

\$160m Suit Filed Against Investment Group, Ernst & Young

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The liquidator to the failed **investment group** Babcock & Brown has filed a \$160 million suit in damages against the company over allegations that it allowed a breach of capital reduction contravention provisions of the Corporations Act. The said breach allegedly started in 2005 until 2008, committed by the directors of Babcock & Brown Ltd, according to an application filed with the Federal Court last week by Deloitte liquidator David Lombe.

The directors allegedly breached BBL's own constitution by allowing multimillion-dollar dividends that were \$160 million shy of the *investment group's* profits. The suit added that they have reduced the share capital of the company.

The defendants in the action include former chairman Jim Babcock, former managing director and CEO Phil Green, former deputy chair Elizabeth Ann Nosworthy, and former directors Geoffrey Martin, Dieter Rampl, Joe Roby, Martin Rey, James Fantaci, Michael Sharpe, and the auditors from Ernst & Young.

Having been one of the leading investment stocks since 2000 up to 2009, Babcock & Brown was then worth \$10 billion. However, the global financial crisis in 2008 aggravated the group's complex ownership structure aided by its huge debt burden. In 2009, it went into liquidation.

Deloitte, liquidator to the investment group, has since started an investigation into the company's failure and the loss of shareholder value. The liquidators conducted last year the public examinations in the Federal Court of the group's former executives and auditors.

The lawsuit filed last week alleged that the directors of the investment group failed to consider the interests of the company apart from the interests of other companies in BBL's group, when it adopted the dividend proposal. Based on court papers, payment of dividends for the previous financial year were to be paid from revenue due to be received in the coming financial year from Babcock & Brown International Pty Ltd (BBIPL).

"The corporate structure and financial arrangements entered into by BBL and BBIPL required the directors to pay particular attention to ensuring BBL did not pay dividends out of profits or reduce its share capital without authorisation, given that BBL owed substantial obligations to holders of Babcock & Brown subordinated notes and the rights of those holders was subordinated to the rights of the bank financiers of BBIPL," court documents stated.

The directors allegedly failed to exercise reasonable skill, care and diligence in authorizing the dividend payments, thus a breach in duty.

In 2005, the directors authorized dividends of \$32.9 million, notwithstanding that the investment group only retained \$5.5 million in earnings.

In 2006, \$56.3 million in dividends was paid vis-a-vis the retained earnings of \$10.6 million, and for the year 2007 nearly \$97 million was paid in dividends vis-a-vis the retained earnings of \$11.95 million.

The application further claimed that had the auditors reviewed the proposed dividend memorandums "with reasonably care," BBL's retained earnings would have been deemed insufficient to pay the dividends, thereby reducing the share capital of the company.

It failed to report the violation to BBL's board or management and to ASIC, and should not have expressed an opinion the financial reports were in accordance with the act. "Had Ernst & Young reported the contraventions or apprehended contraventions to BBL's management or board or to ASIC, BBL would not have paid dividends otherwise than from profits and thus would not have suffered the \$160 million losses," court documents said