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1. Recent Corporate Law and Corporate Governance Developments

1.1 Assessment of the Basel capital framework in Australia

On 18 March 2014, the Australian Prudential Regulation Authority (APRA) welcomed an assessment by the Bank for International Settlements (BIS) Basel Committee on Banking Supervision (the Basel Committee) of the implementation of the Basel capital framework in Australia.

The Basel Committee's report assesses Australia's capital framework for authorised deposit-taking institutions as being "compliant" with the Basel capital framework.

The report on Australia is the eighth in a series of assessments by the Basel Committee under its *Regulatory Consistency Assessment Programme* (the RCAP). An RCAP review makes an assessment of the extent to which the capital framework in each member jurisdiction is aligned with the minimum standards agreed by the Basel Committee. The assessments examine the consistency and completeness of the domestic framework, including the significance of any deviations.

Earlier reports have been published on China, the European Union, Japan, Singapore, Switzerland, the United States and Brazil.

The Basel Committee's Report is available on the BIS website.

1.2 Report on EU securities market conditions

On 12 March 2014, the European Securities and Markets Authority (ESMA) published *ESMA Report No. 1, 2014* on trends, risks and vulnerabilities, and its risk dashboard for the fourth quarter 2013. The report looks at the performance of European Union (EU) securities markets, assessing both trends and risks in order to develop a comprehensive picture of systemic and macro-prudential risks in the EU that can serve both national and EU bodies in their risk assessments.

Overall, the report finds that EU securities markets and investment conditions in the EU improved in the second half of 2013, based on better macro-economic prospects, which also contributed to reduced systemic risk in that period. Overall risks, however, remained at high levels for EU securities markets as reflected by the rapid propagation of uncertainty from emerging markets (EM) countries to EU markets from early 2014.

ESMA also monitors market developments which may present future vulnerabilities.

The report provides in-depth analysis of the following five topics:

- high-frequency trading;
- structural vulnerabilities due to low interest rates;
- first evidence from ESMA's Central Rating Repository;
- EU central securities depositories (CSDs); and
- stress-testing of investment portfolios.

The report and the risk dashboard are available on the ESMA website.

1.3 SEC proposes rules for systemically important and security-based swap clearing agencies

On 12 March 2013, the US Securities and Exchange Commission (SEC) voted to propose a new rule to enhance the oversight of clearing agencies that are deemed to be systemically important or that are involved in complex transactions, such as security-based swaps.

The *Dodd-Frank Wall Street Reform and Consumer Protection Act* called for an enhanced regulatory framework for certain clearing agencies. The SEC's proposal would apply to SEC-registered clearing agencies that have been designated as systemically important by the Financial Stability Oversight Council or that take part in more complex transactions, such as clearing security-based swaps.

Clearing agencies covered by the proposed rule would be subject to new requirements regarding their financial risk management, operations, governance, and disclosures to market participants and the public. The proposal also would establish procedures for the SEC to apply the new requirements to additional clearing agencies.

The proposed rule is available on the SEC website.

1.4 IOSCO report on prudential standards in the securities sector

On 10 March 2014, the International Organization of Securities Commissions (IOSCO) published the consultation report *A Comparison and Analysis of Prudential Standards in the Securities Sector*, which undertakes a high-level comparative analysis of the key prudential/capital frameworks for securities firms.

The consultation report seeks to highlight similarities, differences and gaps among the different frameworks. IOSCO's objective is to update its 1989 report on capital adequacy standards for securities firms (the 1989 Capital Standards Report), based on the issues identified in the consultation report.

The consultation report highlights prudential regulatory and supervisory areas that might be considered in any update of the 1989 Capital Standards Report, particularly:

- to identify opportunities for regulatory capital arbitrage that might (or actually) have materialised from differences in prudential regulations across jurisdictions; and
- to account for the increasing use of internal models and the commensurate increase in infrastructure, systems and controls that are necessary to help ensure that firms are not undercapitalised compared to the risks posed by their positions and activities.

The consultation report is available on the IOSCO website.

1.5 Australian board diversity: latest data

The percentage of women on Australia's top corporate boards has more than doubled and the number of ASX200 companies without a woman on their board halved over the last four years, according to new figures from the Australian Institute of Company Directors (AICD) published on 7 March 2014.

Women now hold 23.8% of directorships in the ASX20, 21.4% of directorships on the ASX50 and 20.5% of directorships on the ASX100.

The number of ASX200 boards without any female directors has more than halved from 87 boards in June 2010 to 42 boards. There are now only five ASX100 boards and one ASX50 board without a female director, and none in the ASX20.

The percentage of females among appointments to ASX200 boards increased from 5% in calendar year 2009 to 22% in 2013 and women have made up 39% of new appointments to ASX 200 boards to date in 2014.

The number of female chairs on ASX200 boards has also doubled from five (2.5% of all chairs) in 2010 to ten (5%).

Further information is available on the AICD website.

1.6 UK rules on crowdfunding

On 6 March 2014, the UK Financial Conduct Authority (FCA) released new rules that aim to better protect people looking to lend money or invest through crowdfunding.

The crowdfunding market is small, but growing rapidly. Securities-based crowdfunding, which the FCA already regulates, allows people to buy shares or debt securities in a company. Last year £28 million was raised for growing businesses, an increase of around 600% compared to 2012.

Loan-based crowdfunding (mainly peer-to-peer (P2P) lending), which will be regulated by the FCA from April 2014, saw £480 million lent by consumers to individuals and businesses in 2013, a rise of around 150% on the previous year.

The rules on loan-based crowdfunding focus on ensuring that consumers interested in lending to individuals or businesses have access to clear information, which allows them to assess the risk and to understand who will ultimately borrow the money. The rules also require firms running the loan-based platforms to have plans in place so that loan repayments continue to be collected even if the online platform enters into difficulties. Also, new prudential regulations will be introduced over time so that these firms have capital to help withstand financial shocks. This is important as consumers who lend money through these firms will not be able to claim through the Financial Services Compensation Scheme.

The policy statement on crowdfunding is available on the FCA website.

1.7 Basel III monitoring results published by the Basel Committee

On 6 March 2014, the Bank for International Settlements (BIS) Basel Committee on Banking Supervision (the Basel Committee) published a report presenting the results of its Basel III monitoring exercise. The study is based on the reporting processes set up by the Basel Committee to periodically review the implications of the Basel III standards for financial markets. The results of previous exercises in this series were published in April 2012, September 2012, March 2013 and September 2013.

A total of 227 banks have participated in the current study, comprising 102 large internationally active or "Group 1" banks (defined as internationally active banks that have Tier 1 capital of more than €3 billion) and 125 "Group 2" banks (i.e. all other banks).

The report is available on the BIS website.

1.8 CAMAC discussion paper: managed investment schemes

On 6 March 2014, the Corporations and Markets Advisory Committee (CAMAC) released a discussion paper on managed investment schemes.

The discussion paper deals primarily with the establishment and ongoing operation of schemes and raises a broad range of governance, disclosure and regulatory issues. It follows on from a July 2012 CAMAC report that made wide-ranging recommendations relating to the restructuring and winding up of financially stressed schemes. Together, the two documents cover every aspect of the managed investment scheme regime, to see whether it is relevant and, if so, appropriate, having regard to the development of managed investment schemes as significant entities in Australia's commercial activities.

In developing this discussion paper, CAMAC has taken the view that the regulatory regime for schemes should be aligned with that for companies, unless there are compelling reasons for treating schemes differently. Unjustified regulatory differences open the way to unnecessary complexity and impose undue compliance burdens on those industry participants who operate both schemes and companies (including through stapled entities).

In addition, the discussion paper:

- canvasses the possibility of assisting responsible entities to manage scheme capital by providing a statutory buyback procedure similar to that for companies;
- reviews the various disclosure requirements for schemes with a view to determining what disclosure regime would best achieve the information needs of scheme investors, while avoiding undue administrative burdens; and
- raises issues relating to valuation of scheme assets, which is a key factor in the pricing of scheme interests and is of particular significance for investors in unlisted schemes.

Other matters with which the paper deals include scheme registration, enforcement and amendment of the scheme constitution, the duties and entitlements of the responsible entity, scheme meetings, scheme takeovers and scheme reorganisations.

The discussion paper is available on the CAMAC website.

1.9 US Supreme Court hears arguments on securities fraud class actions and fraud-on-the-market presumption

On 5 March 2014, the US Supreme Court heard oral argument in *Halliburton Co v Erica P John Fund, Inc*, No. 13-317, in which the Court is considering whether to overrule or significantly limit the ability of plaintiffs to rely on the legal presumption that each would-be class member in a securities fraud class action relied on the statements challenged as fraudulent in the lawsuit. Without this so-called fraud-on-the-market presumption of class-wide reliance, putative class action plaintiffs would face substantial barriers in maintaining securities fraud class actions. According to commentators, the Court's decision could lead to a significant change in the conduct of securities class actions.

The transcript of the proceedings is available on the US Supreme Court website.

1.10 Proxy advisers' best practice principles

On 5 March 2014, the charter signatories to the *Best Practice Principles for Shareholder Voting Research & Analysis* announced the official launch of the industry-developed principles relating to the provision of shareholder voting and governance analytical services.

The high-level principles cover three main areas:

- service quality;
- conflicts of interest management; and
- market communications.

Each principle is supported by related guidance and background information that demonstrate how to apply the principles.

The principles were developed by the independent Best Practice Principles Group (BPPG), comprising the charter signatories, in response to the 19 February 2013 European Securities and Markets Authority feedback statement on the consultation regarding the role of the proxy advisory industry. While ESMA concluded that "it has not been provided with clear evidence of market failure in relation to how proxy advisors interact with investors and issuers", ESMA identified in its feedback statement particular areas that it believed would benefit from improved clarity on the part of the industry. It recommended the establishment of a code of conduct that would foster better understanding among all stakeholders of the role of proxy analysts and what can rightfully be expected from them.

The principles are available on the BPPG website.

1.11 Women on boards: voluntary code for executive search firms

In March 2014, the UK Department for Business Innovation and Skills (DBIS) released a report *Women on Boards: Voluntary Code for Executive Search Firms*.

The Voluntary Code for Executive Search Firms was created to ensure executive search firms support FTSE 350 companies in creating more diverse boards and covered the relevant search criteria and processes.

The code is available on the DBIS website.

1.12 Implementation of Australia's G20 over-the-counter derivative commitments: G4-IRD central clearing mandate

On 27 February 2014, the Treasury released a proposals paper on the implementation of Australia's Group of 20 (G20) over-the-counter derivatives commitments.

At the 2009 G20 summit in Pittsburgh, the Australian Government joined other jurisdictions in committing to substantial reforms to practices in the over-the-counter (OTC) derivatives market.

The three key G20 commitments in this area are to:

- improve transparency by requiring all OTC derivatives to be reported to central registries known as trade repositories;
- improve market efficiency and risk management by requiring standardised OTC derivatives to be cleared through specialised entities known as central counterparties; and
- improve market efficiency and integrity by requiring the execution of all standardised OTC derivatives on exchanges or electronic trading platforms, where appropriate.

Legislation was passed in 2012 which allows the Minister to make a determination with respect to a G20 commitment providing authority for the Australian Securities and Investments Commission (ASIC) to develop detailed rules implementing the determination.

A first determination was subsequently made mandating trade reporting of OTC derivatives, which is currently being implemented through a phased approach.

The Australian Government is publishing this proposals paper to seek stakeholder views on a proposed approach for a first step in implementing its G20 commitments in relation to central clearing of OTC derivatives. This consultation is conducted specifically in relation to the requirements in s. 901B(3) of the Corporations Act 2001 (Cth) (the Act) and related obligations under the Act, and the Legislative Instruments Act 2003 (Cth).

The proposals paper is based on recommendations provided by the Australian Prudential Regulatory Authority, ASIC and the Reserve Bank of Australia contained in Report on the Australian OTC Derivatives Market (July 2013).

The proposals paper is available on the Treasury website.

1.13 Disclosure of non-financial information by certain large EU companies: European Parliament and Council reach agreement to improve transparency

On 26 February 2014, the European Commission announced that the European Parliament and the Council reached agreement on an amendment to existing accounting legislation to improve the transparency of certain large companies on social, environmental and diversity matters. Companies concerned will need to disclose information on policies, risks and results regarding environmental matters, social and employee-related aspects, respect for human rights, anti-corruption and bribery issues, and diversity on boards of directors.

Large public-interest entities (mainly listed companies and financial institutions) with more than 500 employees will be required to disclose environmental and social information in their management reports. This includes listed companies as well as some unlisted companies, such as banks, insurance companies, and other companies that are so designated by European Union (EU) member states because of their activities, size or number of employees. The scope includes approximately 6,000 large companies and groups across the EU.

Further information is available on the European Commission website.

1.14 New draft guidelines to encourage shareholder engagement

On 26 February 2014, the Governance Institute of Australia released for public comment draft guidelines to assist ASX-listed companies and their institutional investors to engage more effectively so as to enhance long-term performance and corporate value.

Developed in consultation with chairpersons and directors from leading listed companies and senior executives in the institutional investor sector, the draft guidelines reflect a consensus that both sides would benefit from a best practice code that establishes clearer lines of communication, promotes greater transparency in governance-related decision-making and sets a course for a more productive relationship between the two groups.

The draft guidelines are available on the Governance Institute of Australia website.

1.15 Survey finds economic crime rising globally

On 19 February 2014, PricewaterhouseCoopers (PwC) released its report on a survey on incidences of economic crime. Economic crime against businesses and other organisations continues to rise around the world. Some 37% of respondents, a 3% rise since 2011, say they have been victims of economic crime, according to PwC's *Global Economic Crime Survey 2014*. About 25% say they have been victims of cybercrime. Theft remains the most common form of economic crime, reported by 69% of respondents.

The survey report is available on the PwC website.

1.16 Anti-money laundering survey

On 13 February 2014, KPMG released its report on a survey on anti-money laundering (AML). AML measures are an increasing priority for boards and senior management across Australia but awareness and take-up across the financial services industry still lags behind the global average, according to the survey.

KPMG's *Global AML Survey 2014*, its fourth such survey, found that 88% of respondents consider AML a priority for boards and senior management, up from 62% in 2011. The 2014 survey tracked responses from 317 AML-related professionals in the financial services industry across 48 countries.

In Australia, while 80% of respondents indicated that boards of directors take an active interest in AML (up from 50% in 2011), this still falls short of the global average. 40% of Australian respondents indicated that AML issues are regularly discussed at board level, compared to the global average of 66%.

The survey is available on the KPMG website.

1.17 Two-strikes rule on remuneration report voting: a three-year stocktake

On 5 February 2014, Guerdon Associates published a stocktake of the effectiveness of the two-strikes rule.

The findings include that:

- "[a] 'strike' (i.e. an against vote of more than 25%) has been recorded at approximately 6% of meetings over the three years since the rule's introduction;
- [i]n total, 40 companies have recorded two strikes: 18 companies in 2013 and 22 in 2012;
- 17 of the 18 companies that recorded a second strike were outside the ASX200;
- [a] spill resolution was carried at only 2 of the 18 companies that were required to put up this resolution in 2013, requiring a spill meeting to be held;
- [o]nly six ASX-listed companies in total have been required to hold a spill meeting since the rule was introduced;
- [n]o incumbent directors have lost their board seat at a spill meeting. Any directors who have been 'voted down' at a spill meeting have been new directors seeking election (more often than not, having been put forward by a substantial shareholder); and
- [e]ight companies have technically recorded three consecutive strikes (although the strike rate resets after the second)".

Further information is available from the Guerdon Associates website.

1.18 Risk intelligent governance: a practical guide for boards

In February 2014, Deloitte released a follow-up report to its 2009 report *Risk Intelligent governance: A practical guide for boards*. The follow-up report provides examples and case studies compiled in Deloitte's work with boards that employ state-of-the-art practices.

These practices focus on six key areas:

- defining the board's risk oversight role;
- fostering a risk intelligent culture;
- approving the risk appetite;
- helping management incorporate risk intelligence into strategy;
- assessing the maturity of the risk governance process; and
- making sure the organisation discloses the risk story to stakeholders.

The follow-up report and the 2009 report are available on the Deloitte website.

1.19 2014 review of the OECD Principles of Corporate Governance

In early 2014, the Organisation for Economic Co-operation and Development (OECD) launched a review of the OECD Principles of Corporate Governance that were first released in May 1999 and last revised in 2004.

The principles are one of the Financial Stability Board's (FSB) 12 key standards for international financial stability and form the basis for the corporate governance component of the report on the observance of standards and codes of the World Bank Group.

The rationale for the review is to ensure the continuing high quality, relevance and usefulness of the principles taking into account recent developments in the corporate sector and capital markets. The outcome should provide policymakers, regulators and other rule-making bodies with a sound benchmark for establishing an effective corporate governance framework.

The *OECD Principles of Corporate Governance (2004)* are available on the OECD website.

1.20 IIASB publishes framework for audit quality

In February 2014, the International Auditing and Assurance Standards Board (IAASB) released *A framework for audit quality: key elements that create an environment for audit quality*.

Financial information should be relevant, timely and reliable to meet the needs of users. National laws and regulations, as well as an entity's stakeholders, often require an external audit of some elements of the financial information to give users confidence that the information can be trusted. For an external audit to fulfil its objective the users of audited financial statements must have confidence that the auditor has worked to a suitable standard and that "a quality audit" has been performed.

For this reason, the IAASB has developed this framework that describes the input, process and output factors that contribute to audit quality at the engagement, audit firm and national levels, for financial statement audits. The framework also demonstrates the importance of appropriate interactions among stakeholders and the importance of various contextual factors.

The framework is available on the IAASB website.

1.21 US securities class action data

On 28 January 2014, Cornerstone Research and the Stanford Law School Securities Class Action Clearinghouse released the report *Securities Class Action Filings: 2013 Year in Review*.

According to the report, plaintiffs filed 166 new federal securities class actions in the US in 2013, a 9% increase over 2012. The 2013 filings, although boosted by a second-half surge, are still 13% below the historical average from 1997 to 2012.

