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1. Recent Corporate Law and Corporate Governance Developments

1.1 Corporate financial distress: Discussion paper

On 14 October 2014, the Australian Restructuring, Insolvency and Turnaround Association (ARITA) published A Platform for Recovery 2014 (October 2014), a discussion paper on dealing with corporate financial distress in Australia. The paper identifies seven current issues in the insolvency regime and proposes law and practice reforms to remedy them. The seven issues include the lack of a restructuring culture in Australia, value destruction as a result of entering into external administration, maximising the return to creditors when companies with minimal liabilities fail, and maximising the prospects of viable small companies in financial distress continuing operations.

The discussion paper is available on the ARITA website.

1.2 Global cross-border M&A data

On 14 October 2014, the International Institute for the Study of Cross-Border Investment and M&A published its quarterly review for the third quarter of 2014 (undated).

The key findings are that:

- Global mergers and acquisitions (M&A) volume in Q3 was US$888 billion, marking the second strongest quarter since 2008, exceeded only by Q2 2014. If deal volume continues at this level, global M&A activity for 2014 would exceed US$3.5 trillion, the highest annual volume since 2007.
- Deal volume for the first three quarters of 2014 has surged more than 50% over the same period last year. Cross-border M&A activity is on pace to reach US$1.4 trillion in 2014, nearly twice the volume of 2013.
- Hostile or unsolicited deals in the first three quarters of 2014 increased to approximately US$550 billion (up 367% over the same period in 2013).
- Strong corporate earnings, continued large cash balances being carried at virtually zero return, attractive financing for most corporate borrowers, generally high stock prices, all of which support and drive accretion—often very substantial—in strategic acquisitions, together with a focus on industry consolidation and growth through acquisition have continued to drive substantial M&A activity in Q3, despite some regional tensions and concerns about growth in certain economies.
- Q3 was led by megadeals in the Energy & Power, Telecommunications, and Retail sectors.

The review is available on the XBMA website.

1.3 Revised Corporate Governance Principles for Banks (consultation paper) issued by the Basel Committee

On 10 October 2014, the Basel Committee released revised guidelines on corporate governance at banks (October 2014) (the Consultative Document) for public comment.

Building on the Committee's Principles for enhancing corporate governance (2010), the Consultative Document sets out revisions that are proposed to:

- strengthen the guidance on risk governance, including the risk management roles played by business units, risk management teams, and internal audit and control functions and the importance of a sound risk culture to drive risk management within a bank;
- expand the guidance on the role of the board of directors in overseeing the implementation of effective risk management systems;
- emphasise the importance of the board's collective competence as well as the obligation on individual board members to dedicate sufficient time to their mandates and to remain current on developments in banking;
- provide guidance for bank supervisors in evaluating the processes used by banks to select board members and senior management; and

- recognise that compensation systems form a key component of the governance and incentive structure through which the board and senior management of a bank convey acceptable risk-taking behaviour and reinforce the bank's operating and risk culture.

The Consultative Document is available on the BIS website.

1.4 IOSCO consults on principles regarding the custody of CIS assets

On 10 October 2014, the International Organization of Securities Commissions (IOSCO) published Consultation Report - Principles regarding the Custody of Collective Investment Schemes' Assets (October 2014). The report is aimed at gathering the views of investment managers, custodians, institutional investors and other interested parties on the development of a set of principles for the custody of collective investment schemes' (CIS) assets.

Custodians play a key role in the safekeeping of CIS assets as recognised in IOSCO Principle No 25, which states that "the regulatory system should provide for rules governing the legal form and structure of collective investment schemes and the segregation and protection of client assets".

CIS managers tend to invest more in complex instruments. The wider array of eligible investment instruments raises questions about the scope of the custodian's safekeeping role and duties. In addition, the growing and now widespread use of electronic book entry to register and track ownership changes in securities is transforming market practices and processes, creating new challenges and risks. CIS have taken important steps to diversify and internationalise their portfolios. Growing foreign investments have increased the need for CIS to appoint sub-custodians in foreign jurisdictions. This trend may have implications, especially regarding the delegation of safe-keeping functions, as custody chains tend to be longer and more complex, involving many foreign jurisdictions.

