely fair and transparent process. Whisky[23] indicated it would participate in the sale process with Tim if satisfied about the terms of the process. This email is designed to test the Karedis' out on these issues and then we can re-group and take stock of the way forward when we have their response. Whisky undertook to Tim to work on the rules of engagement that it would regard as fair and transparent in the sale process and to try to provide them today. …Tim has successfully taken a bit of the heat off the immediate prospect or likelihood of the Karedis selling the assets of The Grape out from underneath him by asserting notice of the proposed Board Meeting for yesterday was inadequate and by explaining to Greg Karedis that Tim would participate in a sale process if, and only if, he could be satisfied that the process would be completely fair and transparent."

[157] No reference is made in the email to any publicly advertised sales process. The copy email transmitted with the email is one sent by Mr Kelly to Mr G Karedis making detailed comment on the latter's email to Mr Kelly of 30 October. In it Mr Kelly asserted that acceptance of his right to acquire 12.3% of the shares was a prerequisite to any agreement in respect of the sale process.

[158] That requirement was re-stated by Mr Kelly in emails to Mr G Karedis of 3 and 4 November 2003. Confirmation of unanimity was also raised in an email of 4 November as a pre-condition of any agreement in respect of the proposed sale.

[159] On 31 October 2003, the solicitors for Woolworths, in an email to the solicitors for Mr Kelly, advised that Woolworths had agreed "that Tim Kelly will proceed along the litigation route which we discussed the other day". The email stated –

> "I have also been asked to advise you to require your client to commence proceedings by no later than next Monday in order to prevent the Karedis interests from endeavouring to push through an asset sale at short notice."

Mr Kelly swears that neither he nor his solicitors responded to the email.

[160] Mr Kelly, on 11 November 2003, in an email to Mr G Karedis asserted –

> "I am not satisfied that your sale process is designed to deliver a sale which is in the best interests of The Grape and its shareholders. I am

---

22 Mr Pocket, a senior executive of Woolworths.

23 A reference to Woolworths.

> firmly of the view that we as directors of The Grape would be failing to act in the best interests of The Grape and its shareholders by not conducting a proper marketing campaign for the sale of the business. … Further, I will also do what is required to have my option to move to 20% honoured and the position on unanimity of decision making clarified once and for all."

[161] An email of 1 December 2003 from a representative of Mr Kelly's solicitors to a representative of Woolworths transmitted a copy of a communication received from the defendants' solicitors and went on to discuss "litigation strategy". The author expressed the view that the agreement between the Kelly interests and Woolworths "has little relevance to the current set of circumstances" and suggested that a new agreement be entered into "as a priority to reflect the present situation and the joint objectives of the parties".

[162] These proceedings were commenced on 8 December 2003.

[163] In his affidavit sworn on 17 March 2004, Mr Kelly admits the existence of communications with Woolworths and Woolworths' solicitors relating to the commencement of these proceedings, that Woolworths has met part of the plaintiffs' legal costs associated with the proceedings and has provided a bank guarantee for $10,000,000 in support of the plaintiffs' undertaking as to damages.

[164] In cross-examination, Mr Kelly admitted that he had "sought to negotiate various agreements with Woolworths for … going forwards" but had "failed to have signed up a deal". No representative of Woolworths gave evidence and Mr Kelly did not reveal the precise detail or status of the arrangements on foot between himself and Woolworths. There is, however, no reason to suppose that Woolworths are no longer continuing to meet a substantial portion of the plaintiffs' legal costs incurred in the proceedings. Nor is it probable that communications between Woolworths and the plaintiffs and their respective legal representatives concerning the conduct of the proceedings and the fate of the business of The Grape have ceased.

[165] **Good faith – applicable principles**

[166] The plaintiffs' submissions relied heavily on the following passages from the reasons of Palmer J in *Swansson v R A Pratt Properties Pty Ltd*–[24]

> "**[36]** Nevertheless, in my opinion, there are at least two interrelated factors to which the courts will always have regard in determining whether the good faith requirement of s 237(2)(b) is satisfied. The first is whether the applicant honestly believes that a good cause of action exists and has a reasonable prospect of success. …The second factor is whether the applicant is seeking to bring the derivative suit for such a collateral purpose as would amount to an abuse of process.
>
> **[37]** These two factors will, in most but not all, cases entirely overlap: if the court is not satisfied that the applicant actually holds the requisite belief, that fact alone would be sufficient to lead to the conclusion that the application must be made for a collateral purpose, so as to be an abuse of process. The applicant may, however, believe that the company has a good cause of action with a reasonable

[24] (2002) 42 ACSR 313.