One possible explanation for the filings' remaining below the historical average in recent years is the decline in the number of unique companies listed on the NYSE and NASDAQ. A new analysis in the report shows that the number of companies on these exchanges has decreased 46% since 1998, providing fewer companies for plaintiffs to target as the subject of federal securities class actions.

The almost 50% decrease in listed companies has played a part in the recent trend of low numbers of class action filings.

The report also analyses the recent increase in IPOs on major US exchanges. The 150 IPOs in 2013 represent the highest number in the last five years. In addition, there has been an increase in larger companies undertaking IPOs in recent years, particularly in 2013.

The report is available on the Cornerstone Research website.

1.22 Recent Centre for Corporate Law and Securities Regulation research papers

(a) Responsibilities of the board of directors (by Reegan Grayson Morison and Ian Ramsay)

In this article the authors analyse the allocation of responsibilities between the board of directors and senior management in board charters of companies listed on the Australian Securities Exchange. There are several reasons why this research is of interest. First, the allocation of responsibilities between the board and senior management is an important part of the system of corporate governance established by companies. Second, on occasions courts have identified the responsibilities of the board of directors. It is useful to compare what courts have said are the responsibilities of the board of directors with what companies themselves state are the responsibilities of their board. Third, there has been an active debate about what responsibilities boards can delegate. This debate can be informed by research on what responsibilities boards retain and what responsibilities they delegate to senior management.

The paper is available here.

(b) Consumer leases and consumer protection: Regulatory arbitrage and consumer harm (by Paul Ali, Cosima McRae, Ian Ramsay and Tiong Tjin Saw)

Consumer leases are regulated in Australia separately from credit contracts. This has created opportunities for regulatory arbitrage and has resulted in significant harm to consumers. Recent reforms, which commenced on 1 March 2013, have addressed this problem by applying to consumer leases many of the statutory protections available to consumers under credit contracts; the distinction between consumer leases and credit contracts, however, has been retained. The authors argue in this article that the distinction is artificial and should be abandoned. They also examine how the uneven regulation of consumer leases and credit contracts has harmed consumers and assess the recent reforms to the regulation of consumer leases. Finally, they investigate the practice of consumer leasing in Australia by reference to a survey of the consumer leasing industry, the cost of consumer leases, and selected "real life" case studies.

The paper is available here.

(c) The politics of payday lending regulation in Australia (by Paul Ali, Cosima McRae and Ian Ramsay)

The regulation of payday lending in Australia has recently been reformed. The reforms followed a highly charged and polarised debate between the conflicting interests of consumer and welfare advocates, who argued for increased protection for payday loan borrowers, and the payday loan industry. The debate followed research findings of the adverse consequences of payday lending for low income and financially vulnerable borrowers. The authors analyse the political dynamic that unfolded and show how the protections proposed to be afforded to payday loan borrowers were reduced in several key respects. The research highlights several concerns. First, key changes to the original proposals do not take account of the recommendations of consumer and welfare advocates and are more consistent with the views of the payday loan industry. Second, the increased complexity of the final form of the regulation of payday lending creates potential for regulatory avoidance and poses problems for enforcement. Third, policies to reduce reliance on payday loans have not been implemented. The result is new regulation of payday loans that may not achieve the key aim of protecting the most vulnerable borrowers from the harm that can result from these loans.

The paper is available here.

2. Recent ASIC Developments

2.1 ASIC publishes seventh markets supervision report

On 19 March 2014, ASIC published its seventh report on the supervision of Australian financial markets and market participants.

Report 386 *ASIC supervision of markets and participants: July to December 2013* (REP 386) highlights the volume of market and participant-related outcomes achieved by ASIC in the second half of 2013.

Key outcomes include:

- 19,255 trading alerts produced;
- 102 market inquiries conducted;
- 31 matters referred for further investigation;
- 16 risk-based assessment visits conducted;
- 73 surveillances completed;
- 26 instances of pre-emptive supervision action;
- seven enforcement outcomes for insider trading offences; and
- four infringement notices issued by the Markets Disciplinary Panel.

REP 386 is available on the ASIC website.

2.2 ASIC information sheet on audit quality

On 17 March 2014, ASIC released information to help directors and audit committees develop robust standards as part of its commitment to improve audit quality.

Information Sheet 196 *Audit quality: The role of directors and audit committees* (INFO 196) explains:

- why audit quality is important;
- the responsibilities of the auditor;
- the roles of directors and audit committees;
- the responsibilities of directors for auditor independence;
- who should manage the appointment of auditors;
- what matters should be considered in setting audit fees; and
- what directors and audit committees can do to promote audit quality.

INFO 196 suggests directors and audit committees consider:

- non-executive directors recommending auditor appointments and setting audit fees;
- assessing the commitment of the auditors to audit quality;
- reviewing the resources devoted to the audit, including the amount of partner time and the use of experts;
- accountability within the audit firm for quality;
- support by company management for the audit process;
- two-way communication with the auditor on concerns and risk areas;
- ensuring independence of the auditor; and
- reviewing audit firm responses to findings from ASIC audit inspections.

INFO 196 is available on the ASIC website.

2.3 ASIC facilitates internet securities offers

On 3 March 2014, ASIC released updated guidance to facilitate and encourage the use of the internet and other interactive media for making offers of securities.

Updated Regulatory Guide 107 *Fundraising: Facilitating electronic offers of securities* (RG 107) aims to ensure that ASIC's guidance reflects current market practices and advances in technology.

RG 107 includes:

- an explanation of ASIC's view on the way the internet and other electronic means can be used in making offers of securities;
- a "good practice guide" to assist offerors, distributors, publishers and other parties involved in distributing offers; and
- continuation of relief for the use of personalised or Australian financial services (AFS) licensee-created application forms.

As part of the update, ASIC confirms its view that the use of electronic disclosure documents is permitted under the law. ASIC Class Order [CO 00/44] - Electronic disclosure documents, electronic application forms and dealer personalised applications has accordingly been revoked. ASIC has issued new ASIC Class Order [CO 14/26] to continue relief for the use of personalised or AFS licensee-created application forms.

ASIC has also released Report 385 *Response to submissions on CP 211 Facilitating electronic offers of securities: Update to RG 107*, which highlights the key issues that arose from the submissions ASIC received in response to Consultation Paper 211 - Facilitating electronic offers of securities: Update to RG 107 (June 2013).

RG 107 and REP 385 are available on the ASIC website.

3. Recent ASX Developments

3.1 ASX consultation on T+2 settlement cycle for Australia

On 25 February 2014, ASX issued a consultation paper on the introduction of a T+2 settlement cycle for cash market trades in Australia. The consultation paper sets out a proposal to shorten the current settlement period of trade-day-plus-three-days (T+3) by one business day, creating capital and margin savings for industry, and a faster settlement of transactions for investors.

ASX is seeking feedback on the benefits, industry readiness, timetable for implementation and other issues that would need to be addressed to enable the transition to T+2. T+2 already operates in a number of major markets, including Germany and Hong Kong, and will shortly be introduced throughout Europe.

The potential benefits of shortening the settlement cycle by one business day include:

- reduced counterparty risk for individual investors, participants and the central counterparty (clearing house), resulting in lower systemic risk for the market as a whole;
- less regulatory capital required to be held by market participants to mitigate risk;
- standardised regional and global settlement practices; and
- improved post-trade operational and process efficiencies, and associated cost savings.

ASX's advisory forum, established under its code of practice in 2013, has prioritised the consideration of introducing T+2. Through the forum, ASX is working with industry to provide the Australian market with global best practice cash market clearing and settlement services.

ASX is seeking feedback on the feasibility of introducing T+2 in the first quarter of the 2016 calendar year, or whether an earlier implementation date is supported.

Further information is available on the ASX website.

3.2 Supplementary consultation paper on proposed governance-related listing rule amendments

On 21 February 2014, ASX issued a supplementary consultation paper on proposed governance-related listing rule amendments. The supplementary consultation paper invites comments from listed entities, their advisers and other stakeholders on modifications to the governance-related listing rule amendments detailed in the consultation paper that was released on 16 August 2013.

The supplementary consultation paper is available on the ASX website.

3.3 ASX and Bank of China to deliver new RMB Settlement Service

On 18 February 2014, ASX announced that ASX and the Bank of China have agreed to deliver Renminbi (RMB) settlement services to the Australian and Chinese financial markets by the middle of 2014.

The service will allow Australian companies to efficiently take or make payments with their Chinese investment and trading partners through proven market infrastructure. Bank of China country head and Sydney branch general manager Shanjun Hu and ASX managing director and CEO Elmer Funke Kupper jointly stated that:

> [the agreement] represents a major milestone in the internationalisation of the RMB and highlights the importance of the Australia-China trade relationship worth $120 billion last financial year.

The key benefits of the new service include:

- Increased accessibility: allowing Australian companies to efficiently use RMB as a settlement currency in their cross-border transactions with trading and investment partners in China;
- Lower costs and risk: Australian companies trading with China will be able to pay and receive RMB, thereby eliminating exchange rate risk and the cost of conversion; and
- New growth opportunities: an important step in expanding the scope and global connectivity of Australia's financial markets. This initiative will allow for a range of investment products, including RMB denominated bonds and other structured instruments, to be developed.

Further information is available on the ASX website.

3.4 ASX Ltd Half-year Report: 31 December 2013

On 13 February 2014, the ASX released its results for the half-year ending 31 December 2013.

ASX managing director and CEO Elmer Funke Kupper said that "ASX produced a positive result for the first six months of the 2014 financial year, with operating revenue growing 8.0% and net profit rising by 10.8%. Improved global economic conditions and an uplift in listings activity in Australia underpinned the result".

Further information is available on the ASX website.

3.5 Reports

On 5 March ASX released:

- the ASX Group Monthly Activity Report;
- the ASX 24 Monthly Volume and Open Interest Report; and
- the ASX Compliance Monthly Activity Report

for February 2014.

4. Recent Takeovers Panel Development

4.1 Lantern Hotel Group: Panel declines to conduct proceedings

On 18 March 2014, the Takeovers Panel announced that it had declined to conduct proceedings on an application dated 11 March 2014 from Totem Holdings Pty Ltd in relation to the affairs of Lantern Hotel Group (Lantern).

The application concerned an offer to Lantern to buy back 24.3% of Lantern's securities held by Millinium Asset Services Pty Ltd and the resulting increase in Torchlight GP Ltd's (Torchlight) relevant interest from approximately 30% to 40% (see TP14/20).

The Panel considered that the buyback offer was unlikely to result in unacceptable circumstances because (among other things) the policy, if not the letter, of s. 609(7) of the Corporations Act 2001 (Cth) (the Act) applied. Therefore either no relevant interest was acquired in breach of s. 606 of the Act, or any breach was not unacceptable.

The Panel considered that, if the buyback was to proceed and Torchlight proposed to vote in favour of the shareholder approval for the buy-back, a fresh application could be made by ASIC or a person interested.

The Panel concluded there was no reasonable prospect that it would make a declaration of unacceptable circumstances. Accordingly, the Panel declined to conduct proceedings.

The Panel will publish its reasons for the decision in due course on the Takeovers Panel website.

5. Recent Research Papers

5.1 "Comply-or-explain" in Belgium, Germany, Italy, the Netherlands and the UK: insufficient explanations and an empirical analysis

This study analyses the level and quality of the application of the "comply-or-explain" principle for listed companies in Belgium, Germany, Italy, the Netherlands and the UK. Although the comply-or-explain principle has now become a central element in the corporate governance of the European Union, a common understanding of the scope and necessary conditions for it to work effectively has not yet been achieved. This study explains the comply-or-explain principle from the perspective of the economic theory (legitimacy theory and theory on market failure) and is the first study of the application of the principle in which consecutive years are analysed for multiple countries simultaneously with one research method. In this study 237 annual accounts for the years 2005 - 2007 are analysed for five countries. The results show that company size and the period of time the comply-or-explain principle has been applicable in a country predict the level and quality of compliance. Although the level of code compliance is high, the quality of the explanations for code provisions not complied with is insufficient. Further fine-tuning of the comply-or-explain principle is necessary to achieve the most effective application in order to make the principle work in practice as intended.

The paper is available on the SSRN website.

5.2 The hidden nature of executive retirement pay

There are two competing theories of why public companies pay executives generous retirement benefits. One is that retirement pay is easier to hide from shareholders than other forms of compensation. The other is that retirement benefits align executives' interests with those of long-term creditors, since the executives may not receive their payouts if the company goes bankrupt. The latter view depends on the assumption that retirement benefits put executives in a similar contractual position as that of the company's creditors. Yet no previous work has tested that assumption.

This article provides the first systematic study of the contractual structure of executive retirement payouts in the US. Using retirement pay data for thousands of executives, the authors show that a large proportion of executives link the value of their payouts to the company's stock price and receive the bulk of these payouts immediately following their departure - features that contradict the incentive-alignment theory of retirement pay. The evidence also shows that the full amount and structure of retirement pay are undisclosed - findings consistent with the camouflage theory. While the structure of some executives' payouts can be reconciled with the incentive-alignment theory, current rules do not give investors the information they need to tell the difference between payouts that align incentives and those that camouflage compensation. Lawmakers should require companies to reveal the magnitude and structure of these payouts, and neither regulators nor commentators should assume that retirement benefits suppress top managers' appetite for risk.

The paper is available on the SSRN website.

5.3 Determinants of corporate governance codes

Corporate governance codes are an increasingly prominent feature of the regulatory landscape in many countries, yet remarkably little is known about the determinants of corporate governance reform.

Potential determinants include:

1. the diffusion of an international benchmark model of good governance;
2. a country's legal system;
3. the desire to attract foreign investors; and
4. the influence of interest groups.

The author constructs a proxy for the investor-friendliness of 52 corporate governance codes of different jurisdictions and collects data on the code issuers. The author finds strong evidence that the drafters of codes emulate international benchmark models and that jurisdictions belonging to different legal traditions use different regulatory strategies, some evidence that portfolio equity inflows are associated with the investor-friendliness of codes, and no evidence that interest groups succeed in affecting rules. The article suggests a method for the modelling of legal evolution, convergence, and the political economy of corporate governance codes.

The paper is available on the SSRN website.

5.4 Assessing transnational private regulation of the OTC derivative market: ISDA, the BBA, and the future of financial reform

For the last 20 years, the dominant narrative of the over-the-counter (OTC) derivatives market has been one of absent regulation, deregulation, and regulatory conflict, predictably resulting in disaster. This article challenges this narrative, arguing that the global derivatives market has been subject to pervasive and harmonised regulation by what should be recognised as transnational private regulators. Recognising the reality of widespread transnational private regulation of derivatives has significant implications, which this article explores. Appreciating the actual regulatory status quo is essential if policymakers are to correctly diagnose problems, avoid past regulatory errors, and plan effective remedies. There are also advantages to relying on private transnational regulation, as increased governmental effort to regulate the OTC derivatives space may undermine and fracture existing regulation. To be sure, private transnational regulation carries risks that have sometimes materialised, such as the manipulation of LIBOR. Thus, this article also evaluates best practices in regulating through transnational private governance.

The paper is available on the SSRN website.

5.5 Regional financial regulation in Asia

The Asian financial crisis (1997 - 1998) and the global financial crisis (2007 - 2009) highlighted the potential value of financial regionalism, i.e., regional-level cooperation in financial policy. This paper argues that there is a mediating role for regional-level institutions of financial regulation between national regulators in Asia and global-level institutions such as the International Monetary Fund and the Financial Stability Board.

This potential role includes:

i. monitoring financial markets and capital flows to identify regional systemic risks such as capital flows;
ii. coordinating financial sector surveillance and regulation to promote regional financial stability; and
iii. cooperating with global-level institutions in rule formulation, surveillance and crisis management.

This is particularly important in an environment of increasing financial integration and harmonisation in the region.

The paper is available on the SSRN website.

5.6 Making bank resolution credible

Financial difficulties at large financial institutions present governments and regulators with an unenviable dilemma. On the one hand, they are afraid to permit such a firm to enter "ordinary" insolvency proceedings, lest this transmit financial shock to other, connected, institutions. Yet every voter can grasp the moral hazard problems and distributional inequity associated with government handouts for the financial sector. Consequently many jurisdictions have introduced, or are designing, "special resolution" mechanisms for financial institutions. The first generation of such mechanisms was based on the US FDIC receivership regime. These focus on waiving property rights so as to effect a very rapid transfer of complex assets and short-term liabilities to a purchaser who will be able to stand behind those liabilities and thereby ensure stability. This model works well for small to medium sized domestic banks, but is insufficient to provide a credible alternative to bailouts for large, complex financial institutions.

As a result, a series of new measures - which are termed "second generation" resolution mechanisms - have been developed. First, there has been a realisation that the level of complexity is such that resolution *ex post* is impossible without careful planning by supervisors *ex ante*. Second, this planning process can be used not only to understand, but also to modify, the structure of complex financial institutions and their regulatory oversight so as to facilitate resolution should it be necessary. Third, the use of "bail-in" or mandated debt to equity swaps provides a potentially very useful additional resolution tool when used in conjunction with such forward planning and oversight. Fourth, in the context of international financial institutions, coordination and allocation of responsibility amongst national regulators is an integral part of the planning process.

The implications of this shift are clear. For the resolution of large complex financial institutions to be credible, it must be thought of as an integral part of the ongoing oversight of financial institutions by regulators, and not as simply a set of mechanisms that are kept for troubled times. Investment in regulatory capacity - recruitment and training to build human capital in the regulatory sector - is therefore crucial to ensuring the success of resolution.

The paper is available on the SSRN website.

5.7 Corporate governance models and practices in Japan and East Asia: proceedings of a panel discussion

Despite general interest in the economic rise of Asia and in the role of law in the development of the region, the literature on comparative corporate governance in Asia is surprisingly undeveloped with respect to in-depth comparisons among Asian countries. In particular, it should be both valuable and feasible to compare and contrast corporate governance systems and practices among countries in East Asia, in light of Japan's historical influence and more recent divergences from that influence.

