Steve Vizard, Insider Trading and Directors' Duties

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Background

The debate concerning Steve Vizard and his share trades has been unprecedented. While we have seen much media attention in recent years focused upon major corporate collapses, it is rare to see so much attention focused upon the actions of one individual in relation to 3 share trades. However, the facts are highly unusual.

On 4 July 2005, the Australian Securities and Investments Commission (ASIC) announced that it had commenced civil penalty proceedings in the Federal Court against Steve Vizard. ASIC alleged that Vizard breached his duty as a director of Telstra Corporation Ltd by improperly using information given to him as a director of Telstra to gain an advantage for either himself and/or others. ASIC alleged that between March and July 2000, Vizard used confidential Telstra information when he traded in the shares of 3 listed public companies, Sausage Software Ltd, Computershare Ltd and Keycorp Ltd.

In its media release, ASIC stated that it was seeking the following orders from the court:

- declarations that Vizard contravened the former Corporations Law on 3 separate occasions by improperly using Telstra information to gain an advantage for himself and/or others;
- pecuniary penalties in such amount as the court considers appropriate for each contravention; and
- a disqualification order prohibiting Vizard from being involved in the management of companies for such period as the court considers appropriate.

Interestingly, it was also stated in the 4 July media release that ASIC had filed a Statement of Agreed Facts with the Federal Court in which Vizard agreed with the facts that gave rise to the allegations and that Vizard also agreed with ASIC that it was appropriate for the court to declare that he contravened his duty to Telstra in using the Telstra information, and for the court to make orders imposing pecuniary penalties and a disqualification order.

ASIC stated in its media release that as the matter was currently before the court, it would be making no further comment.

A furore quickly erupted. The media release contained facts which could be read as indicating Vizard had engaged in insider trading. Yet he had only been charged with civil breaches of his duties as a director of Telstra. In the following days, many allegations were made. These included that Vizard was being treated more leniently than others because of his political connections, that ASIC had done a deal with Vizard, and that generally ASIC was not pursuing vigorously enough criminal enforcement of our corporate laws.

Adding fuel to the fire was the fact that Vizard was on vacation in France when the furore erupted because he knew the date ASIC would be filing the proceedings against him in court and issuing its media release. But what he did do is have his public relations people contact journalists the day the ASIC media released was published to let them know his side of the story.

The intense media debate that erupted following the publication of the 4 July media release included front page newspaper articles, lead stories on TV and radio, editorials in major newspapers, comments from politicians calling for explanations from ASIC and extensive discussion on talk back radio programs.

Subsequently, ASIC did release additional information in response to the sustained pressure, including critical information about the lack of evidence to sustain a criminal prosecution.

Another reason why there was so much debate was of course the prominence of the defendant. Vizard was well known across the country. In the early 1990's, he was the host of the Tonight Live show. He had also been President of the National Gallery of Victoria, Chairman of the Victorian Major Events Company, member of the Melbourne Cricket Club Committee and he had also been awarded an Order of Australia and named Australian Father of the Year.

The Share Trades

The background to the controversial share trades was the incorporation of Creative Technology Investments Pty Ltd (CTI) on 10 December 1999. The sole director, shareholder and company secretary of CTI was Gregory Lay. Lay and his firm provided accounting services to Vizard.

A loan agreement between Brigham Pty Ltd (a company controlled by Vizard) and CTI provided for:

- Brigham to advance funds to CTI for share purchases; and
- profits from CTI's share trading to be split 90% to Brigham and 10% to CTI.

In December 1999, $1 million was provided by Vizard to Brigham and then to CTI.

There were 3 share trades which were the subject of ASIC's Federal Court proceedings against Vizard.

(1) Sausage Software Ltd

In 1999 Telstra acquired 10% of Sausage Software (SS) and 25% of Solution 6 Holdings (S6). In February and March 2000, SS, S6 and Telstra discussed a proposal:
- for SS and S6 to merge;
- for S6 to acquire Telstra's eBusiness platform; and
- for Telstra to control 40% of the merged entity.

Information about these negotiations was sent to Telstra directors. On 7 March 2000, Vizard instructed Lay to have CTI acquire about $500,000 SS shares. This was done

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CTI bought SS shares at an average price of $5.76. On announcement of the merger, SS shares rose to $7.40. On 27-28 March 2000 Vizard instructed Lay to have CTI sell some of its SS shares.