> prospect of success but nevertheless may be intent on bringing the derivative action, not to prosecute it to a conclusion, but to use it as a means for obtaining some advantage for which the action is not designed or for some collateral advantage beyond what the law offers. If that is shown, the application and the derivative suit itself would be an abuse of the court's process: *Williams v Spautz* (1992) 174 CLR 509 at 526; 107 ALR 635 at 648. The applicant would fail the requirement of s 237(2)(b).
>
> **[38]** Where the application is made by a current shareholder of a company who has more than a token shareholding and the derivative action seeks recovery of property so that the value of the applicant's shares would be increased, good faith will be relatively easy for the applicant to demonstrate to the court's satisfaction. So also where the applicant is a current director or officer: it will generally be easy to show that such an applicant has a legitimate interest in the welfare and good management of the company itself, warranting action to recover property or to ensure that the majority of the shareholders or of the board do not act unlawfully to the detriment of the company as a whole."

[167] It was submitted, by reference to *Williams v Spautz*[25] that it may be impossible to establish abuse of process by a plaintiff who, although having an ulterior purpose in view as a desired by-product of litigation, has a genuine cause of action which he would wish to pursue in any event. The plaintiffs, it is submitted, intend to prosecute the action to a conclusion and I accept that the evidence suggests that this is so. I also accept that the plaintiffs have a belief in the existence of a good cause of action with reasonable prospects of success.

[168] I do not accept, however, that for the purposes of s 237(2), absence of "good faith" can be shown only where the applicant does not intend to prosecute the proposed action to a conclusion. Nor does it seem to me that *Swansson* is authority for any such proposition. In the course of his reasons in *Swansson*, Palmer J said – [26]

> "Further, if an applicant for leave under s 237 seeks by the derivative action to receive a benefit which, in good conscience, he or she should not receive, then the application will not be made in good faith even though the company itself stands to benefit if the derivative action is successful."

[169] "Good faith", or *bona fides*, is a concept long known to company law.

[170] In *Mills v Mills*,[27] Dixon J observed –

> "Directors of a company are fiduciary agents, and a power conferred upon them cannot be exercised in order to obtain some private advantage or for any purpose foreign to the power. It is only one application of the general doctrine expressed by Lord *Northington* in *Aleyn v. Belchier* [1758) 1 Eden 132, at p. 138; 28 E.R. 634, at p. 637.]: 'No point is better established than that, a person having a power, must execute it bona fide for the end designed, otherwise it is corrupt and void.'"

---

25 (1992) 174 CLR 509 at 526.

26 At 321.

27 (1937-1938) 60 CLR 150 at 185.

[171] In *Ngurli Ltd v McCann*[28], Williams ACJ, Fullagar and Kitto JJ referred to the above passage from *Mills v Mills* with approval.[29] Earlier,[30] their Honours had said –

> "Voting powers conferred on shareholders and powers conferred on directors by the articles of association of companies must be used bona fide for the benefit of the company as a whole. In *Greenhalgh v. Arderne Cinemas Ltd.* (1951) Ch 286, Evershed M.R., in a case relating to a special resolution altering the articles of association, said: 'In the first place, I think it is now plain that **"bona fide for the benefit of the company as a whole" means not two things but one thing. It means that the shareholder must proceed upon what, in his honest opinion, is for the benefit of the company as a whole'.**" (emphasis supplied)

[172] This passage occurs in a paragraph which commences –

> "But the powers conferred on shareholders in general meeting and on directors by the articles of association of companies can be exceeded although there is a literal compliance with their terms. **These powers must not be used for an ulterior purpose."** (emphasis supplied)

[173] In *Harlowe's Nominees Pty Ltd v Woodside (Lakes Entrance) Oil Co NL*,[31] in dealing with the validity of a resolution by directors to issue shares in the capital of the company, Barwick CJ, McTiernan and Kitto JJ said –

> "An inquiry as to whether additional capital was presently required is often most relevant to the ultimate question upon which the validity or invalidity of the issue depends ; but that ultimate question must always be whether in truth the issue was made honestly in the interests of the company : *Richard Brady Franks Ltd. v. Price* (1937) 58 CLR 112, at p 142 ; *Mills v. Mills* (1938) 60 CLR 15 at pp 163, 169 ; *Ngurli Ltd. v. McCann* (1953) 90 CLR 425, at pp 438-441. … But if, in making the allotment, the directors had an actual purpose of thereby creating an advantage for themselves otherwise than as members of the general body of shareholders, as for instance by buttressing their directorships against an apprehended attack from such as Harlowe, the allotment would plainly be voidable as an abuse of the fiduciary power, unless Burmah had no notice of the facts."

[174] The above passage from *Harlowe's Nominees* was referred to with approval in *Howard Smith Ltd v Ampol Petroleum Ltd*,[32] in which their Lordships quoted with approval the following passage from *Hindle v John Cotton Ltd*[33]-

> "Where the question is one of abuse of powers, the state of mind of those who acted, and the motive on which they acted, are all important, and you may go into the question of what their intention was, collecting from the surrounding circumstances all the materials which genuinely throw light upon that question of the state of mind of the directors so as to show whether they were honestly acting in

---

28 (1953) 90 CLR 425.
29 At 440.
30 At 438.
31 (1967-1968) 121 CLR 483 at 493.
32 [1974] AC 821 at 836.
33 (1919) 56 Sc.L.R. 625, 630-631 per Viscount Finlay.