At a recent conference a distinguished group of corporate law scholars from Japan, South Korea, Taiwan, and China engaged in a broad-ranging panel discussion centring on the question of the operation and reform of traditional stakeholder-oriented corporate governance systems featuring concentrated ownership and a board of directors involved in day-to-day management against the need to account for greater monitoring of management on behalf of shareholders. For example, the panellists agreed that the traditional internal corporate auditors (or *kansayaku* in Japanese) have not appeared to operate effectively in monitoring management, and to some extent they should be supplemented or replaced by outside directors. However, the scope and pace of such change varies considerably among countries in east Asia, and scepticism remains about the effectiveness of outside directors. The panel discussion highlighted both the challenges and significant potential rewards for greater scholarly collaboration in making cross-Asian comparisons in the field of corporate governance.

The paper is available on the [SSRN website](#).

5.8 The foundations of corporate social responsibility

The authors investigate the roles of legal origins and political institutions—believed to be the fundamental determinants of economic outcomes—in corporate social responsibility (CSR). They argue that CSR is an essential path to economic sustainability, and document strong correlations between country-level sustainability ratings and various extensive firm-level CSR ratings with global coverage. They contrast the different views on how legal origins and political institutions affect corporations' trade-off between shareholder and stakeholder rights.

Their empirical evidence suggests that:

a. legal origins are more fundamental sources of CSR adoption and performance than firms' financial and operational performance;
b. among different legal origins, the English common law—widely believed to be mostly shareholder-oriented—fosters CSR the least;
c. within the civil law countries, firms of countries with German legal origin outperform their French counterparts in terms of ecological and environmental policy, but the French legal origin firms outperform German legal origin companies in social issues and labour relations. Companies under the Scandinavian legal origin score highest on CSR (and all its subfields);
d. political institutions—democratic rules and constraints to political executives—are not preconditions for CSR and sustainability, and sometimes even hinder CSR implementation.

The results are robust after controlling for corporate governance, culture, firm-level financial performance and constraints, and different indices of political institutions.

The paper is available on the [SSRN website](#).

5.9 Say on pay around the world

Shareholders have long complained that top executives are overpaid by corporate directors irrespective of their performance. Largely powerless to stop these practices, in 2002, they prevailed upon the UK Parliament to adopt legislation requiring public companies to permit their shareholders to have a mandatory, non-binding vote on the compensation of their top executives (*Say on Pay*). Since that time, there has been a wave of such legislation enacted in countries around the world, including the US, Australia, Belgium, the Netherlands, and Sweden, while Switzerland, Germany and France appear to be moving rapidly in the same direction. In this article, the authors ask, what is the justification for adopting these rules?

For countries where most corporations have dispersed ownership structures, like the US, the UK and Australia, proponents claimed that these votes would allow shareholders to more stringently monitor management and thereby reduce the agency costs of the separation of ownership and control in public companies. In concentrated ownership countries, such as the Netherlands, Germany, Sweden, France and Belgium, the existence of controlling shareholders at most companies in these countries means that there already is close supervision of pay levels by a concentrated owner with strong incentives not to overpay executives. However, the authors argue that there are other compelling reasons why *Say on Pay* has been enacted in these nations.

They find several other reasons for these changes: movements at larger public companies toward increased dispersion of ownership in several of these countries that are opening up a need for an alternative monitor of executive pay; strong support of such legislation by foreign institutional investors whose ownership interests in firms from these countries has increased dramatically in recent years; social pressures in many of these countries against rising levels of income inequality; political responses by left-leaning parties to these social pressures by introduction of *Say on Pay* legislation; and the presence of important state-owned enterprises in some of these countries that allows the state to play an important role in the regulation of executive pay using different techniques, including *Say on Pay*. On balance, these arguments have carried, or seem likely to carry, the day in each of the countries the authors examine.

The authors conclude by examining existing evidence on the effects of *Say on Pay* votes and how it is likely to evolve over time.

The paper is available on the SSRN website.

5.10 Labour representation in governance as an insurance mechanism

The authors investigate how Germany's mandated 50% labour representation on supervisory boards affects layoffs and wages during adverse industry shocks. They hypothesise that parity-codetermination helps the implementation of implicit contracts that insure employees against adverse shocks. They estimate difference-in-differences in employment and wages using panel data at the establishment level. The results show white-collar and skilled blue-collar employees of firms with parity-codetermination are protected against layoffs during shock periods and pay an insurance premium of about 3.5% in the form of lower wages. Unskilled blue-collar workers, who lack real representation on the board, are not protected against shocks. The effects of employment insurance manifest in higher operating leverage and a greater frequency of major asset sales during industry downturns. The authors conclude that mandated parity codetermination helps implementing implicit insurance contracts for employees with real representation on the board.

The paper is available on the [SSRN website]().

6. Recent Corporate Law Decisions

6.1 "Reasonable endeavours" in commercial contracts - an obligation conditioned by a balancing of the parties' business interests

(By Ian Pelekanakis, Herbert Smith Freehills)

Electricity Generation Corporation v Woodside Energy Ltd [2014] HCA 7, High Court of Australia, French CJ, Hayne, Crennan, Kiefel and Gageler JJ, 5 March 2014

The full text of this judgment is available [online]().

(a) Summary

A gas supply agreement (GSA) obliged the suppliers to make available gas up to a certain amount each day. The buyer was obliged to purchase a minimum annual amount. Beyond the guaranteed daily amount, the suppliers were obliged to use reasonable endeavours to supply a daily supplementary amount nominated by the buyer. In determining whether they were able to supply the supplementary amount, the suppliers could take into account "all relevant commercial, economic and operational matters". When an explosion at another gas producer's plant led to an inflated market price for gas for a period of time, the suppliers refused to supply the supplementary amount and instead entered into a temporary agreement with the buyer to supply gas at the prevailing market price. The Court agreed with the trial judge that the suppliers had not breached their obligation to use reasonable endeavours to supply to supplementary amount. The Court held that the standard of reasonableness in a commercial contract is necessarily conditioned by the surrounding circumstances, including the commercial objects of the contract and the balancing of the parties' business interests where there is a conflict. In all the circumstances, the obligation to use reasonable endeavours did not require the suppliers to sacrifice their business interests in obtaining a higher price for their gas.

(b) Facts

Electricity Generation Corporation (Verve) was the buyer and Woodside Energy Ltd, together with various other gas suppliers in Western Australia (the Sellers), were the suppliers of natural gas under a long-term GSA.

(i) Relevant terms of the GSA

The GSA provided for an annual minimum quantity (AMQ) of gas to be purchased by Verve on a "take or pay" basis. Each of the Sellers was obliged to make available its proportionate share of a maximum daily quantity (MDQ) of gas. Clause 3.3(a) provided that, where Verve nominated an amount of gas which exceeded the MDQ, the Sellers were obliged to "use reasonable endeavours" to make available a supplementary maximum daily quantity (SMDQ) at a prescribed price. Clause 3.3(b) provided that, "in determining whether they are able to supply SMDQ on a day, the Sellers may take into account all relevant commercial, economic and operational matters".

(ii) Apache incident and resultant dispute

An explosion occurred at a gas plant operated by Apache, the other principal source of domestic gas in Western Australia. The explosion led to a temporary reduction in the supply of natural gas to the Western Australian market by 30–35%, which led to demand exceeding supply. At this point in time, many customers in Western Australia sought to purchase gas from the Sellers at prices far exceeding those contained in the GSA. The Sellers informed Verve that they would not supply SMDQ under the GSA for an indefinite period and instead offered to supply Verve with an equivalent quantity of gas at the prevailing market price. This price exceeded the price for SMDQ. Under protest, and without prejudice to its rights under cl. 3.3, Verve accepted this offer. These circumstances persisted until the gas supply shortage ended, at which point the Sellers supplied SMDQ to Verve pursuant to the GSA.

It was common ground that the Sellers had the capacity to supply the SMDQ nominated by Verve during the relevant period. Verve commenced proceedings in the Supreme Court of Western Australia, arguing that the Sellers had breached their obligation under cl. 3.3 by failing to "use reasonable endeavours" to deliver the SMDQ to Verve during the relevant period. The trial judge rejected Verve's claim, whose appeal was allowed by the Court of Appeal. The Sellers then appealed to the High Court of Australia.

(c) Decision

(i) General principles regarding the construction of commercial contracts and "reasonable endeavours" clauses

The Court re-affirmed the general principle that the terms of a commercial contract are to be determined by what a reasonable businessperson would have understood those terms to mean. This requires consideration of the language used by the parties, the surrounding circumstances known to them and the commercial purpose or objects to be secured by the contract. An appreciation of the commercial purpose/objects is facilitated by an understanding of the genesis of the transaction, the background, the context and the market in which the parties operate.

The Court also made some general statements regarding the construction of "reasonable" or "best" endeavours clauses in commercial contracts. The Court held that the nature and extent of such obligations is necessarily conditioned by what is reasonable in the circumstances, which can include circumstances that may affect an obligor's business. Such provisions recognise that there may be a conflict between the independent business interests of the obligor and the interests of the obligee. This conflict is to be resolved by reference to a standard of reasonableness. Such a standard of reasonableness can be informed by an express internal standard, where the contract refers to certain considerations, as in this case cl. 3.3(b) did.

(ii) Application of the general principles

The Court agreed with the conclusion of the trial judge that the Sellers had not breached their obligations under cl. 3.3. The Court considered that the chief commercial object of the GSA was for Verve to secure a daily supply of gas up to a certain quantity (the MDQ) and for the Sellers to have an assured annual price (the AMQ). The Court contrasted this chief purpose, which involved unconditional obligations, with the supplementary purpose of providing for the supply of the SMDQ, a conditional obligation. Clause 3.3 provided for a balancing of interests if the business interests of the parties in respect of the supply of SMDQ do not entirely coincide, or if they conflicted.

Verve had contended, and the Court of Appeal had accepted, that:

- the reference in cl. 3.3(b) to the Sellers' "ability" to supply the SMDQ was confined to the Sellers' capacity to supply the SMDQ; and
- the Court of Appeal had also held that cl. 3.3(a) obliged the Sellers to use reasonable endeavours to deliver the SMDQ and that cl. 3.3(b) merely set out

> the factors which the Sellers could take into account to inform their obligation under cl. 3.3(a).

The High Court rejected both of these arguments. First, the Sellers' "ability" to supply the SMDQ involved a consideration of both the Sellers' capacity and business interests. Second, cl. 3.3(b) did not merely set out the factors relevant to the obligation to use reasonable endeavours, but rather cl. 3.3(b) conditioned this obligation on the balancing of the Sellers' responsibility to Verve and their own business interests. The standard of reasonableness was informed by this balancing exercise and in light of the surrounding circumstances known to both parties at the time of entering the GSA. These circumstances included that the Sellers sold and supplied gas to customers and buyers in the market other than Verve, that some essential services depend on gas supply, and that the prevailing market price of gas at any particular time may be greater than the price for the SMDQ provided for by the GSA.

In all the circumstances, the Court held the standard of reasonableness did not oblige the Sellers to supply SMDQ to Verve when the Apache incident occasioned business conditions (being the Sellers' ability to obtain a higher market price) leading to a conflict between the parties' business interests.

6.2 Liquidator's decision to reduce or vary a proof of debt not a decision to reject it

(By James Siemon, Minter Ellison)

Perrin v Williams [2014] QSC 21, Supreme Court of Queensland, Jackson J, 28 February 2014

The full text of this judgment is available online.

(a) Summary

This case examines whether a decision by a liquidator to accept a second proof of debt as superseding the previous proof of debt (and therefore to accept it as the basis for the only claim by the creditor against the company) was a decision able to be appealed under s. 1321 of the Corporations Act 2001 (Cth) (the Act). The case also examines the definition of "a person aggrieved" under s. 1321 of the Act and, therefore, examines who may bring an appeal under that section.

(b) Facts

On 3 March 2009, ACN 084 908 092 Pty Ltd (the Company) went into a creditors' voluntary winding up under Part 5.5 of the Act. On 11 March 2009, the second respondent submitted a first formal proof of debt for $21,870,363. This amount was disputed by the liquidator.

On 18 July 2013, the liquidator issued a further report to creditors, in which she stated that she would accept that the second respondent was a creditor of the Company for $6,098,464. On 7 August 2013, the second respondent executed and lodged a second formal proof of debt for that amount and, on 15 August 2013, the liquidator wrote to the second respondent, admitting the claim in full and notifying the second respondent that she would treat the second proof of debt as "superseding all earlier proofs of debt and the basis for the only claim made by [the second respondent] in the Company".

On 13 September 2013, the applicant filed an appeal under s. 1321 of the Act.

That section provides that:

1. A person aggrieved by any act, omission or decision of: ...
    d. a liquidator or provisional liquidator of a company; may appeal to the Court in respect of the act, omission or decision and the Court may confirm, reverse or modify the act or decision, or remedy the omission, as the case may be, and make such orders and give such directions as it thinks fit.

The matter came before Jackson J as a determination of separate questions prior to the appeal. His Honour therefore considered the following questions:

- whether the liquidator made any decision to reject for dividend purposes the second respondent's proof of debt submitted on or about 11 March 2009;
- whether the liquidator made a decision as to whether the proof of debt dated 7 August 2013 lodged by the second respondent was the basis for the only claim by the second respondent against the Company; and
- whether the applicant was an aggrieved person pursuant to s. 1321 of the Act.

(c) Decision

(i) The liquidator's decisions

In addressing the first two questions, Jackson J noted that the decision made by the liquidator was to accept the second proof of debt on the basis that it superseded the first proof of debt. His Honour referred to r. 5.6.56 of the Corporations Regulations 2001 (Cth) (the Regulations), which provides that "[a] proof of debt or claim may be withdrawn, reduced or varied by a creditor with the consent of the liquidator". His Honour expressed his view that, when the liquidator admitted the second formal proof of debt lodged by the second respondent, the second respondent was taken to have elected between the two proofs of debt. In treating the second proof of debt as superseding the first proof of debt, the liquidator therefore consented to the reduction or variation of the first proof of debt.

His Honour therefore found that there was no decision to reject for dividend purposes the second respondent's proof of debt submitted on 11 March 2009, but that the liquidator had made a decision that the second respondent's proof of debt dated 7 August 2013 was the basis for the only claim by the second respondent against the Company. His Honour characterised the decisions made by the liquidator as being, first, to consent to the reduction or variation of the first proof of debt under r. 5.6.56 of the Regulations and, second, to accept the second proof of debt and admit the debt. Although it was a consequence of those decisions that the first proof of debt was rejected or not accepted, his Honour found that the concept of a decision in s. 1321 of the Act did not stretch to allowing that consequence to be treated as a separate appealable decision. In particular, his Honour expressed concern that to extend the concept of a decision in s. 1321 in such a way would risk impairing the efficient administration of liquidations of this kind.

His Honour therefore ordered that the first two questions set down for determination be answered "No" and "Yes" respectively.

(ii) A person aggrieved

In relation to the third question, whether the applicant was a person aggrieved pursuant to s. 1321 of the Act, Jackson J considered the applicant's arguments that his involvement in property maintenance proceedings in the Family Court of Australia against the second respondent gave him a financial interest in her assets and also that the second respondent had assigned to the applicant the debt owed to her by the company together with her rights relating to the proofs of debt.

Noting that the applicant needed to demonstrate that he was a person aggrieved when the originating application of the appeal was filed, his Honour found that, although the applicant may have had a right to an order in the Family Court, no order had been made crystallising any rights he had to the results of the second respondent's proofs of debt against the Company. His Honour also stated that it was not sufficient that the applicant was merely "a person who is deprived of something or is adversely affected by the act", finding that this was not the test under s. 1321 of the Act. His Honour gave the example that creditors of the second respondent, although affected by a decision regarding her submitted proof of debt, would not be persons aggrieved by that decision.

Jackson J therefore found that the applicant was not a person aggrieved on 13 September 2013 and ordered that the third question be answered "No".

Jackson J continued his analysis, however, by assuming that on 11 February 2014 the second respondent retained a right to prove a debt or claim against the Company for the amount assigned to the applicant. His Honour noted that this still did not make the applicant a person aggrieved on 13 September 2013 and that any appeal brought on 11 February 2014 would have been out of time.

Furthermore, his Honour suggested that for the applicant (as assignee) to be a person aggrieved, the second respondent must also have fallen within that definition. His Honour found that a decision by a liquidator to accept a proof of debt and admit the debt would not cause the person who lodged that proof to be "aggrieved" on an ordinary use of language. However, given the scope of the questions set down for determination, he declined to proceed further to decide whether the applicant was a person aggrieved on 11 February 2014.

6.3 Multiple applications by liquidators to extend time in respect of voidable transactions

(By Rachel Loftus and Will Heath, King & Wood Mallesons)

JP Morgan Chase Bank, National Association v Fletcher; Grant Samuel Corporate Finance Pty Limited v Fletcher [2014] NSWCA 31, New South Wales Court of Appeal, Beazley P, Macfarlan and Gleeson JJA, 28 February 2014

The full text of this judgment is available online.

(a) Summary

This case concerned a liquidators' application for a further extension of time in which to make an application to the Court under s. 588FF(1) of the Corporations Act 2001 (Cth) (the Corporations Act) in respect of voidable transactions. Under s. 588FF(3), such an application must be made by the liquidator within three years of the relation-back day (s. 588FF(3)(a)), or within such longer period ordered by the Court on application by the liquidator within that three year period (s. 588FF(3)(b)).

The liquidators applied for an extension of time within the three year period required by s. 588FF(3)(b), but then sought an order varying the extension after the three year period had expired. The Court considered whether s. 79 of the Judiciary Act 1903 (Cth) (the Judiciary Act) operated in these circumstances to "pick up" the applicable state procedural rule contained in the Uniform Civil Procedure Rules 2005 (NSW) (the UCPR), namely rl. 36.16(2)(b).

Rule 36.16(2)(b) of the UCPR allows the Court to set aside or vary a judgment or order after it has been entered if it has been given or made in the absence of a party, whether or not the absent party had notice of the relevant hearing or of the application for the judgment or order.