Taking into account these recent market developments, the consultation paper explores the key risks associated with the custody function.

The report proposes nine principles divided into two sections aimed at identifying the core issues that should be kept under review by the regulatory framework.

- Principle 1: The regulatory regime should make appropriate provisions for the custodial arrangements of the CIS.
- Principle 2: CIS assets should be segregated from:

    - the assets of the responsible entity, its related entities and other schemes;
    - the assets of the custodian / sub-custodian throughout the custody chain; and
    - the assets of other clients of the custodian throughout the custody chain (unless CIS assets are held in a permissible omnibus account).
- Principle 3: CIS assets should be entrusted to a third party custodian. In limited circumstances where the regulatory regime permits self-custody of CIS assets, additional safeguards should be put in place to ensure proper segregation and protection of CIS assets.
- Principle 4: The custodian should be functionally independent from the responsible entity.
- Principle 5: The responsible entity should seek to ensure that the custody arrangements in place are disclosed appropriately to investors in the CIS offering documents or otherwise made transparent to investors.
- Principle 6: The responsible entity should use appropriate care, skill and diligence when appointing a custodian to safe keep CIS assets.
- Principle 7: The responsible entity should, at a minimum, consider a custodian's legal/ regulatory status, financial resources and organisational capabilities during the due diligence process.
- Principle 8: The responsible entity should formally document its relationship with the custodian and the agreement should seek to include provisions about the scope of the custodian's responsibility and liability.
- Principle 9: Custody arrangements should be monitored on an ongoing basis for compliance with the terms of the custody agreement.

The consultation report is available on the IOSCO website.

1.5 Proposals to improve the operational risk capital framework released by the Basel Committee

On 6 October 2014, the Basel Committee released Consultative Document - Operational risk: Revisions to the simpler approaches (October 2014) for public comment. The document sets out a revised standardised approach for measuring operational risk capital. The existing framework sets out different approaches that banks may use to calculate their operational risk capital requirement. Once finalised, a new unitary standardised approach will replace the current non-model-based approaches, which comprise the Basic Indicator Approach (BIA) and the Standardised Approach (TSA), including its variant the Alternative Standardised Approach (ASA). In addition to streamlining the framework, the new approach will address weaknesses identified in the existing approaches.

The Committee also published a review (6 October 2014) of banks' implementation of the Principles for the Sound Management of Operational Risk (2011). The principles embody the lessons from the financial crisis and evolving sound practice in operational risk management. The review covered 60 systemically important banks (SIBs) in 20 jurisdictions and took the form of a questionnaire against which banks self-assessed the extent and quality of their implementation.

Progress in implementing the principles varies significantly across banks and, overall, more work is needed to achieve full implementation. In particular, four principles that have been identified as being among the least thoroughly implemented are: (i) operational risk identification and assessment; (ii) change management; (iii) operational risk appetite and tolerance; and (iv) disclosure. The Committee encourages supervisors to continue working with banks to ensure that plans are in place to improve compliance with the principles, and to achieve a level of implementation commensurate with banks' size, complexity and risk exposure.

The consultative document and the review are available on the BIS website.

1.6 IOSCO publishes second securities markets risk outlook

On 1 October 2014, IOSCO published its Securities Markets Risk Outlook 2014-15 (October 2014) (the Outlook). The Outlook is a forward-looking report focusing on identifying potential risks in securities markets.

The Outlook has been prepared during a transformative period for global financial markets. As the initial impact of the 2008 financial crisis recedes, securities markets are an increasingly important financing channel for the economy. At the same time, innovation is re-entering the markets, while accommodative monetary policies continue to bolster securities markets. Consequently, the identification and analysis of the build-up of systemic risk in securities markets is of growing significance.

The Outlook is divided into two parts.

Part I describes selected global trends and potential vulnerabilities in securities market, including the following:

- The importance of securities markets is growing.
- Asset price valuation is increasing, while volatility remains low. A change in the monetary stance will create winners and losers while markets are adjusting to the new reality.
- Derivative markets are still growing and clearing is increasing.

- Some real estate markets and real estate investment trusts could still be vulnerable.
- Capital flows into emerging markets have grown and are affecting securities prices.