Between 30 March 2000 and 17 April 2000, the ASX Miscellaneous Industrials Index (which comprised 22 entities including SS and S6) fell from a high of 3092 on 30 March 2000 to a low of 2069 on 17 April 2000, a fall of 33%.

The price of SS fell from $6.65 on 30 March 2000 to $1.70 on 17 April 2000 – a fall of 74%. Because of the technology crash, CTI lost $150,720 on its SS share trades.

(2) Computershare Ltd

During 1999 Telstra acquired 15% of Computershare Ltd (CP) – which Vizard knew. On 6 January 2000, Vizard instructed Lay to have CTI acquire $100,000 CP shares.

During March 2000, Telstra directors were notified of a proposal for Telstra to sell its CP shares. During March 2000, Vizard instructed Lay to have CTI sell its CP shares and CTI made a net profit of $2,592.

On 13 July 2000, Telstra announced it was selling two-thirds of its CP shares. The price of CP shares fell from $8.17 on 12 July 2000 to $7.50 on 13 July 2000.

(3) Keycorp Ltd

In June and July 2000, Telstra directors discussed Telstra acquiring 51% of Keycorp Ltd (KC). On 13 July 2000, Vizard, in his capacity as a director of Telstra, signed a circular resolution approving the acquisition and faxed it to the company secretary of Telstra.

On 14 July 2000, Vizard instructed Lay to have CTI acquire $250,000 of KC shares. On 21 July 2000, Telstra and KC announced that Telstra had agreed to subscribe for 51% of KC shares for $515 million. On 20 July 2000 the KC share price was $12.80. On 21 July 2000, following the announcement, the KC share price rose to $15.79.

On 26 or 27 July 2000 Vizard instructed Lay to have CTI sell some KC shares. The CTI profit was $38,364. CTI still has 15,937 KC shares worth only $1.68.

ASIC's Civil Action Against Vizard

ASIC's civil action against Vizard was under s183(1) of the Corporations Act. This section provides that a person who obtains information because they are, or have been, a director or other officer or employee of a corporation must not improperly use the information to:

- gain an advantage for themselves or someone else; or
- cause detriment to the corporation.

ASIC's claim against Vizard was that he breached his duty as a director of Telstra by improperly using information given to him as a director of Telstra to gain an advantage for either himself and/or others. ASIC alleged three separate breaches of s183(1) based on the share trading in the three companies.

The possible penalties for a breach of s183(1) in this particular case were:
- pecuniary penalties of up to $200,000 for each breach; and/or
- a management banning order for such period as the court determines.

There was intense debate about whether these penalties would be appropriate for someone in Vizard's position. It was noted by many commentators that the maximum financial penalty ($600,000) would be likely to have only a minor effect on someone of his wealth. It was also observed that a ban on managing companies would leave Vizard free to conduct substantial business operations through a variety of non-corporate entities such as partnerships and trusts. He could even conduct business and investment through companies, provided he did not manage those companies.

Why Wasn't Vizard Prosecuted?

There were two possible criminal prosecutions that would have been considered by ASIC and the Commonwealth Director of Public Prosecutions (DPP). The first of these was criminal prosecution for breach of insider trading laws. The insider trading laws were changed in 2001- after the 3 share trades – to allow civil proceedings for breach of the insider trading laws. The second possible criminal prosecution was for improper use of information pursuant to s184(3). A key difference between criminal and civil prosecution for improperly using information is whether the information is used dishonestly. If so, then a criminal prosecution may be available.

Because of the intense media and public pressure on ASIC and the DPP to explain their decision making in relation to the Vizard matter, on 28 July 2005, the DPP issued a media release. It is stated in the media release that there was insufficient evidence to bring criminal proceedings against Vizard for insider trading. The key matter was that Gregory Lay declined to provide a signed statement of his ASIC interviews attesting to the truth of the statements he gave in these interviews. According to the media release: "Evidence from this witness was critical for a criminal prosecution as it would connect Mr Vizard with CTI and the trades and the timing of the trades".