A majority of the Court (Macfarlan and Gleeson JJA) found that s. 79 of the Judiciary Act permits the Court to rely on rl. 36.16(2)(b) of the UCPR to vary an earlier order and further extend the time for a liquidator to make an application under s. 588FF of the Corporations Act. Such a variation order can be made outside the time required by s. 588FF(3)(a), so long as the original application to extend time under s. 588FF(3)(b) was made within the three year period stipulated by s. 588FF(3)(a) of the Corporations Act. Beazley P dissented on this point.

(b) Facts

The liquidators of Octaviar made an application to the Court in respect of voidable transactions, pursuant to s. 588FF(1) of the Corporations Act.

On 30 May 2011, prior to the third anniversary of the relation-back day, Hammerschlag J made an order under s. 588FF(3)(b) to extend the time for making the application under s. 588FF(1) to 3 October 2011. JP Morgan and Grant Samuel (the Appellants), who were potentially affected by that order, were not parties to the application, nor present when the application was heard and the orders made.

On 19 September 2011, after the third anniversary of the relation-back day, Ward J (as her Honour then was) made an order under rl. 36.16(2)(b) of the UCPR to vary Hammerschlag J's order and extend the time for making an application to 3 April 2012. While the liquidators advised the Appellants of their intention to seek the variation of Hammerschlag J's order, the Appellants did not attend the hearing and no person or entity was joined as a defendant. However, the liquidators' explanation for the delay in bringing proceedings was accepted because of the complexity and magnitude of the matter.

The Appellants applied to set aside Ward J's orders. Black J dismissed the appellants' application.

The Appellants appealed the decision of Black J, arguing:

- first, that only one application for extension of time may be made under s. 588F(3)(b);
- second, that rl. 36.16(2)(b) of the UCPR does not permit an order extending time to be made; and
- third, that rl. 36.16(2)(b) of the UCPR does not empower the Court to vary an order that has been made in the absence of a person affected by the order who is not a party.

(c) Decision

(i) Multiple applications may be made under s. 588FF(3)(b) for an extension of time

The Court unanimously agreed that more than one application for an extension may be brought under s. 588FF(3), provided that each application is brought within the three year period.

(ii) Whether, pursuant to s. 79 of the Judiciary Act, rl. 36.16(2)(b) of the UCPR permits variation of an order extending time to permit a further extension of time

Macfarlan and Gleeson JJA found that the only restriction imposed by s. 588FF(3)(b) on the Court's power to extend time is that the Court's order must be "on an application" made by the liquidator during the three year time period required by s. 588FF(3)(a).

Macfarlan and Gleeson JJA found that s. 588FF(3)(b) does not require an order, as distinct from an application, to be made during the period specified in s. 588FF(3)(a). The original application was made during the required three year period. While Ward J's subsequent order to further extend the time was made outside this period, it did not conflict with s. 588FF. Ward J made her variation order "on an application" filed in conformity with s. 588FF(3)(b). As such, her Honour's order under rl. 36.16(2)(b) had been validly made.

Macfarlan JA noted, "Hammerschlag J's order extending time implicitly brought the application for extension of time to an end because what was sought by the application was achieved. That termination was subject, however, to the rules of court which were able to, and effectively did, provide for its revival in certain circumstances [such as rl. 36.16(2)(b)] ... The position would be the same if an application were made for variation of this, or any other, order under the slip rule (rl. 36.17)".

Macfarlan and Gleeson JJA relied on *Gordon v Tolcher* [2006] 231 CLR 334 as authority for the proposition that once an application for extension of time is made in conformity with s. 588FF(3)(b), the regulation of the conduct of the litigation is left for the procedural law of the state or territory court in which the application was filed, which is picked up by s. 79 of the Judiciary Act.

Beazley P, in dissent, found that the application made under rl. 36.16(2)(b) was an application "invariably" based on additional evidence calling for a fresh exercise of the discretion to extend time. Beazley P concluded that rl. 36.16(2)(b) of the UPCR, to the extent that it permits making a fresh, new or further application for an extension of time, is inconsistent with s. 588FF(3)(b) and is not picked up by s. 79 Judiciary Act (at [89] - [93]). However, corrections or amendments permitted by the "slip rule" in rl. 36.17 would be permitted.

(iii) The Court has power under rl. 36.16(2)(b) to vary an order that has been made in the absence of a person affected by the order who is not a party on the record

Beazley P, Macfarlan and Gleeson JJA agreed that the Court has power under rl. 36.16(2)(b) of the UCPR to vary an order that has been made in the absence of a person affected by the order, when the absent party is not a party on the record.

The Court considered the meaning of the word "party" in rl. 36.16(2)(b). Beazley P noted that the word "party" in procedural legislation often means "party or parties to the proceedings" in a narrow sense, although it may also be used in a broad sense to mean persons with an interest in the proceedings.

Beazley P also observed there are a variety of circumstances in which a person, not a party formally joined to the proceedings, may challenge or seek to vary orders that have been made. Macfarlan JA agreed, noting that rl. 36.16(2)(b) is remedial in that it permits the Court to exercise a broad discretion to correct a judgment or order it considers requires correction, which conforms with the statutory requirement for the Court to facilitate the just, quick and cheap resolution of the real issues in the proceedings.

6.4 Quasi-partnerships and unfairly prejudicial conduct: are share purchases which fail to comply with pre-emptive rights an act within the conduct of a company?

(By Katrina Sleiman and Shariqa Shaheed, Corrs Westgarth Chambers)

Graham v Every [2014] EWCA Civ 191, England and Wales Court of Appeal (Civil Division), Arden, McCombe and Vos LJJ, 27 February 2014

The full text of this judgment is available online.

(a) Summary

The appellant (Mr Graham) and the respondents, Messrs Every, Olsson, De Pommes, Carande and Rymer (the Respondents) are or were shareholders in a company that carries on the business of owning and operating an ice bar and restaurant (the Company). Mr Graham was removed from his position as a director of the Company and shortly thereafter petitioned the Court for relief from unfair prejudice under s. 994 of the Companies Act 2006 (UK) (the Companies Act).

At first instance, Stuart Isaacs QC (the Deputy Judge) allowed in part the Respondents' application to strike out certain allegations from Mr Graham's petition. The two allegations that were struck out were that the Respondents' actions were contrary to the common understanding between the parties when the Company had been formed (the Understanding Allegation) and that Mr Every had purchased shares in a manner that contravened a pre-emption agreement (the Non-compliant Share Purchase Allegation).

Mr Graham appealed, seeking to reinstate the parts of the petition that had been struck out. The Respondents cross-appealed and claimed that Mr Graham's petition was an abuse of process, was not properly particularised and should be struck out entirely. The Court of Appeal allowed Mr Graham's appeal, dismissed the cross-appeal, but upheld the Deputy Judge's order as to costs.

(b) Facts

Mr Graham alleged that he and the Respondents (collectively, the Joint Venturers) started the Company on the basis of a common understanding as to its business, development and operation which was documented in an agreement in 2005, but was not signed by all parties (the Heads of Agreement). The Heads of Agreement set out specific rights and obligations of the Joint Venturers in respect of the Company and stated that the business premises would be fitted out by Willowmead Ltd and Straight Impact Ltd at a budgeted cost which would be managed by certain directors. Mr Graham was not consulted in respect of certain decisions, such as the Company entering into a loan agreement with Willowmead Ltd.

In late January 2009, Mr Graham learnt that two of the Respondents, Messrs Rymer and Carande, had sold their collective 26.6% shareholding in the Company to Mr Every on or around 14 January 2009 for an uncertain sum. Later in 2009, Mr Graham was removed from his position as director. On 7 January 2010, the Respondents sent an offer to Mr Graham to buy back his entire shareholding (the Offer).

At first instance the Deputy Judge struck out part of Mr Graham's petition. His Honour held that part of the Understanding Allegation should be struck out because certain matters that Mr Graham had raised in relation to the rights and obligations of the Joint Venturers did not form part of the Heads of Agreement. His Honour also ordered that the Non-compliant Share Purchase Allegation be struck out on the basis that it could not amount to unfair prejudice and Mr Graham should have made a claim for damages for breach of contract. The Deputy Judge ordered that neither party should have their costs of the strike out application.

(c) Decision

The case concerned s. 994 of the Companies Act, which provides that:

1. A member of a company may apply to the court by petition for an order under this Part on the ground—

a. that the company's affairs are being or have been conducted in a manner that is unfairly prejudicial to the interests of members generally or of some part of its members (including at least himself), or
b. that an actual or proposed act or omission of the company (including an act or omission on its behalf) is or would be so prejudicial.

Arden LJ delivered the leading judgment. As a preliminary comment, her Honour noted that Mr Graham had accepted that his petition failed to give a large number of particulars which it ought to give. Nevertheless, Arden LJ was reluctant to make an order striking out the petition on a technical pleading point unless the substance of the allegation would inevitably fail.

(i) Was there a common understanding between the parties that went beyond the Heads of Agreement?

The Court found that the Understanding Allegation had merit because the common understanding was only partially found in the Heads of Agreement. Arden LJ said that the Deputy Judge had correctly found that of itself, the uncertainty surrounding the execution of the Heads of Agreement should not support a finding that Mr Graham has no real prospect of success. However, Arden LJ departed from the narrow approach of the Deputy Judge and stated that only using this document as the basis of the understanding between the parties was not enough.

The Court considered that the Company appeared to be a "quasi-partnership", with a number of unique characteristics, such as a small number of members, the involvement of members in the running of the business, restrictions on the disposal of shares and that profits were generally paid as remuneration. Accordingly, Arden LJ said that the Court was required to look beyond the company's memorandum and articles to extrinsic materials such as other agreements and understandings between the members to fully comprehend the question of governance, and the dynamic between the members, their rights and obligations.

(ii) Did pre-emption agreements of individual shareholders constitute an act or conduct of the company's affairs?

Her Honour stated that normally, denial of pre-emption rights for the sale of shares in a company would not constitute an act or conduct of the company's affairs for the purposes of s. 994 of the Companies Act since they are actions of shareholders in their personal capacity, and did not concern events directly involving the company. However, again due to the "quasi-partnership" nature of the Company, her Honour found that the denial of pre-emption rights was within the scope of s. 994(1) of the Companies Act. Her Honour's reasoning was that the Company remunerated its directors by dividend and not salary, such that the benefit obtained by each director was directly proportionate to their shareholding. Consequently, when Mr Graham was not informed that Messrs Rymer and Carande intended to sell their shareholding, he was denied an opportunity to exercise his right of pre-emption. When Mr Every bought the shares without giving Mr Graham this opportunity, he had interfered with the way the Company would remunerate Mr Graham and it effectively meant that was unfairly prejudicial to Mr Graham's interests as a member.

It was also noted by Vos LJ that diluting the shareholding of a member may amount to unfair prejudice to his interests, and this is the consequence of the alleged actions of the Respondents. The Deputy Judge, therefore, had asked the wrong question; his Honour should have instead asked whether the pleaded allegations, if true, were capable of establishing that the company's affairs were being or had been conducted in an unfairly prejudicial manner.

An additional point raised by McCombe LJ was that one of the problems that has beset litigation under s. 994 of the Companies Act and its predecessors, has been the tendency (to some extent to be found in this case) of engaging in satellite litigation by way of applications to strike out petitions on pre-conceived technicalities. His Honour considered that it would be artificial to strike out the Non-compliant Share Purchase Allegation on the basis that, looked at in isolation, it might not be an "act of the company", as that fails to give due regard to the general words of the section which speak of the company's affairs being "conducted in a manner that is unfairly prejudicial". In cases of this sort, his Honour considered the factual context as being of great significance.

(iii) Did the Respondents make a proper Offer and did Mr Graham's failure to accept it have a bearing on his petition?

The Court dismissed the Respondents' cross-appeal on the basis that their Offer did not comply with well-established guidelines for such offers. Lord Justice Arden cited the well established principles in *O'Neill v Phillips* [1999] 2 BCLC 1 at [16] that a court will consider when deciding whether to strike out a petition on grounds that respondent shareholders had made an offer to buy-out the petitioning shareholders. These requirements include, among others, making an offer to purchase for fair value on a *pro rata* basis, valuation by a competent expert and equal access to information. Her Honour stressed that these were important rights of members in a company, and as such, Mr Graham's failure to accept the Offer was not unreasonable.

As a final point, the Court upheld the Deputy Judge's order that there be no order as to costs.

6.5 Interpreting "on behalf of" and "for the benefit of" in unreasonable director-related transactions

(By Olivia Draudins and Daniel Davids, Corrs Westgarth Chambers)

In the matter of Wulguru Retail Investments Pty Ltd (in liquidation); Vasudevan as joint and several liquidator of Wulguru Retail Investments Pty Ltd (in liquidation) v Becon Constructions (Australia) Pty Ltd [2014] VSCA 14, Supreme Court of Victoria, Court of Appeal, Nettle, Beach JJA and McMillan AJA, 24 February 2014

The full text of this judgment is available online.

(a) Summary

The question to be determined by the Court in this case was whether a mortgage granted by Wulguru Pty Ltd (Wulguru) to the appellant, Becon Construction (Australia) Pty Ltd (Becon), a creditor of Wulguru's sole director, in consideration for a covenant by Becon not to sue the director, constituted an unreasonable director-related transaction within the meaning of s. 588FDA of the Corporations Act 2001 (Cth) (the Act).

Section 588FDA(1)(b)(iii) provides that a transaction is an unreasonable director-related transaction if it is a payment, conveyance or other disposition of property of the company made by the company to a person on behalf of, or for the benefit of, a director of the company.

The Court held that the primary judge's interpretation of the phrase "for the benefit of" was incorrect, primarily informing its interpretation of these phrases in light of the anti-avoidance purpose of s. 588FDA.

First, in considering the scope of "on behalf of", the Court did not determine this question on the basis of whether or not Becon was acting under the instructions of the director as the primary judge had. The Court instead held that the anti-avoidance purpose of s. 588FDA suggested a requirement that to be made "on behalf of" the director, a disposition must be of some benefit to the director; a disposition merely effected on a director's instructions is insufficient.

Turning to the scope of "for the benefit of", the Court suggested that the term "benefit" should be interpreted to include both direct and indirect benefits, as restricting its meaning to direct benefits only would not achieve s. 588FDA's anti-avoidance purpose. It was not necessary for the Court to rule on this issue however, as the Court held that the director had received a direct benefit. Further, the Court held that the phase "for the benefit of" should be attributed its ordinary meaning, rejecting arguments that "for the benefit of" should be restricted only to situations where a disposition results in a director being given an equitable interest. Consequently, the

Court found that contractual rights, such as the relief granted to the director under the Deed (as defined below), fell within the ordinary meaning of "for the benefit of" under s. 588FDA.

(b) Facts

Warren Thompson, the sole director of Wulguru, Richmond Commercial Pty Ltd (Richmond) and Mulgrave Commercial Pty Ltd (Mulgrave), guaranteed loans made by Becon to Richmond and Mulgrave. Richmond and Mulgrave defaulted on their obligations and Becon instituted proceedings against Mr Thompson.

On 23 February 2011, Mr Thompson, Wulguru, Richmond and Becon entered into a deed at the request of Mr Thompson under which Wulguru executed a mortgage in favour of Becon (the Mortgage) in exchange for Becon agreeing to discontinue the proceedings against Mr Thompson (the Deed).

On 28 November 2011, Wulguru entered into a contract to sell the mortgaged property to a third party. Wulguru became insolvent on 21 March 2012, before the proceeds of the sale were distributed. Wulguru's liquidators (Liquidators) sought to prevent Becon from obtaining the proceeds from the sale of the mortgaged property, claiming that the entering into the Deed and the granting of the Mortgage (the Transactions) were unreasonable director-related transactions under s. 588FDA.

At first instance, the primary judge held that the Transactions were neither "on behalf of" nor "for the benefit of" Mr Thompson. The Liquidators had claimed that the Transactions were entered into "on behalf of" Mr Thompson as they were entered into on Mr Thompson's instructions. However, the primary judge held that for the Transactions to be "on behalf of" Mr Thompson, Mr Thompson's instructions to enter the Transactions needed to be given to and acted upon by Becon, which had not occurred. Further, the primary judge held that for the Transactions to be "for the benefit" of Mr Thompson, Becon's holding of the Mortgage needed to be for the active benefit of Mr Thompson, and not a benefit that was merely derived by Mr Thompson from the Transactions.

The Liquidator appealed on these two issues, mounting substantially the same arguments, being that the Transactions were made:

- "on behalf of" Mr Thompson, as the Transactions were entered into and executed on his instructions; and
- "for the benefit of" Mr Thompson, as the Transactions had the benefit of relieving him of his obligations as surety to Becon.

(c) Decision

(i) Whether the Transactions were "on behalf of" Mr Thompson

The Court dismissed the Liquidator's first argument, finding that the requirement that a disposition be made "on behalf of" a director requires something more than it being effected merely on the instructions of the director. Rather, by reference to the anti-avoidance purpose of s. 588FDA (as set out in the Act's explanatory memorandum) the Court held that the use of the phrase suggested an additional requirement that there be some benefit granted to the director by the disposition.

(ii) Whether the Transactions were "for the benefit of" Mr Thompson

The Court considered the scope of the term "benefit" in the context of the anti-avoidance purpose of s. 588FDA and its aim of preventing directors from stripping benefits out of companies to their own advantage. On this basis, the Court suggested that the term "benefit" should not be confined to direct benefits only, but should encompass both direct and indirect benefits. However, the Court did not need to rule on this issue as it was held that the relief of Mr Thompson's surety obligations, as granted by the Transactions, constituted a direct benefit. In this respect, previous decisions which suggested s. 588FDA did not apply to indirect benefits were therefore distinguishable.

The Court then turned to the question of how broadly "for the benefit of" should be interpreted. Becon advanced several arguments for a restricted interpretation of "for the benefit of". Becon relied upon statements made in *Re Great Wall Resources Pty Ltd (in liq)* [2013] NSWSC 354 in support of the view that there must be an equitable interest in favour of that person in order for a transaction to be "for the benefit of" a person, not just a financial interest or mere contractual right. The Court rejected this argument as it considered this interpretation restricted the meaning of "for the benefit of" in a way that did not aid the purpose of s. 588FDA. In this respect, the Court also noted that the ordinary meaning of "for the benefit of" (for the advantage, profit or good of), which included legal or financial advantages, better accorded with s. 588FDA's anti-avoidance objectives.