> discharge of their powers in the interests of the company or were acting from some bye-motive, possibly of personal advantage, or for any other reason."

[175] In the context of the exercise of fiduciary powers, as the above discussion reveals, the requirement that a director act "bona fide" imports the obligation to act honestly and for no ulterior purpose. The concept of good faith is inextricably linked with these obligations and the obligation to act in the interests of the company.

[176] Relevantly, the purpose of s 237 is to permit a person within a described class to bring proceedings in the name of a company where it is probable that the directors of the company will fail to do so. In applying to the court for leave to bring proceedings, an applicant, in a sense, is assuming a role of the company's directors. It would thus surprising if the expression "good faith" in s 237(2)(a) did not have the meaning long attributed to it in relation to determinations or conduct by directors.

[177] That meaning, in any event, is consistent with the normal meaning of "good faith" in the context of the exercise of a right or power required to be exercised in "good faith". In *Central Estates (Belgravia) Ltd v Woolgar*,[34] the Court of Appeal considered a statutory provision which prevented a landlord from bringing proceedings to enforce any right of re-entry or forfeiture terminating the tenancy without leave of the court, where the tenant has made a claim to acquire the freehold or an extended lease, unless the court is satisfied that the claim was not made in good faith. In the course of his reasons Denning MR said –

> "To my mind under this Act a claim is made 'in good faith' when it is made honestly and with no ulterior motive. It must be made by the tenant honestly in the belief that he has a lawful right to acquire the freehold or an extended lease, and it must be made without any ulterior motive, such as to avoid the just consequences of his own misdeeds or failures."

Conclusions on the question of "good faith".

[178] The plaintiffs have the onus of proving that they are acting in good faith. They have failed to satisfy the onus. I consider it probable that in pursuing the litigation the plaintiffs are seeking advantages for themselves "otherwise than as members of the general body of shareholders".

[179] In the absence of full disclosure by the plaintiffs (which I consider not to have occurred), such advantages are unable to be identified precisely but one such likely advantage is the receipt of more money than the plaintiffs would otherwise stand to receive by virtue of their percentage shareholdings. Another advantage is the use of the financial power of Woolworths to assist in pursuing the claims in respect of the option and voting rights. Also it is probable that the plaintiffs have a purpose of preferring the interest of Woolworths in any procedure for the sale of the assets of The Grape.

[180] I infer also that another purpose of the plaintiffs in bringing and pursuing the litigation under consideration is to assist in securing for Mr Kelly a continued role in The Grape. The "preliminary strategy paper" transmitted on 7 October 2003

---

[34] *Central Estates (Belgravia) Ltd v Woolgar* [1971] 3 All ER 647 at 649.

reveals that one of Mr Kelly's objectives at that time was to obtain "an Executive Service Agreement". There is no reason to suppose that Mr Kelly is no longer seeking to obtain that or a similar objective.

[181] Mr Kelly is in a position in which his personal interests conflict with his duties as a director of The Grape. It may be that this conflict of interests, in itself, would make it difficult for Mr Kelly to establish "good faith". In view of the findings just made, however, it is unnecessary to investigate this question.

[182] Having regard to the foregoing, it is also unnecessary for me to express a concluded view on whether it would be in the best interests of TGM and HWI that the plaintiffs have leave under s 236. "Best interests" in the context of this case would appear to relate only to obtaining the best price for the assets of The Grape. Different views no doubt exist as to how this objective ought be attained. Mr Kelly maintained in these proceedings that the directors were under an obligation to market the assets publicly in order to discharge their duty. He also criticised the Karedises for failing to approach Woolworths to ascertain their possible interest. The latter criticism is hypocritical in the extreme but that, of itself, does not show that it is unjustified. It is unjustified because, until they learnt of Mr Kelly's dealings with Woolworths, the Karedises were entitled, for the reasons they advanced, to believe that Woolworths was not interested in reviving its interests in acquiring The Grape.

[183] The criticisms based on lack of marketing are also difficult for the plaintiffs to sustain. Mr Kelly has an intimate knowledge of the industry but never put forward public process (at least in any genuine way) in discussions with his fellow directors. Nor did he approach any of the liquor chains identified by him as prospective purchasers in order to ascertain whether they might be interested. Of course, his interest, after his agreement with Woolworths, lay in assisting it, not in canvassing the possibility of other bidders. I am unable to find that Mr Kelly now has a genuine desire that The Grape offer its assets for sale by some "open sale process". That finding is relevant also to the existence of "good faith" on the part of the plaintiffs.

[184] Since the action was commenced the Karedises have become aware of Woolworth's interest in The Grape and the timings contemplated in the sales process resolved upon on 10 November have ceased to have relevance. Plainly, as Mr G Karedis acknowledged in his evidence, the board will need to give fresh consideration to any proposed asset sale. The merits of the majority directors' conduct on 10 November have thus ceased to be of fundamental importance. That is another reason why it is unnecessary to express a concluded view on this aspect of the case.

Conclusion

[185] For the above reasons, the defendants are entitled to judgment in the action with costs, including reserved costs to be assessed on the standard basis.