The Federal Court Judgment

On 28 July Finklestein J delivered his judgment in relation to the penalties to be imposed on Vizard. Because Vizard had agreed that it was appropriate for the court to declare that he had breached his duties and that penalties should be imposed, the only issue for the court was the penalties to be imposed.

ASIC submitted that the appropriate penalties to be imposed on Vizard were $130,000 for each breach of his duty as a director (a total of $390,000) and a 5 year disqualification order prohibiting Vizard from being involved in the management of companies.

In his judgment, Finklestein J identified four key sentencing principles - general deterrence, personal deterrence, rehabilitation and retribution. In this case, the Judge observed that personal deterrence and rehabilitation were not relevant.

The Judge also observed that "good character" should play only a minor role in sentencing for most white collar corporate crime. In relation to the public humiliation which Vizard had suffered since the ASIC media release, the court observed that "shaming" – which Vizard had suffered - is not a substitute for court imposed punishment.

However, the court stated that where a defendant acknowledges wrongdoing and cooperates, this usually results in a reduction in penalty.

The Judge was very critical of Vizard's actions. He stated that they were "both dishonest and a gross breach of trust" and that he "well knew that what he was doing was wrong". Vizard's "breach of trust was carefully concealed and only discovered by chance", "everything was done for personal gain" and it was "only because of the vagaries of the marketplace that the defendant did not realise his gain".

In relation to penalties, the Judge agreed with ASIC's submission to impose a pecuniary penalty of $130,000 for each breach of director's duty (a total of $390,000) but the Judge doubled ASIC's recommended penalty of a 5 year banning order and instead imposed a banning order of 10 years.

The Lessons

There are a number of lessons that arise from the Vizard matter. Very importantly, there are lessons for ASIC. There is no doubt that ASIC's reputation has suffered damage as a result of wide ranging and extensive criticism of its actions.

ASIC made two errors. First, its media release of 4 July 2005 was deficient in relation to the information that it did not disclose. First, there was no mention of the important role of the DPP. The DPP made an independent evaluation of the results of ASIC's investigation of Vizard's share trades and formed the view that there was insufficient evidence to bring a criminal prosecution for insider trading. This important information was missing from the media release.

Second, the media release contained no information about the legal options that were available to ASIC and the DPP for bringing enforcement action against Vizard. What this meant was that for more than a week, there was incorrect information in media discussion about the legal options that were available. This lead to even more confusion and criticism of ASIC. ASIC should have outlined what its legal options were in its media release.

Third, the 4 July 2005 media release contained facts which could easily be interpreted as indicating Vizard had engaged in insider trading. Yet the media release contained no mention of insider trading. ASIC needed to indicate why it was that it had decided to bring civil proceedings for breaches of directors' duties against Vizard. Some of this information was subsequently made public by ASIC (such as the lack of evidence) but this was too late.

ASIC could have avoided some of the extensive criticism which has been aimed at it if it had been more transparent in its 4 July media release.

The second matter concerns the fact that the Judge doubled the management banning order which ASIC had suggested to the court was appropriate. In the minds of many, this indicated that ASIC had misjudged the seriousness of Vizard's actions.

There is another issue. It is interesting to note that the Judge referred to Vizard's actions in misusing the Telstra information as "dishonest". Given that whether the information is used dishonestly is a key difference between criminal and civil proceedings, it is understandable there is still a question as to whether criminal proceedings should have brought for breaches of director's duties. Interestingly, the DPP's media release of 28 July 2005 states in the opening paragraph that it explains the decision of the DPP "to not prosecute Steve Vizard for criminal offences of insider trading". It does not mention criminal offences for breaches of Vizard's director's duties.

Finally, there has been extensive discussion about whether law reform is needed. The Judge observed that if it is thought that the monetary penalty he imposed is insufficient, then Parliament should increase the maximum penalty allowed. This is no doubt something the Government will consider.

In response to the Vizard matter, some have suggested that ASIC should be able to conduct its own major prosecutions and not have to refer the results of its investigations to the DPP. I disagree. I suggest it is important that there be an independent body, such as the DPP, which independently reviews and evaluates the results of investigations by regulators in order to determine whether criminal proceedings are appropriate. This is a healthy check on regulators which, for good reasons, have very extensive investigative powers.

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