Becon also advanced various "floodgate" arguments to the effect that allowing such a broad interpretation of "for the benefit of" would put too great a range of transactions at risk of being voided as unreasonable director-related transactions. The Court dismissed these arguments as baseless, again noting that the anti-avoidance purpose of s. 588FDA encouraged a broad interpretation.

(iii) Outcome

Given that prior to the Deed, Mr Thompson alone was liable to Becon, and as the Deed conferred no corresponding advantage on Wulguru in exchange for the Mortgage, the Court of Appeal held that no reasonable person in Wulguru's circumstances would have entered into the Transactions. Consequently, the Court of Appeal voided the Transactions under s. 588FF of the Act.

6.6 A company not permitted to appear without a legal representative

(By Kathy Ge, Ashurst)

Ilford Tower Pty Ltd v Equity One Mortgage Fund Ltd [2014] VSCA 16, Supreme Court of Victoria, Court of Appeal, Warren CJ, Tate JA and Sifris AJA, 21 February 2014

The full text of this judgment is available online.

(a) Summary

Ilford Tower Pty Ltd (Ilford Tower) and Teresa Dinc, the first and second appellants, were found by the trial judge to have defaulted on two separate loan agreements with Equity One Mortgage Fund Ltd. The appellants, through their solicitors, filed a notice of appeal. However at the commencement of the appeal, the solicitors were granted leave to cease to act on the basis that they had not been paid by the appellants.

Mr Strangio, the sole director of Ilford Tower then sought leave to appear on behalf of the company in order to continue to advance the appeal on its behalf. The Court refused Mr Strangio's application.

In considering whether to allow Mr Strangio's application, the Court considered rl. 1.17(1) of the Supreme Court (General Civil Procedure) Rules 2005 (Vic) (the General Civil Procedure Rules) which states that: except where otherwise provided by or under any Act or these Rules, a corporation, whether or not a party, shall not take any step in a proceeding save by a solicitor. The Court held that circumstances in this case did not warrant departing from the rule that a company will not be permitted to appear without a legal representative.

(b) Facts

In 2009, the appellants entered into two separate loan agreements with Equity One Mortgage Fund Ltd (Equity One). Both loans were secured by a mortgage over the same land and both loans were guaranteed by Ms Dinc. The trial judge awarded judgment for Equity One. The appellants' solicitors filed a notice of appeal that identified 15 grounds of appeal. As mentioned in the summary above, at the commencement of the appeal, the appellants' solicitors were granted leave to cease acting on the basis that they had not been put in funds. The Court of Appeal granted this leave for the solicitors to cease acting and the solicitors withdrew from the matter.

At this point, Mr Strangio sought leave to appear on behalf of Ilford Tower so as to continue to advance the appeal on its behalf.

(c) Decision

The Court refused Mr Strangio's application to appear on behalf of the company.

The Court considered rl. 1.17(1) of the General Civil Procedure Rules which requires a corporation to not take any steps in a proceeding without a legal representative and stated a number of reasons why the Court would not depart from rl. 1.17(1) in this case.

The Court considered the list of factors given by Forrest J in *Worldwide Enterprises Pty Ltd v Silberman* (2010) 26 VR 595. For the present case, the complexity of the issues involved and the significant challenges Mr Strangio would face in prosecuting the appeal, and the fact that the burden on the Court and the respondent would be substantially increased if he were given leave to do so, meant that in the Court's view, it would not be appropriate to depart from the rule in this case.

The starting point is that a company will not usually be permitted to appear without a legal representative and will require leave to do so. For the administration of justice, those permitted to appear before it owe a responsibility to the Court to ensure that the Court is properly informed and not misled. A proceeding conducted by a person unskilled in advocacy tends to last longer and to cost more. In determining whether to allow such an advocate to appear, the Court must have regard not merely to the position of the party for whom he seeks to appear, but also to that of the other party.

It was apparent that Mr Strangio had little grasp of how to present factual material in a way admissible to the Court. He would face significant difficulties in prosecuting the appeal himself.

The Court had reservations that Mr Strangio had authority to act for Ilford Towers—while he was the sole director of the company, the majority of the shares were not owned directly by Mr Strangio. Furthermore, the Court stated that even if they accepted Mr Strangio had the requisite authority, there were a range of other factors which should be considered in order to warrant a departure from rl. 1.17(1).

Mr Strangio informed the Court that the company had sufficient funds to obtain representation. He submitted that its reluctance to obtain alternative representation was because he had doubts about the willingness of solicitors and counsel generally to follow the company's instructions in relation to the conduct of the appeal.

6.7 Liquidators do not have an obligation to retain an amount for any income tax liability associated with a capital gain from the realisation of assets in the absence of a tax assessment

(By Emanuel Poulos and Mabel Koo, Ashurst)

Australian Building System Pty Ltd v Commissioner of Taxation [2014] FCA 116, Federal Court of Australia, Logan J, 21 February 2014

The full text of this judgment is available online.

(a) Summary

The liquidators of Australian Building Systems Pty Ltd (ABS) lodged an objection to a private ruling made by the Commissioner regarding s. 254 of the Income Tax Assessment Act 1936 (Cth) (the ITAA 1936). The Commissioner ruled that the liquidator was required to account out of the proceeds of sale, for any capital gains tax (CGT) liability that crystallises on the sale of an asset that belonged to the company before liquidation.

The Commissioner subsequently disallowed the liquidators' objection.

The liquidators appealed the Commissioner's ruling and also sought a declaration that they were not required under s. 254 of the ITAA 1936 to retain sufficient money to pay such tax, if any, which is or will become due as a result of the disposal of the asset. Their appeal was successful.

Among other things, the Court held that there is no obligation on liquidators to retain an amount for any income tax liability associated with a capital gain from the realisation of assets in the absence of a tax assessment. However, the Court did caution that a prudent liquidator would be "entitled" to retain the gain, even in the absence of a tax assessment, until the income tax position in respect of the tax year in which the CGT event had occurred had become certain by the issuing of an assessment or other advice from the Commissioner.

(b) Facts

On 6 April 2011, the creditors of ABS, which was in voluntary administration, resolved that the company be wound up. The liquidators of ABS sold one of the company's assets, being real property located south of Brisbane. This was a capital gains tax event, but no tax assessment for the tax year in which the CGT event occurred had been issued.

The liquidators sought a private ruling from the Commissioner to confirm:

- whether s. 254 of the ITAA 1936 required them to account to the Commissioner out of the proceeds of sale for any CGT liability associated with the sale of an asset that belonged to the company before the company went into liquidation; and
- assuming the liquidators were required to account for any tax liability, whether a requirement to retain monies arose at the time an assessment was issued or at the time the capital gain "crystallised".

Section 254 of the ITAA 1936 essentially provides that an agent or trustee (which includes a liquidator or receiver):

- is answerable as taxpayer in respect of the income, or any profits or gains of a capital nature, derived by him or her in his or her representative capacity, or derived by the principal by virtue of his or her agency, and for the payment of tax thereon;
- shall make the returns and be assessed thereon;
- is authorised and required to retain out of any money which comes to him or her in his or her representative capacity so much as is sufficient to pay "tax which is or will become due" in respect of the income, profits or gains; and
- is made personally liable for the tax payable in respect of the income, profits or gains to the extent of any amount that he or she has retained, or should have retained, but he or she shall not be otherwise personally liable for the tax.

The Commissioner's private ruling required the liquidators to account for any tax liability on the sale of the property and provided that the retention obligation arose at the time a capital gain crystallises and not when a tax assessment is issued. The liquidators objected to the private ruling, but this was disallowed by the Commissioner.

ABS and the liquidators challenged the correctness of the Commissioner's ruling in the Federal Court. They also raised the issue of the priority of any tax liability under s. 254 of the ITAA 1936 having regard to the operation of sections of the Corporations Act 2001 (Cth) that apply to the priority of claims in a winding up. The validity of the section was also questioned. Additionally, the liquidators sought declaratory relief against the Commissioner in respect of the obligations imposed on them by the private ruling.

(c) Decision

The Court focused on the expression "tax which is or will become due", which it considered was crucial to enlivening the retention obligation under s. 254 of the ITAA 1936.

Logan J referred to the High Court decision of *Bluebottle UK Ltd v Deputy Commissioner of Taxation* (2007) 232 CLR 598 where it was held that "due" means "assessed as owing". His Honour also referred to *Deputy Commissioner of Taxation v*

Barkworth Olives Management Ltd [2011] 1 Qd R 326, where Fraser JA observed that the expression "tax which is or will become due" is "an expression that postulates a degree of certainty about the fact and amount of the tax liability which might not be present before a notice of assessment is served".

In the present case, Logan J noted that the "taxation liability will depend upon what amount, if any, proves, at the conclusion of a given year of tax to be the taxpayer's taxable income. That amount may be far from certain at the time when the CGT event occurs".

Logan J concluded that the obligation to retain an amount for "tax which is or will become due" could only arise once a tax assessment was issued. As no assessment had yet been issued, it was held that no retention obligation arose under s. 254 of the ITAA 1936.

Logan J also cautioned that a "prudent" liquidator would, however, be "entitled" to retain the gain for a time against other expenses that might arise in the course of the administration and at the very least, would be entitled to retain the gain until the income tax position in respect of the tax year in which the capital gains tax event had occurred had become certain by the issuing of an assessment or other advice from the Commissioner.

Given the Court's conclusion, it did not have to consider the priority issue, which it held can and should await the issuing of an assessment. The Court also held that s. 254 of the ITAA 1936 was not invalid as it is solely a provision in aid of tax collection and does not impose any incontestable tax.

6.8 Authority to convey message only extends to actual message conveyed

(By Emma Newnham and David Bryant, King & Wood Mallesons)

Kilcran, in the matter of Allco Finance Group Limited (Receivers and Managers Appointed) (In Liquidation) v Gothard [2014] FCAFC 6, Full Court of the Federal Court of Australia, Besanko, Foster and Farrell JJ, 18 February 2014

The full text of this judgment is available online.

(a) Summary

The key issue in this case was whether an employee, Mr Kilcran, had been terminated by statements made by receivers and managers appointed to his employer, Allco Finance Group Ltd (AFG), and made to Mr Kilcran's superior, Mr Mansveld.

The Full Court of the Federal Court found that Mr Mansveld had authority to communicate to Mr Kilcran what the receivers and managers had actually said, no more and no less.

The Court found that the receivers and managers' statements did not amount to a termination. Accordingly, inaccurate reporting of these statements by Mr Mansveld to Mr Kilcran could not have the effect of terminating Mr Kilcran's contract of employment.

(b) Facts

Mr Kilcran was an employee of AFG. Pursuant to a management agreement between a subsidiary of AFG (the Manager) and Allco SIF Ltd (SIF), employees of AFG were, in effect, seconded by AFG to SIF for no charge.

On 27 March 2008, shortly after Mr Kilcran was seconded to SIF, Mr Kilcran was made redundant by AFG. The letter informing Mr Kilcran of this fact stated that his employment would come to an end on 27 June 2008 and promised various entitlements provided certain conditions were met.

On 27 June 2008, this letter was superseded by another agreement which provided similar entitlements, including on redundancy. The redundancy entitlements were stated to be conditional on Mr Kilcran continuing to work until the termination date, 30 June 2009 or such other date designated by AFG.

On 4 November 2008, Mr Gothard and Mr Sherman were appointed receivers and managers of AFG.

On 25 November 2008, Mr Mansveld and Mr Gothard attended a board meeting of SIF. Mr Mansveld gave evidence that Mr Gothard stated at the meeting that Mr Gothard and Mr Sherman were of the view that AFG would not continue to pay the salaries of the SIF staff, or other SIF expenses, beyond the end of November 2008.

Mr Gothard gave a different account of the meeting. His evidence was that he stated at the meeting that it did not make sense for AFG to continue to provide the services to SIF without compensation, but that he was prepared to continue to provide the services if SIF reimbursed AFG for the cost of the employees going forward.

The management agreement between SIF and the Manager was terminated on 19 December 2008. The SIF staff were paid in December 2008 by AFG.

In February 2009, Mr Kilcran lodged a proof of debt or claim with AFG claiming $273,260.03 for "Employee Entitlements", which included a redundancy claim. In June 2011, the proof of debt or claim was rejected in all respects except his claim for annual leave. The receivers rejected the claim on the basis Mr Kilcran had resigned with effect from 1 December 2008.

Mr Kilcran appealed to the Federal Court against the decision of the receivers under s. 1321 of the Corporations Act 2001 (Cth), which allows a person aggrieved by a decision of a receiver to appeal to the Court in relation to that decision. He argued his employment contract was terminated or repudiated by AFG, or that he was made redundant or constructively dismissed and that he was therefore entitled to the Employee Entitlements.

The trial judge found Mr Kilcran's employment with AFG came to an end by way of a consensual resignation and dismissed Mr Kilcran's claim.

His Honour preferred Mr Gothard's account of the conversation on 25 November 2008 and accepted that Mr Mansveld had the authority of AFG to pass on to the relevant employees, including Mr Kilcran, what he was told by Mr Gothard, but not more.

Mr Gothard had not told Mr Mansveld that the SIF staff would no longer be employed by AFG at the end of November. Whether Mr Mansveld had conveyed something different to Mr Kilcran or not, Mr Mansveld's authority extended only to accurately communicating what Mr Gothard had told him.

Mr Kilcran's arguments regarding repudiation and constructive dismissal failed for the same reasons.

Mr Kilcran appealed to the Full Court.

(c) Decision

Mr Kilcran's first group of submissions on the appeal were put on the premise that the trial judge was correct to accept Mr Gothard's account of the conversation which took place at the board meeting on 25 November 2008. The five submissions raised are discussed below.

In the alternative, Mr Kilcran also submitted that the trial judge had erred in accepting Mr Gothard's evidence and should have accepted Mr Mansveld's account of the conversation on 25 November 2008. The Court rejected the arguments raised, concluding that the trial judge had not erred in the way he resolved the difficulties associated with the two differing accounts.

(i) Mr Gothard's statements at the meeting on 25 November 2008 amounted to a termination of Mr Kilcran's employment contract

Mr Kilcran submitted there was no material difference between the two accounts of what was said and that even if Mr Gothard's account was accepted, his statements amounted to a termination.

The Full Court found that there was a material difference between Mr Gothard saying that AFG would not continue to provide the employees to SIF without charge and him saying that AFG would no longer employ the employees. Moreover, no date or time for the cessation of the existing arrangements was mentioned by Mr Gothard.

Their Honours concluded Mr Gothard's statements did not constitute express termination of Mr Mansveld and his team (including Mr Kilcran) by AFG and the receivers.

(ii) Mr Mansveld had the ostensible authority of AFG to say what he did to Mr Kilcran after the meeting on 25 November 2008

Mr Kilcran submitted Mr Mansveld had ostensible authority to communicate to his team any matter relevant to their continued employment, even if it was not something Mr Gothard had said. He relied principally on the following matters:

- Mr Mansveld was a senior executive of AFG and the chief executive officer of SIF. He was Mr Kilcran's superior with authority to communicate with him on employment matters;
- the receivers had advised employees that reporting lines would remain the same during the receivership;
- Mr Mansveld had actual authority from AFG and the receivers to pass on to his team what Mr Gothard said at the meeting on 25 November 2008; and
- the CEO of AFG had emailed employees, including Mr Kilcran, on 13 November 2008 informing them they would be informed by their manager and HR as and when their employment finished.

The Full Court found Mr Mansveld did not have general authority to make statements on behalf of AFG and the receivers. He did not have general authority as to the manner and content of statements made to his team. Mr Mansveld was authorised to communicate the specific conversation he had with Mr Gothard and nothing more.

(iii) Mr Gothard's account amounted to a repudiation of the employment contract or constructive dismissal of Mr Kilcran

Mr Kilcran's submission that Mr Gothard's statements made on 25 November 2008 amounted to repudiation was rejected by the Court for the same reasons the argument that Mr Kilcran had been terminated by those statements was rejected.

(iv) Mr Kilcran had been made redundant

Mr Kilcran submitted as an alternative case before the trial judge that he had been made redundant on 30 November 2008 or, alternatively, 19 December 2008.

The trial judge considered it difficult to accept these arguments, firstly, because the management agreement was not terminated until 19 December 2008 and, secondly, because to accept that Mr Kilcran became redundant on 19 December 2008 left unexplained why Mr Kilcran's own evidence that he ceased employment at the end of November should be rejected.

The Court noted Mr Kilcran had not raised any errors with the trial judge's reasons.

(v) The trial judge erred in his construction of Mr Kilcran's contract of employment

The Court found that the letter dated 27 June 2008 clearly required Mr Kilcran to continue to work until the termination date to be entitled to the employment benefits on redundancy. Mr Kilcran did not work until the termination date, 30 June 2009, and on the findings of the trial judge, the receivers did not specify an earlier termination date. Mr Kilcran's arguments on the construction of the contract accordingly failed.

6.9 Breakdown of a family quasi-partnership leading to a successful petition for winding up

(By Louis Italiano, DLA Piper)

Harding v Edwards [2014] EWHC 247 (Ch), England and Wales High Court (Chancery Division), Rose J, 14 February 2014

The full text of this judgment is available online.

(a) Summary

This case concerned a petition seeking an order to wind-up a company pursuant to s. 122(1)(g) of the Insolvency Act 1986 (UK) (the Insolvency Act).

In deciding that it was just and equitable to wind up the company, Rose J considered:

- that the company was a family business that had been run as a quasi-partnership;
- evidence of longstanding disputes between shareholder-directors;
- that the distributions of shareholdings had resulted in the company being deadlocked; and

- the fact that there was no viable alternative to winding up.

(b) Facts

Sally Harding and Rosemary Walton (the Petitioners) were sisters and shareholders and directors of the company Brand & Harding Ltd (the Company), which operated a farm of 242 acres in Cambridgeshire. The First Respondent was the Petitioners' elder sister, Elizabeth Edwards (Mrs Edwards), who was also a shareholder and director of the Company.

The Second Respondent, also a shareholder in the Company, was Mrs Janet Harding (Mrs Harding), who was the sisters' mother and suffered from dementia and Parkinson's disease and was appointed a Court of Protection Deputy. The Third Respondent was a shareholding trust (the Trust) that had been established under the will of the three sisters' father. The trustees of the Trust included Mrs Edwards' husband Edmond Edwards (Mr Edwards) and Mrs Harding.

The relationship between the Petitioners and Mrs Edwards deteriorated throughout worsening disputes between the parties from 2002. The Petitioners and Mrs Edwards were unable to reach agreement on matters relating to the future governance of the Company and the Petitioners therefore brought a petition to have the Company wound up on the basis that it was just and equitable to do so under s. 122(1)(g) of the Insolvency Act.

The petition was actively opposed only by Mrs Edwards, who argued that the Company was profitable and successful and that she was able to run it autonomously for the benefit of all the parties.

(c) Decision

In reaching the decision that it was just and equitable that the Company be wound up pursuant to s. 122(1)(g) of the Insolvency Act, Rose J noted that the apposite questions to be considered in the circumstances were derived from the dicta of *Lord Wilberforce in Ebrahimi v Westbourne Galleries* [1973] AC 360, as extracted in the subheadings below.

(i) Was the Company intended to be run as a quasi-partnership?

Rose J held that as shares in the Company had always been held by family members and its business was a family farm, there could be no doubt that the Company was intended to be run as a quasi-partnership.

(ii) Was the Company in fact run as a quasi-partnership?

Mrs Edwards disputed that the company was in fact run as a quasi-partnership on the basis that the Petitioners had shown little interest in running the Company since 2002.

However, Rose J considered the Petitioners' presence and active participation at annual shareholder and director meetings evidenced that they remained involved in the management of the Company to the extent that could be reasonably expected of them having regard to the way the Company had been run. Her Honour therefore found that the Company was in fact run as a quasi-partnership.

(iii) Were there grounds for the Court to intervene in the affairs of the Company?

Rose J noted that the primary area of dispute between the parties was whether there were grounds for the Court to intervene in the affairs of the Company on the basis of a company deadlock, improper management or a breakdown of mutual trust and confidence among quasi-partners.

Rose J pointed to four factors relating to the parties' business relationship that demonstrated the Court had grounds to intervene in the Company's affairs"

- there had been an ongoing dispute between the parties over who should act as the Company's accountant and in particular whether it was appropriate for Mr Edwards to be engaged in such a role. Her Honour regarded this dispute to be an important instance of the shareholders and directors being unable to disentangle personal animosities from a decision that should be a straightforward matter for a small company;
- the Petitioners and Mrs Edwards were embroiled in a longstanding dispute over access to the Company's records held at its registered office, which was Mrs Edwards' residential address. Her Honour considered that the parties' behaviours in relation to the dispute evidenced the "unhealthy state of the management of the Company";
- Mr and Mrs Edwards had purported to hold shareholder and director meetings in the absence of the Petitioners in attempts to remove the Petitioners as directors and to appoint Mr Edwards as a director of the Company. Her Honour considered that these attempts demonstrated that the future of the Company was likely to be marred by such "unconstructive attempts to oust the Petitioners from the Company when they do not want to be ousted"; and
- a deadlock had been created by the distribution of shareholdings in the Company. Substantial shareholdings of the company were held by Mrs Harding and her Court of Protection Deputy had declined to be involved in company decisions. Further, Mr Edwards purported to exercise the voting rights of the Trust shares to vote in accordance with Mrs Edwards at Company meetings despite evidence to suggest that the other trustees did not support this. Her Honour considered the state of the shareholdings to be "a recipe for decisions being taken and challenged and having to be reversed" that had rendered the Company "truly deadlocked".

(iv) Was there an alternative to winding up the Company?

Rose J found that there was no alternative to winding up the Company that the Petitioners were unreasonably refusing to pursue. Her Honour noted that while the Petitioners had acknowledged that they would reluctantly be prepared to sell their shares, Mrs Edwards had offered them only a "wholly unrealistic" proposal lacking in essential details including the share price.

(v) Should the Court's discretion be exercised to wind up the Company?

In considering whether to exercise the Court's discretion to wind up the Company, her Honour considered that the history and relationship between the Petitioners and Mrs Edwards indicated that there was no prospect of matters improving. Her Honour therefore held that it was just and equitable that the Company should be wound up and granted the petition under s. 122(1)(g) of the Insolvency Act.

6.10 Strict compliance of procedural requirement necessary to effect transfer of shares or appointment of a company director

(By Amy Wei, Ashurst)

In the matter of Motasea Pty Ltd [2014] NSWSC 69, Supreme Court of New South Wales, Black J, 14 February 2014

The full text of this judgment is available online.

(a) Summary

This case demonstrates the need for strict compliance by companies and their members with the Corporations Act 2001 (Cth) (the Act) and any relevant clauses of the company constitution to effect a valid transfer of shares or appointment of a director.

The present case involved close family members who consistently conducted the family business on an informal basis. Black J found that despite the existence of some documentary evidence supporting purported transfers of shares to and the appointment as director of Janine Gooley (the Plaintiff), and irrespective of whether the members held common intentions, the transactions were invalid for falling short of satisfying the requirements prescribed by the Act and the company's constitution.

As Black J stated:

> I do not consider that the Court is bound by the parties' agreement in that regard if it is contrary to the evidence and the requirements of the Corporations Act and the Company's constitution ...

(b) Facts

Motasea Pty Ltd (the Company), the first defendant in these proceedings, was incorporated in December 1988, at which time Bill Gooley (the Second Defendant) and his late wife each held one share. In 1997, prior to Mrs Gooley passing away, she purportedly transferred her share to the Second Defendant. However, the relevant minutes of meeting, signed transfer and share certificate could not be located.

(i) Plaintiff as shareholder of the Company

The Plaintiff, also Mr and Mrs Gooley's daughter, claimed she first became a shareholder in the Company in May 2000, evidenced only by an annual return of the company that was lodged with the Australian Securities and Investments Commission (ASIC) which recorded the Plaintiff and the Second Defendant as each holding a share in the Company. Subsequent annual returns and minutes of general meetings also recorded the Plaintiff as a shareholder, although none of these were signed by the Second Defendant or lodged with ASIC, and there was no evidence any of the general meetings actually took place.

In January 2013, the Second Defendant lodged a request for correction with ASIC in respect of the 2000 annual return, asserting that the information in it which indicated that the Plaintiff was a shareholder was, in fact, false.

(ii) Plaintiff as director of the Company

The Plaintiff also claimed that she is, and remains a director of the Company. It was common ground between the parties that the Plaintiff was appointed as a director of the Company in 2000, and subsequently removed as a director in late 2010. According to evidence presented by both the Plaintiff and the Second Defendant, the Plaintiff was reappointed as a director of the Company at a general meeting in October 2012. The dispute lies in the legal validity and effectiveness of the Second Defendant's attempt in February 2013 to again remove the Plaintiff as a director of the Company. The Plaintiff claimed that a document lodged with ASIC recording that she had ceased to be a director, and a minute of resolution of a sole member of the Company purporting to remove her as a director signed by the Second Defendant were both of no force or effect, as she was also a member of the Company and was not notified of the meeting that took place for the purpose of removing her as a director.

(iii) Orders sought

Based on the above facts, the Plaintiff sought a declaration that she is and remains a shareholder and director of the Company, and in the alternative, an order that the Defendants be estopped from asserting the contrary.

(c) Decision

The Plaintiff's application was dismissed and the Plaintiff ordered to pay the Defendants' costs of the proceedings.

(i) Whether the Plaintiff is a shareholder of the Company

The Court found the evidence did not support a finding that the Plaintiff became a shareholder in the Company in 2000, and the Plaintiff therefore could not have been a shareholder at the time of these proceedings.

Black J emphasised that whether a person is a member of a company is determined under s. 231 of the Act and any relevant clauses of a Company's constitution, irrespective of what was in an agreement between the Company and the individual.

The Court found that in the present case, the necessary procedural requirements were not satisfied in the purported transfer of the late Mrs Gooley's share to the Second Defendant, so as to allow the latter to subsequently transfer that share to the Plaintiff. There was no member's register, no executed or stamped documents evidencing or recording such a transfer and no evidence of any minute of meeting relating to any such transfer. There was also no evidence that any capital gains tax or applicable stamp duty was paid on such a transfer.

The Plaintiff also did not give evidence of the execution of a transfer of any share in the Company to her. The only piece of evidence relied on was the 2000 annual return lodged with ASIC recording her as a shareholder. The weight to be given to this, the Court found, must be determined by reference to s. 1274B(2) of the Act, pursuant to which the ASIC database, which presently records Bill Gooley as the sole owner of the two ordinary shares in the Company, constitutes the *prima facie* position. The Court did not find that the evidence presented displaced the *prima facie* position.

(ii) Whether the Plaintiff is a director of the Company

The Court found the Plaintiff was not validly appointed as a director of the Company in October 2012, and therefore could not have been one at the time these proceedings were brought.

Again, Black J found the procedural requirements were not complied with. The meeting that supposedly occurred in October 2012 appointing the Plaintiff as a director of the company was not effective as the late Mrs Gooley's estate, who held the other share in the Company, was not represented at the meeting, and thus the quorum requirement for such a meeting under the Company's constitution was not satisfied.

As the Plaintiff was not validly appointed as a director of the Company in October 2012, it was irrelevant whether the Second Defendant's attempt to remove her as a director in 2013 was valid or effective.

(iii) Estoppel claims

The Court rejected the Plaintiff's claims of both representational estoppel and conventional estoppel.

Black J found that so far as the Plaintiff relied on a representational estoppel, the element of unconscionability was not established. The Second Defendant's action of correcting the ASIC records to indicate that the Plaintiff was in fact not a shareholder, which is the true position as Black J found above, is "consistent with conscience".

In regards to the Plaintiff's submissions on a conventional estoppel, Black J found the Plaintiff did not suffer any detriment of substance. In fact, it appeared the Plaintiff obtained significant financial benefits from her involvement with the Company.

Further, Black J opined that even if estoppel were established, the appropriate form of relief is not necessarily to give effect to the relevant representation. In the present matter, any detriment suffered by the Plaintiff could be remedied by relief falling well short of an order that she be registered as a shareholder or appointed as a director of the Company.

6.11 Application to bring derivative claim under common law refused

(By Liam Hickey, Herbert Smith Freehills)

Abouraya v Sigmund [2014] EWHC 277 (Ch), England and Wales High Court (Chancery Division), Justice David Richards, 13 February 2014

The full text of this judgment is available online.

(a) Summary

Mr Abouraya and Ms Sigmund were equal shareholders in, and the only two directors of, Triangle Metals & Minerals Trading Ltd (Triangle HK).

Mr Abouraya applied to bring a derivative claim on behalf of Triangle HK and its wholly-owned subsidiary, Triangle Metals & Minerals Ltd (Triangle UK), against Ms Sigmund. The application was made under the common law rather than under the Companies Act 2006 (UK) (the Companies Act).

The High Court refused Mr Abouraya permission to bring the derivative claim. The principal basis for the refusal was that Mr Abouraya could not show that either he or Triangle HK had suffered any loss as a result of the alleged misconduct of Ms Sigmund, nor had Mr Abouraya established a *prima facie* case that Ms Sigmund had personally benefited from the alleged misconduct.

(b) Facts

The claimant Mr Abouraya and the defendant Ms Sigmund each held 50% of the shares in Triangle HK, and were the two directors of that company. Triangle UK and another company, Triangle Metals & Minerals GmbH (Triangle Switzerland), were wholly-owned subsidiaries of Triangle HK. Ms Sigmund was the sole director of Triangle UK and Triangle Switzerland.

Mr Abouraya applied to bring a claim against Ms Sigmund on behalf of and for the benefit of Triangle HK and Triangle UK. Mr Abouraya alleged that Ms Sigmund had procured the misappropriation of funds from Triangle UK to Triangle Switzerland, and had diverted a business opportunity from Triangle UK to Triangle Switzerland. (Mr Abouraya also asserted that Ms Sigmund had misappropriated some smaller amounts belonging to Triangle UK, but this submission was not pursued by the judge).

Mr Abouraya accepted that insofar as there was any loss to Triangle UK as a result of the alleged misconduct of Ms Sigmund, there was a corresponding gain to Triangle Switzerland, with the result that there was no loss to Triangle HK or to Mr Abouraya in his capacity as a shareholder of Triangle HK.

Mr Abouraya's motivation for bringing the claim in these circumstances was that he claimed to be a creditor of Triangle UK, and had commenced a separate proceeding for recovery of sums he alleged were due to him from Triangle UK. Mr Abouraya was concerned that Triangle UK would not have sufficient assets to meet any judgment in his favour. If the derivative claim were successful, Triangle UK would have additional assets to meet a judgment in Mr Abouraya's favour in the separate proceeding.

Another significant matter was that there was a dispute between Ms Sigmund and Mr Abouraya concerning the ownership of Mr Abouraya's share in Triangle HK. Mr Abouraya had agreed to transfer his share to Ms Sigmund, but had halted the process designed to register the transfer of the share. Mr Abouraya alleged this was because the contract for the sale of the share was conditional on Triangle UK repaying sums he alleged were due to him or his company. This assertion was disputed by Ms Sigmund. If Mr Abouraya's assertion could not be sustained, the agreement to transfer the share would be specifically enforceable against Mr Abouraya, and beneficial ownership of the share would therefore lay with Ms Sigmund.

(c) Decision

The application to bring a derivative claim was brought under the common law, rather than under Part 11 of the Companies Act.

There were two reasons for this:

- first, Mr Abouraya was not a member of Triangle UK, and under the Companies Act the derivative claim must be brought by a member of a company whom the cause of action is vested in; and
- second, under the Companies Act a company applying to bring a derivative claim must be incorporated in the UK, and the only member of Triangle UK, being Triangle HK, was incorporated in Hong Kong.

Given the cause of action was vested not in the company of which the claimant was a member but in a subsidiary of that company, Mr Abouraya applied to bring what is termed a "double derivative claim", which the judge held was permitted under the common law. The fact that the claimant was a member of a foreign company was no bar to the bringing of such a claim under the common law.

The judge found that in considering whether to grant permission to bring a derivative claim under the common law, regard must be had to three matters:

- first, the claimant had to establish a *prima facie* case that Triangle UK was entitled to the relief claimed;
- second, the claimant had to establish a *prima facie* case that there was conduct which amounted to "fraud" and that the wrongdoers remained in control of the company. After reviewing the authorities on the scope of "fraud" for the purposes of a derivative claim, the judge found that it was a requirement that the alleged wrongdoing resulted in a loss to the company (and hence an indirect loss to the shareholders of that company), and that the wrongdoers personally gained from their breaches of duty; and
- third, the Court must consider whether, in all the circumstances, it was an appropriate exercise of its discretion to grant permission to bring a derivative claim.

In respect of the first requirement, the judge found that on the evidence Triangle UK had a *prima facie* entitlement to relief.

However, Mr Abouraya could not establish the second requirement. Any loss to Triangle UK was offset by a gain to Triangle Switzerland. Therefore, Triangle HK, and Mr Abouraya as a shareholder of Triangle HK, had not suffered any loss as a result of the alleged misconduct of Ms Sigmund. Further, Mr Abouraya could not show a *prima facie* case that Ms Sigmund had benefited personally from the alleged breaches of duty.

There were also discretionary matters that told against granting permission to bring a derivative claim. These included that Mr Abouraya's purpose in bringing the derivative claim was to advance his interests in his capacity as an alleged creditor of Triangle UK. In addition, Mr Abouraya had commenced another claim in respect of Triangle UK, and case management considerations told against granting him permission to also bring the derivative claim. Finally, the judge also noted that there was an unresolved dispute concerning the beneficial ownership of Mr Abouraya's share in Triangle HK. The judge noted that it was close to inconceivable that the Court would give permission for a nominee shareholder to proceed with a derivative action against the wishes of the beneficial owner of the share.

6.12 Liquidators survive ASIC challenge to remove them based on lack of perceived independence and impartiality

(By Laura Hawes, Clayton Utz)

Australian Securities and Investments Commission v Franklin (liquidator), in the matter of Walton Construction Pty Ltd (In Liquidation) [2014] FCA 68, Federal Court of Australia, Davies J, 13 February 2014

The full text of the judgment is available online.

(a) Summary

The Australian Securities and Investments Commission (ASIC) was unsuccessful in its application to the Federal Court seeking the removal of Liquidators appointed to Walton Construction Pty Ltd and Walton Construction (Qld) Pty Ltd on the grounds of a perceived lack of independence and impartiality.

The Liquidators had been appointed by the Mawson Group, who had worked with these particular companies as advisors prior to their collapse and had referred a number of appointments to the Liquidators' firm previously, generating significant fees. ASIC alleged that there might be a need for the Liquidators to investigate certain transactions of the companies to which entities connected with the Mawson Group were parties and that the Liquidators might be concerned "not to bite the hand that feeds them".

The Court found that a reasonable creditor (the fair minded observer) would have a high level understanding of the liquidation process, of a liquidator's duties and responsibilities and the nature of professional referral relationships between insolvency practitioners and their appointors and, with that understanding and knowledge, would not apprehend a lack of independence and impartiality in this instance.

(b) Facts

ASIC applied to the Court for:

- an order under s. 503 of the Corporations Act 2001 (Cth) (the Act) for the removal of the Liquidators as liquidators of the companies because of an apprehension that the Liquidators might lack independence and impartiality; and
- a declaration that the "declaration of relevant relationships (DIRRI)" made by the Liquidators upon their (initial) appointment as Administrators was deficient and, on that basis, that they had contravened s. 436DA of the Act.

ASIC contended that a reasonable apprehension of lack of independence and impartiality existed because of the following matters:

- the Liquidators were first appointed as Administrators of the companies upon the referral of the Mawson Group, which provided business advisory and restructuring services to companies in financial difficulty;
- the Mawson Group, as advisors, had worked with the companies prior to their collapse;
- the companies had transacted asset sales and debt assignments shortly before they went into administration that the Liquidators would need to investigate, in circumstances where it appeared that the other parties to the transactions were companies connected with the Mawson Group, and the asset sales and debt assignments effectively resulted in the transfer of a significant part of the businesses of the companies;
- there was a need for the Liquidators to investigate whether those transactions could be challenged as uncommercial transactions or unreasonable director-related transactions, whether the directors had breached their duties and whether Mawson Group personnel were involved in such breaches, in circumstances where:
    - the Mawson Group was involved in the appointment of the insolvency practitioners who would ultimately investigate transactions to which entities connected with the Mawson Group were parties; and
    - the Liquidators' firm, Lawler Draper Dillon, had been referred six other voluntary administrations by the Mawson Group;
- the referrals from the Mawson Group had generated a substantial volume of work with significant fees for Lawler Draper Dillon; and

- in three of the other administrations, there were antecedent transfers of assets and debt assignments by the companies to entities connected with the Mawson Group.

In addition, ASIC contended that the DIRRI made by the Liquidators on their appointment as Administrators was deficient.

The DIRRI relevantly provided that "[t]he companies were referred by Mr P McCurry of Mawson Group, who refers us insolvency type matters from time to time. Referrals from solicitors, business advisors and accountants are common place and do not impact on our independence in carrying out our functions as Administrators. Other than this, there are no other known relevant relationships from the previous 24 months with the company ... [or] an associate of the company ... that should be disclosed".

ASIC contended that s. 60(1)(b) of the Act (which defines what is meant by a "declaration of relevant relationships" for the purposes of the requirement to make one under s. 436DA, the operative provision) required the Liquidators to also address, in the DIRRI, why they did not believe that the referral relationship with the Mawson Group resulted in any actual or perceived conflict of interest or duty in the context of the potential need to investigate certain transactions involving the Mawson Group, whether or not the relationship did give rise to a perceived lack of independence and impartiality.

(c) Decision

The Court found that:

- there was no substance in ASIC's claim of apprehended lack of independence or impartiality, and refused the order sought to remove them; and
- the DIRRI was not deficient and refused the declaration sought by ASIC.

The Court did not agree with ASIC's contention that the circumstances of their appointment gave rise to an apprehension of lack of independence or impartiality.

The Court applied the test of the "fair minded observer" and said:

> The fair minded observer, appropriately informed, would know that the liquidators' firm is commonly referred voluntary administrations and other insolvency work by solicitors, business advisors and accountants and would know that this was the nature of the firm's business relationship with the Mawson Group. The fair minded observer would also know that the Mawson Group is a business advisory firm providing corporate restructuring advice to troubled companies, and that its relationship with the companies was a professional one. The fair minded observer, appropriately informed, would also know that there is nothing about the conduct of the other insolvencies referred by the

> Mawson Group to the liquidators' firm that brings the firm's independence and impartiality into question having regard to their professional relationship with the Mawson Group. With such an appreciation, the fair minded observer may reasonably conclude that the liquidators would similarly discharge their statutory duties and responsibilities impartially and as required by law in the conduct of the liquidations in issue, uninfluenced by their relationship with the Mawson Group. Moreover, the fair minded observer, appropriately informed, would also know that if there was any deficiency in the DIRRI, such deficiency (if that be the case) was inadvertent and not intended. It is therefore difficult to perceive how in that circumstance, there should be some "heightened" apprehension of lack of independence and impartiality.

In relation to the DIRRI, the Court found that:

- s. 60 of the Act prescribes quite clearly that a DIRRI must state whether the administrator or his or her firm has, or has had (within the preceding 24 months), "a relationship" with the company or, relevantly, its associates and, if so, the administrator must state his or her reasons for believing why that "relationship" does not "result in" the administrator "having a conflict of interest or duty";
- the Liquidators had disclosed their firm's business association with the Mawson Group and explained why the referral relationship did not compromise their independence in carrying out their function as Administrators;
- ASIC's contention that the Liquidators were required to address why the need for investigation did not result in any conflict was no more than to state a conclusion about the possibility of a conflict of interest or duty because of the relationship with the Mawson Group; and
- the need to investigate the Mawson Group was a matter pertaining to the performance of the Liquidators' duties and did not objectively add anything further as to whether the existence of the association with the Mawson Group may give rise to any conflict of interest or duty or might be seen to undermine their independence.

6.13 Reinstatement of a director after disqualification for convictions

(By Annabel Humphreys, Minter Ellison)

Re Colin Gregory Ryan [2014] QSC 18, Supreme Court of Queensland, Lyons J, 10 February 2014

The full text of this judgment is available online.

(a) Summary

This case provides an example of where the Court will exercise its discretion under s. 206G of the Corporations Act 2001 (Cth) (the Corporations Act) to grant leave to a person who is disqualified from managing a corporation to manage a particular corporation. The relevant factors the Court may consider include the person's character and protecting the public from the risk of inappropriate or improper management of a corporation.

(b) Facts

Colin Gregory Ryan was a director of the publicly listed New Zealand company Capital+Merchant Finance Ltd (CMF). Three of CMF's directors were executive directors and New Zealand residents, and the other two, including Mr Ryan, were non-executive directors and Australian residents. CMF was a finance company which funded its operations by investments made by members of the public.

During the course of his directorship, Mr Ryan signed two prospectuses containing untrue statements, and CMF issued advertisements that also contained untrue statements. This caused Mr Ryan to commit offences under s. 58 of the Securities Act 1978 (NZ) (the NZ Securities Act).

It was a defence to all three charges that Mr Ryan had an honest belief in the truth of the statements. Mr Ryan did not, however, have reasonable grounds for that belief, and it was on that basis he pleaded guilty and was convicted. The sentencing judge held Mr Ryan's conduct in relying on the three executive directors for the truth of the statements amounted to gross negligence.

Prior to being convicted, Mr Ryan was a director and executive chairman of an Australian company, CMI Ltd (CMI). As a consequence of his convictions, Mr Ryan was automatically disqualified from managing a corporation in Australia for a period of five years pursuant to s. 206B of the Corporations Act, and accordingly ceased to be a director of CMI.

Mr Ryan applied to the Court for leave, pursuant to s. 206G of the Corporations Act, to manage:

- corporations generally; or
- any company of which Mr Ryan and his wife are the only members and CMI.

Section 206G of the Corporations Act provides that a person who is disqualified from managing a corporation may apply to the Court for leave to manage corporations or a particular corporation if the person was not disqualified by ASIC. The Court may grant leave subject to conditions.

(c) Decision

Lyons J granted leave to Mr Ryan to manage CMI on the condition that leave is to cease:

- if there are less than 4 directors of CMI, not including Mr Ryan, for a period of 14 days or more; or
- should CMI make an offer of, or issue, debentures to members of the public in order to use the money obtained through such an issue for investment purposes.

Lyons J refused to grant leave to Mr Ryan to manage corporations generally or any company of which Mr Ryan and his wife were the only members.

In deciding the application, Lyons J referred to the principles and relevant considerations set out by Gordon J in *Duffy, Re Westgate Ports Ltd* [2010] FCA 608. His Honour particularly focused on the legislative policy being one of protecting the public from the risk of inappropriate or improper management of a corporation, as opposed to punishing the offender. His Honour did, however, take into account that where a statutory provision imposes an automatic disqualification, this has a punitive aspect to it, and it follows that a grant of leave involves some abatement of punishment.

The fact that investments were made pursuant to the two prospectuses containing untrue statements was considered to be of considerable significance to the application. His Honour considered the nature of Mr Ryan's involvement as non-executive director, as opposed to executive director, did not diminish the seriousness of the conduct that resulted in Mr Ryan's convictions. His Honour considered these factors should be weighed in the context of Mr Ryan's general character and risk of reoffending.

Lyons J noted the offences were not committed for the applicant's personal profit and that the application was supported by the board of CMI. Various submissions were made by former business associates of Mr Ryan which led his Honour to find that, "save for the matters which gave rise to the convictions, the applicant has been a highly skilled and effective company director for many years, with considerable commercial acumen, who has diligently discharged his duties in relation to company management".

The following factors led Lyons J to form the view that the risk of Mr Ryan reoffending was not significant enough to be a bar to granting leave:

- the offending conduct was significantly out of character;
- the sentences imposed on Mr Ryan had a great impact on him;
- Mr Ryan cooperated with New Zealand authorities;
- Mr Ryan would not have sole control of the company. In that regard, his Honour considered it was not of particular significance that Mr Ryan would be unsupervised and that a specific proposal to take part in the management of a specific corporations was not provided;
- CMI's business was quite different to the business of CMF, and it was difficult to identify a risk of loss in CMI of the kind that occurred in the case of CMF;
- Mr Ryan had a deep knowledge of the business of CMI which significantly minimised the risk of Mr Ryan offending because of his uninformed reliance on others; and
- there was no suggestion the other directors of CMI were not of good character.

A factor which further supported Mr Ryan's application was that he was able to show that it would be of benefit to CMI if he were able to take part in the management of the company, and that the board of CMI recognised this. Mr Ryan was not required to demonstrate that it was necessary that leave be granted for CMI to be able to conduct its business successfully.

His Honour considered the following matters were not of significant weight:

- that, had the offences been committed in Australia, the Court would have had the discretion to remove Mr Ryan as director, rather than this being an automatic consequence;
- conversely, Mr Ryan may have been charged with a criminal offence which, if convicted, would have resulted in his automatic disqualification; and
- Mr Ryan's age, in that he had less time available to him to be an effective director.

6.14 The transfer of shares voided as an uncommercial transaction

(By Peter Motti, Minter Ellison)

In the matter of DJG Equities Pty Ltd [2014] NSWSC 36, Supreme Court of New South Wales, Black J, 7 February 2014

The full text of this judgment is available online.

(a) Summary

This case considered whether a transfer of shares was an uncommercial transaction under ss. 588FB and 588FC of the [Corporations Act 2001 (Cth)] (the Act). The Court held in this case that the transfer was an uncommercial transaction and an insolvent transaction for the purposes of ss. 588FB and 588FC of the Act respectively. The transfer in question was declared a voidable transaction under s. 588FE of the Act.

(b) Facts

By the Originating Process filed on 26 November 2013, the Plaintiffs, in their capacity as liquidators (the Liquidators) of DJG Securities Pty Ltd (Securities) and as receivers (the Receivers) of the assets of the D&T Family Discretionary Trust (the Trust), sought a range of orders.

In this application, the Liquidators pressed a claim for a declaration that the transfer of 1,000 shares in the first defendant, DJG Equities Pty Ltd (Equities) to the second defendant, Stephen Hitchings, on 14 May 2013 (the Transfer), was voidable under s. 588FE of the Act and sought an order under s. 588FF of the Act that the transfer was void as at, and after, the date it was made.

On 16 March 2009, Securities was appointed as trustee of the Trust pursuant to a Trust Deed that entitled it to an indemnity for all liability it incurred in performing the Trust or as trustee.

The Trust Deed also limited the liability of the trustee or any officer of a corporate trustee for loss other than that attributable to dishonesty or any wilful act or omission known by the trustee or relevant officer to be a breach of trust, and did not limit the scope of the relevant indemnity.

On 14 May 2013, Securities was wound up, pursuant to a winding up application, and the Liquidators were appointed as its liquidators. On the same day, Equities lodged a Form 484 (Change to Company Details) with the Australian Securities and Investments Commission (ASIC) which purported to record the transfer of 1,000 shares in Equities from Securities to Mr Hitchings for $1.00. A covering letter dated 13 May 2013 from Equities to ASIC attaching that Form 484 stated that:

> The shareholding of DJG Equities Pty Ltd is held in trust for the DMT Family Discretionary Trust. Therefore the shares in the ASIC register are noted as not beneficially owned. Up until 29th October 2012, the trustee of the DMT Family Discretionary Trust was DJG Securities Pty Ltd up until its retirement on this date. As at 29 October 2012, a new trustee was appointed, being Craig Stephen Hitchings as trustee of the DMT Family Discretionary Trust. The shareholding of DJG Equities Pty Ltd is now held as follows:

Craig Stephen Hitchings as Trustee of the DMT Family Trust.

The Liquidators' evidence was that the Form 484 was lodged with ASIC without their knowledge, consent or authority, and that the nominal consideration alleged to have been payable by Mr Hitchings in respect of the Transfer was not in fact received by Securities or the Liquidators.

(c) Decision

The order sought by the Liquidators had two bases, first, that the Transfer was an uncommercial transaction for the purposes of s. 588FB of the Act and, second, that the transfer was an insolvent transaction of Securities which became a party to the transaction for the purpose of defeating, delaying, or interfering with, the rights of any or all of Securities' creditors on a winding up of Securities, for the purposes of s. 588FE(5) of the Act.

(i) Was the transfer an uncommercial transaction?

Section 588FB(1) of the Act provides that:

> A transaction of a company is an uncommercial transaction of the company if, and only if, it may be expected that a reasonable person in the company's circumstances would not have entered into the transaction, having regard to:
>
> a. the benefits (if any) to the company of entering into the transaction;
> b. the detriment to the company of entering into the transaction;
> c. the respective benefits to other parties to the transaction of entering into it; and
> d. any other relevant matter.

Black J referred to the decision in *Lewis v Doran* [2005] NSWCA 243, [136], where Giles JA observed that the description of an uncommercial transaction in s. 588FB(1) of the Act is "directed primary attention to a balancing of benefit and detriment of a transaction of a company". Black J noted that the question of whether a reasonable person in the company's circumstances would not have entered into the transaction is determined by "an objective inquiry by reference to the factors specified in section 588FB(1)", citing the decisions in *Tosich Construction Pty Ltd (in liq) v Tosich* (1997) 78 FCR 363, 367 and *Old Kiama Wharf Company (in liq) v Betohuwisa Investments Pty Ltd* [2011] NSWSC 823, [35] as authorities for that proposition.

His Honour noted that the Liquidators primarily relied on the timing of and amount paid for the Transfer as evidence of its uncommercial character and contended that the Transfer was at undervalue. His Honour agreed that "[t]here was no substantive financial benefit to Securities in entering the transaction, where the stated consideration was $1.00". Black J accepted the Liquidators' argument that an inference that those shares had real value could be drawn from the evidence as to Equities' assets and liabilities and from the steps taken to remove Equities from the Liquidators' control on the day that Securities was wound up.

A second factor supporting the view that the Transfer was an uncommercial transaction was, in his Honour's opinion, its practical effect in making it more difficult for Securities to exercise its right of indemnity, as former trustee of the Trust, against assets of the Trust, which his Honour viewed as particularly striking given the timing of the Transfer on the day that Securities was wound up. The Transfer created a practical impediment to the exercise of Securities' right of indemnity, so far as its effect was that the assets available to Securities to meet that right of indemnity ceased to include its interest in Equities.

For these reasons, his Honour found that the Transfer could not be explained by normal commercial practice and a reasonable person in Securities' circumstances would not have entered into that Transfer and held that it was an uncommercial transaction, for the purposes of s. 588FB of the Act.

(ii) Was the transfer an insolvent transaction?

Section 588FC of the Act provides that a transaction is an insolvent transaction of a company if, relevantly, it is an uncommercial transaction of the company and the transaction is entered into at a time the company is insolvent. His Honour found that the insolvency of Securities at the time of the Transfer could readily be inferred by, inter alia, the winding up order made in respect of Securities on the same date as the Transfer. There was no dispute that the Transfer occurred during the relation-back period under s. 588FE(4) of the Act, so that it was also a voidable transaction for the purposes of s. 588FE(1) of the Act, if it was (as Back J held) an uncommercial transaction and an insolvent transaction.

(iii) Orders and costs

Black J observed that s. 588FF of the Act allowed the Court to make any of the orders set out in the section on the application of a liquidator, where a transaction is voidable because of s. 588FE, including an order to set aside the Transfer. His Honour was satisfied that that was the appropriate relief in this case.

His Honour made orders in the form proposed by the Liquidators, namely:

- that the transfer of 1,000 shares in Equities by the Liquidators to Mr Hitchings on or about 14 May 2013 was void as at, and after, the time it was made; and
- that Equities pay the Plaintiffs' costs in respect of the declaration made in order 1 as agreed or as assessed.

6.15 Plaintiff's unsuccessful attempt to establish a Quistclose trust over funds invested for the production of a film, which were exchanged for shares, after the project failed

(By Adam Katz, DLA Piper)

China v Smith (also known as James With) [No 3] [20114] WASC 29, Supreme Court of Western Australia, Martin J, 7 February 2014

The full text of this judgment is available online.

(a) Summary

The plaintiffs were unsuccessful in establishing a "Quistclose trust" over $1,000,000 they invested for the production of a film. It was accepted that the funds were invested for a purpose mutually agreed upon, and that purpose failed, however there was no mutual intention to keep the funds separate from general assets. The investment funds were exchanged for shares as part of a capital raising scheme, and therefore the funds could become general capital of the defendant's corporation.

(b) Facts

Paul China (the first plaintiff) wrote a film script for a motion picture. His brother, Ben China (the second plaintiff), worked as a journalist in the entertainment industry. The brothers met James Smith (the first defendant), an actor, who expressed interest in producing and acting in Paul's film.

Mr Smith presented crudely drafted documents, including an investors' agreement between Ben (the Investor) and Mr Smith (the Producer). The agreement dealt with the raising of $500,000, which was to be provided by a company associated with Ben and Paul and their father, Shaun. That company, China Brothers Production Co Pty Ltd (CB Co), became the third plaintiff, whose directors were Ben, Paul and Shaun.

Mr Smith was appointed as the sole director and secretary of Tired Horses Films Holdings Pty Ltd (THFH) (the second defendant), a company established to hold funds for the purpose of producing the film. Smith held 100 ordinary shares in THFH. CB Co held 1,500,000 A class shares, which had no voting rights but enjoyed paramount dividend and winding up rights over ordinary shares.

CB Co advanced almost $500,000 in accordance with the schedule of payments of the first investor agreement.

A number of payments were made to Smith, however the largest of them ($402,028.19) was remitted to the "Company Production Account"—not to a personal bank account of Smith. These funds were received in the ANZ account of THFH.

A second investor's agreement, between an investor (CB Co) and a producer (Mr Smith), was entered into. Under the agreement, CB Co made two equal payments of $500,000 into THFH's nominated bank account. Below Mr Smith's signature as "producer" the agreement referred to "Tired Horses Films Holdings Pty Ltd".

By making three payments into the THFH ANZ account between August 2008 and May 2009, as per the two investor agreements, CB Co was in receipt of 1,500,000 A class shares in THFH.

In July 2009, there was almost $1,000,000 in the THFH ANZ account. However, despite freezing orders issued in July 2009, in August 2009 $475,000 was moved out of the THFH account into an account operated by TRI-US Entertainment Pty Ltd (the Fourth Defendant).

(c) Decision

In determining whether a Quistclose trust existed, Martin J considered:

- whether the funds advanced to THFH by CB Co were for the primary purpose of making the film;
- whether the purpose had failed; and
- whether it was the mutual intention of the parties that the funds advanced by CB Co not become part of the general assets of THFH.

In relation to the first issue, Martin J concluded that the funds advanced by CB Co to THFH were for the purpose of meeting expenses THFH incurred making the film. This was evident from the terms of the production, writing, and directing agreements. On this point, the plaintiffs emphasised the fact that CB Co's advances of $402,028.19 and then of $1 million to THFH were all made into a specific ANZ "production account"—in accordance with the two investment agreements.

In relation to the second issue, Martin J concluded that the primary purpose (of making the film) had failed.

This was evidenced by the fact that:

- there was insufficient funding to make the film;
- there was a falling out between all of the plaintiffs and Smith;
- in 2008, investors were told they would see a return in 36 months, however at the time of judgment in 2014 the film had not been made;
- freezing orders remain in place and the defendants had not attempted to challenge them after more than four years; and

- no attempt to explain the diversion of almost half the funds held in the ANZ THFH account to TRI-US Entertainment had been made.

In relation to the final issue, Martin J concluded that the funds advanced were to form part of the general assets of THFH. Martin J referred to a number of decisions in coming to this conclusion.

In *Barclays Bank Ltd v Quistclose Investments Ltd* [1970] AC 567, there was a mutual intention of the parties that the money advanced would not become part of the assets of the recipient, but were to be used exclusively for payment of dividends. It was also agreed that if the dividend could not be paid, the money would be returned.

Similarly, in *Compass Resources Ltd v Sherman* [2010] WASC 41, Beech J stated that it is not sufficient to show that the parties intended (objectively) that the monies be used only for a particular purpose. There must also be an intention that the money does not become part of the general assets of the company and be used only for the particular purpose.

Martin J found that the two investment agreements were for capital raising by THFH: A Class shares in THFH were issued in return for money. Therefore CB Co received something of value for its investment. So, unlike most Quistclose cases, this was not a case of loan funds being obtained by a borrower to be used for a purpose which subsequently fails.

The plaintiffs claimed that the existence of a specific bank account into which funds were paid, and the express recognition (in both investment agreements) that the single purpose of THFH was to produce the film, strongly supported the finding of a Quistclose trust. However Martin J characterised the subscription funds, once in the hands of THFH, as THFH's own current asset general funds. The fact that THFH was a single purpose company did not preclude this finding.

As a result, the application for declaratory relief and consequential orders implementing that relief failed.

6.16 Forgeries and the reliance on statutory assumptions in the due execution of documents

(By Deandra McDonald, Clayton Utz)

Australia and New Zealand Banking Group Ltd v Frenmast Pty Ltd [2013] NSWCA 459, New South Wales Court of Appeal, Macfarlan, Meagher and Barrett JJA, 19 December 2013

The full text of this judgment is available online.

(a) Summary

In this case, the NSW Court of Appeal considered whether ANZ could rely upon the statutory assumptions under ss. 128 and 129 of the Corporations Act 2001 (Cth) (the Act) that a guarantee had been duly executed in circumstances where two directors of the guarantor company signed the guarantee and the signature of one of the directors had been forged.

(b) Facts

ANZ was the financier for a group of companies that operated a manufacturing business. One of the group companies, Frenmast Pty Ltd (Frenmast), executed a guarantee in favour of ANZ as security for two facilities: one facility was held by another group company, Australian Fresh Confectionary Pty Ltd (AFC) and the other facility held by two of its directors, Robert Tiricovski and his wife Slavica.

The guarantee was purportedly executed by two directors of Frenmast, Robert and Vlado Tiricovski, in accordance with s. 127(1)(a) of the Act.

Section 127(1) permits a company to execute a document without using a common seal if the document is signed by:

a. two directors of the company; or
b. a director and a secretary of the company.

It was later revealed that the signature of Vlado had been forged.

ANZ relied upon the assumption under s. 129(5) of the Act that the guarantee had been duly executed by Frenmast as the document appeared to have been executed in accordance with s. 127(1). Relevantly, s. 128(1) provides that a person is entitled to make the assumptions in s. 129 "in relation to dealings with a company" and s. 128(3) provides that those assumptions may be made "even if an officer or agent of the company acts fraudulently, or forges a document, in connection with those dealings".

The primary judge held that ANZ was not entitled to rely upon an assumption that the guarantee had been duly executed because it had not had any relevant dealings with Frenmast in relation to the procuring of the guarantee. On appeal to the NSW Court of Appeal, the case focused on two primary issues. The first was whether ANZ had any dealings with Frenmast concerning the giving of the guarantee. This question required the consideration of whether there were any communications, negotiations or other steps which constituted "dealings" between ANZ and Robert Tiricovski in his capacity as a director of Frenmast concerning the giving of the guarantee in which he was purporting to act on behalf of the company; and, if so, whether he had actual or ostensible authority to engage in those communications or negotiations. The second issue concerned whether dealings are required to be with someone who has actual or ostensible authority to enter into the guarantee (as distinct from the authority to engage in communications in connection with the guarantee).

(c) Decision

(i) Were there dealings concerning the guarantee between ANZ and Frenmast?

The Court of Appeal overturned the findings of the primary judge that there had been no relevant dealings between ANZ and Frenmast. The Court noted that ANZ had sent letters of offer directed to Frenmast regarding the taking of the guarantee. These letters of offer were responded to by the signing and return of written acknowledgements by Robert Tiricovski on behalf of Frenmast. At the same time the guarantee was issued by ANZ to Frenmast for execution. The signed guarantee was then returned to ANZ by Robert as a director of Frenmast purporting to act on its behalf. The Court held that these communications constituted a dealing or dealings in relation to the taking of the guarantee.

The Court then had to consider whether Robert had actual or ostensible authority to engage in those communications on Frenmast's behalf. The Court of Appeal held in the affirmative. Historically, Frenmast had permitted Robert to manage its banking relationship with ANZ and this included receiving and responding to communications from ANZ. Frenmast submitted that even if Robert had ostensible authority to have communications with ANZ on its behalf, his actual authority did not extend to communications concerning a guarantee of the facilities of AFC and Robert and Slavica because that transaction was solely for his or their benefit and not for the benefit of Frenmast. This argument was rejected by the Court of Appeal. The Court noted that ANZ was not shown to have had notice that Robert was acting contrary to the interests of Frenmast and solely in his own interests. ANZ was entitled to assume by reason of ss. 128 and 129(4) of the Act that Robert, as a director, was properly performing his duties to the company and Frenmast is not entitled to assert that this assumption is incorrect.

(ii) Were the dealings required to be with someone having actual or ostensible authority to enter into the guarantee?

The primary judge held that even if there was a dealing between ANZ and Robert Tiricovski, it was not a relevant dealing with Frenmast because, although he was a director of Frenmast, Robert did not have actual or ostensible authority to give the guarantee on its behalf. This question focused on whether Robert was required to have actual or ostensible authority to enter into the guarantee on behalf of Frenmast as distinct from the question as to whether he had authority to merely engage in communications with ANZ in respect of the guarantee. The Court of Appeal held that the primary judge erred in his finding on this matter. ANZ did not need to demonstrate that Robert had actual or ostensible authority to enter into the guarantee on behalf of Frenmast. In order to establish that there were relevant "dealings with the company" for the purposes of s. 128 of the Act, it was sufficient that Robert had actual or ostensible authority to undertake communications and negotiations with ANZ in respect of the guarantee on behalf of the company. The Court of Appeal relied on a passage from the judgment by Hodgson CJ in *Eq in Soyfer v Earlmaze* [2000] NSWSC 1068 made with respect to an earlier observation of Gleeson CJ in *Story v Advance Bank Australia Ltd* (1993) 31 NSWLR 722 (*Story*) where it was noted:

> In fact, some protection to the company is given by the requirement that the person must be engaged in dealings with the company in the first place; which in my opinion means that there must be dealings (in the sense of negotiations or other steps in relation to a contemplated transaction) with someone on behalf of the company which are dealings authorised by the company, and the document in respect of which the assumptions may be made must be a document which is "in relation to" those authorised dealings (and I take this to extend to a document arising out of authorised negotiations or other steps). I note that in *Story* at 733, Gleeson CJ suggested that the concept of having dealings with a company must embrace purported dealings, because if the provisions only applied where the person representing the company had actual authority, they would be largely unnecessary. I take this as meaning that it is not necessary that the person representing the company have authority from the company to commit the company to the relevant transactions or execute the relevant documents; but in my opinion, it is necessary that the person have authority to undertake some negotiations or other steps, so that the dealings, in relation to which the document is executed, are properly considered to be dealings with the company.

Accordingly, ANZ was entitled to rely on the assumptions in the Act that the guarantee had been duly executed by Frenmast. The Court of Appeal concluded that there were relevant dealings concerning the guarantee between ANZ and Frenmast. Those dealings were undertaken by Robert Tiricovski in his capacity as director on behalf of Frenmast and it was within his actual or ostensible authority to do so. Frenmast was not entitled to assert that the guarantee had not been duly executed as a result of the forgery.

6.17 Document lodged at administrator's meeting did not constitute a proof of debt in liquidation

(By Jared Lynch, Ashurst)

Re Equititrust Limited (in liq) [2013] QSC 346, Supreme Court of Queensland, McMurdo J, 17 December 2013

The full text of this judgment is available online.

(a) Summary

The Supreme Court of Queensland determined that a document lodged at an administrator's meeting was not a proof of debt in a liquidation for the purposes of the Corporations Regulations 2001 (Cth) (the Regulations). A document lodged at an administrator's meeting will not constitute a proof of debt in the liquidation, at least until the creditor acts in a way towards the liquidator which puts forward the document as a proof of debt. A proof of debt or claim which may be withdrawn, reduced or varied only with the consent of the liquidator is one which the creditor has submitted to the liquidator.

(b) Facts

The receiver of the Equititrust Income Fund (the Fund) brought the action appealing a number of decisions made by the liquidators of Equititrust Ltd (in liquidation) (receivers and managers appointed) (the Company), which was the responsible entity for the Fund. The decisions were made in connection with a document submitted on behalf of the Fund to the administrators of the Company.

Prior to its liquidation, the Company was under administration. At a second meeting of its creditors it was resolved that the Company be wound up. For the purposes of that meeting, the Fund provided a document to the Company administrators, which claimed that the Company was indebted to the Fund in an amount of $537,656.57.

The Fund claimed that the document had no effect after the creditors' meeting and wished to lodge a proof of debt for an amount substantially higher than that claimed in the document. The Fund argued that the document had no effect after the creditors meeting or, in the alternative, that the Fund had withdrawn the document.

The Company treated the document as a formal proof of debt and rejected it. In response to the Fund's alternative claim, the Company argued that the document could only be withdrawn with the consent of the Company, which it had refused to provide.

(c) Decision

In construing the relevant provisions of the Act and Regulations, McMurdo J noted that the Corporations Act 2001 (Cth) (the Act) makes no provision for the proof of debts within an administration and, more specifically, for the purposes of a meeting convened under s. 439A. Nor does it empower the administrator to require the submission of a proof of debt, or a formal proof of debt, for such a meeting or any other purpose. Cases in which the view has been expressed about applying r. 5.6.23 about proofs in this context are not clearly wrong and should be accepted. The document was a formal proof of the debt or claim to the administrators within r. 5.6.23(1)(b).

The Court held, however, that the starting point is that there is no provision of the Act or of the Regulations which is in terms that a proof of debt lodged at an administrator's meeting will constitute a proof of debt as if it had been lodged with a liquidator, in the event that the company is placed in liquidation.

In construing the relevant provisions of the Act and Regulations, McMurdo J considered the following:

- r. 5.6.48 permits a liquidator to fix a day by which creditors whose debts or claims have not been admitted are to formally prove their debts or claims. If a formal proof lodged for voting at an administrator's meeting is to be treated as a formal proof in the liquidation, the operation of r. 5.6.48 would be unclear where the debt or claim has not been admitted by the liquidator;
- there is the difference between a proof of debt which is relevant to an administrator in a meeting under s. 439A and a proof of debt for a liquidation, as to the date or dates upon which a debt is said to be owing. The relevant date for the purposes of s. 554(1) is necessarily a different date from that on which the meeting under s. 439A was held;
- further, the liquidator must have a statement that the company was not only indebted to the creditor as at the relevant date, but remained indebted as at the date of the proof of debt;
- r. 5.6.49 provides that a formal proof of debt is to be delivered or sent to the liquidator. A proof lodged with the administrator, as the chairperson of a meeting under s. 439A, would not satisfy r. 5.6.49 unless subsequently the document was delivered or sent by the creditor to the liquidator. It follows that a proof of debt or claim which may be withdrawn, reduced or varied only with the consent of the liquidator is one which the creditor has submitted to the liquidator; and
- consequently a proof of debt for voting purposes at a meeting under s. 439A could not comply with the requirement of r. 5.6.49(2).

Following the reasoning in *Derwinto Pty Ltd (in liq) v Lewis*, McMurdo J decided that it would be problematical to give a proof of debt which has been lodged with an administrator, and subsequently rejected by the administrator, an ongoing effect as a proof of debt lodged with a liquidator.

Accordingly, a document will not be a proof of debt in and for the purposes of a liquidation, at least unless the creditor acts in a way towards the liquidator which effectively puts forward the document as a proof of debt intended to be assessed by the liquidator. Otherwise a proof of debt lodged at an administrator's meeting will not constitute a proof of debt in the liquidation.

6.18 Assessing solvency where a company is dependent on loans repayable on demand

(By Robert Prosser, Herbert Smith Freehills)

International Cat Manufacturing (in liq) v Rodrick [2013] QCA 372, Supreme Court of Queensland, Court of Appeal, Holmes, Gotterson and Morrison JJA, 10 December 2013

The full text of this judgment is available online.

(a) Summary

This case concerns whether International Cat Manufacturing Pty Ltd (the Company) was insolvent at the time a charge was granted over the Company's assets. The Court held that the Company was not insolvent because, at the relevant time, it was being provided with loans which provided sufficient working capital for the Company to meet its debts as and when they fell due.

(b) Facts

The appellant Company operated a business building catamarans. The Company was incorporated in March 2002 with Ms Sarah Morrin and her husband, Mr Justin Coghlan, as its directors.

Mr Raymond John Rodrick (the first respondent) was an early customer of the Company; through his company Nu-Log Pty Ltd (Nu-Log) (the second respondent) he contracted for the construction of a boat. In addition, Mr Rodrick played an increasingly prominent role in the operations and management of the Company from early 2003 until the eventual appointment of receivers to the company in August 2005.

During this period both Mr Rodrick and Nu-Log were lending money to the Company. However, by November 2003 the Company's need for funds was such that without further financial support from Nu-Log it would have become insolvent. Accordingly, Mr Rodrick arranged for Nu-Log to provide a loan to the Company in exchange for a charge (the Charge) to secure the debt. Subsequently, Nu-Log provided further funds to the Company and also received repayments on the loans. It was common ground between the parties that the viability of the Company depended on the funds being provided by Nu-Log and Mr Rodrick.

Eventually, Mr Rodrick and Ms Morrin had a series of disagreements regarding the way in which the business was being conducted and the repayment of the loan to Nu-Log. In August 2005 Nu-Log appointed receivers to the Company pursuant to the charge and in September 2005 the Company went into liquidation.

(c) Decision

(i) The Company was not insolvent at the time the charge was granted

The appellants challenged the primary judge's finding that the loan arrangement with Mr Rodrick was sufficient to ensure the Company's solvency. In concluding that the Company was able to pay all its debts as and when they became due and payable, the Court focused on two key characteristics of the loans provided to the Company by Nu-Log and Mr Rodrick.

First, although the loans were being provided by a *de facto* director and a related party of the Company, the evidence demonstrated that the financial support was likely to continue. Morrison JA came to this view based on Mr Rodrick's willingness to provide funding early in his association with the Company, his desire to become a part owner and his belief that the business was profitable. Therefore, Mr Rodrick was regarded as a "committed financial supporter" of the Company.

Second, the "commercial realities" of the case pointed clearly to the conclusion that the provision of the loans meant that the Company was able to pay its debts as and when they fell payable. Specifically, Mr Rodrick's genuine "belief in the quality of the product ICM produced, and its likely success, led him not only to provide finance to it but to commit as a part owner of the company". Also, the boat ordered by Mr Rodrick was only partly constructed at the time he agreed to continue providing funds in exchange for the Charge. These factors meant that Mr Rodrick had a vested interest in the Company continuing as a viable business.

It is important to note that the fact that the loans were repayable on demand did not affect the Court's finding of solvency. Morrison JA cited numerous cases in support of the proposition that, where commercial reality dictates that a financier will not demand the repayment of a loan in the immediate future, a finding of insolvency is unlikely to follow. In this case, it was clear that Mr Rodrick had no intention of calling for the repayment of the loans.

This decision is a timely reminder that Courts will take a pragmatic view when assessing whether or not a company is solvent. The Court reiterated the principle, accepted in *Williams v Scholz* [2008] QCA 94, that "the key concept is ability to pay the company's debts as and when they fall due". In this case, the Court was willing to accept that the availability of an ongoing source of credit was sufficient to allow the Company to meet all its debts as and when they fell due.