Part II identifies the potential systemic risks in or related to securities markets. Many of the potential risks described below were identified in the 2013-14 risk outlook and are expanded upon in this year's iteration.

These potential systemic risks are:

- the search for yield and the return of leverage in the financial system;
- the search for yield and volatility affecting emerging markets;
- risks in central clearing;
- the increased use of collateral and risk transfer; and
- governance and culture of financial firms.

The report is available on the IOSCO website.

1.7 IOSCO issues report on market-based financing for SMEs and infrastructure

On 30 September 2014, IOSCO published the research report Market-based long-term financing solutions for SMEs and infrastructure (September 2014). The report is a compilation of recent examples of capital market solutions in developed and emerging markets that have contributed to the financing of small and medium enterprises (SME) and infrastructure projects.

The research report was prepared for the G20 Finance Ministers and Central Bank Governors. It describes innovative structures and products in equity capital markets, debt capital markets, securitisation and pooled investment vehicles that provide practical solutions to broadly recognised challenges for financing of SMEs and infrastructure projects.

Since the 2008 global financial crisis, the banking sector which has traditionally been a major source of funding for long-term financing (LTF) needs, has undergone a significant deleveraging process. This has increased the gap between supply and demand for LTF in many economies around the world. As governments implement austerity measures and face budget constraints, public funding for SMEs and infrastructure projects has been constrained.

Against this backdrop of constrained funding, there has been a gradual shift from a predominantly bank-funded model for LTF towards a model that includes a greater share of capital market-based funding.

The report is available on the IOSCO website.

1.8 IMF report: Risk taking, liquidity and shadow banking

In October 2014, the International Monetary Fund (IMF) published the global financial stability report Risk Taking, Liquidity, and Shadow Banking: Curbing Excess while Promoting Growth (October 2014).

The report finds that six years after the start of the financial crisis, the global economic recovery continues to rely heavily on accommodative monetary policies in advanced economies. Monetary accommodation remains critical in supporting the economy by encouraging economic risk-taking in the form of increased real spending by households and greater willingness to invest and hire by businesses. Prolonged monetary ease may also, however, encourage excessive financial risk-taking.

Chapter 1: Improving the Balance Between Financial and Economic Risk Taking

Chapter 1 concludes that although economic benefits of monetary ease are becoming more evident in some economies, market and liquidity risks have increased to levels that could compromise financial stability if left unaddressed. The best way to safeguard financial stability and improve the balance between economic and financial risk taking is to put in place policies that enhance the transmission of monetary policy to the real economy—thus promoting economic risk-taking—and address financial excesses through well-designed macroprudential measures.

Chapter 2: Shadow Banking Around the Globe: How Large, and How Risky?

Chapter 2 examines the growth of shadow banking around the globe, assessing risks and discussing regulatory responses. Although shadow banking takes vastly different forms within and across countries, some of its key drivers tend to be common to all: search for yield, regulatory circumvention, and demand by institutional investors. The contribution of shadow banks to systemic risks in the financial system is much larger in the United States than in Europe. The chapter calls for a more encompassing (macroprudential) approach to regulation and for enhanced data provision.

Chapter 3: Risk Taking By Banks: The Role of Governance and Executive Pay

Chapter 3 discusses how conflicts of interest between bank managers, shareholders, and debt holders can lead to excessive bank risk-taking from society's point of view. It finds that banks with boards of directors independent from management take less risk. There is no clear relation between bank risk and the level of executive compensation, but a better alignment of bankers' pay with long-term outcomes is associated with less risk.

The report is available on the IMF website.

1.9 FSB releases proposals on cross-border recognition of resolution actions and action to address cross-border close-out risk

On 29 September 2014, the Financial Stability Board (FSB) released Consultative Document - Cross-border recognition of resolution action (29 September 2014) for public comment. The FSB is consulting on proposals to achieve the cross-border recognition of resolution actions and remove impediments to the cross-border resolution.

The consultative document proposes a set of policy measures and guidance consisting of:

- elements that jurisdictions should consider including in their statutory cross-border recognition frameworks to facilitate effective cross-border resolution as required by the FSB's Key Attributes of Effective Resolution Regimes for Financial Institutions (2011); and
- contractual approaches to cross-border recognition that focus on two particular cases where achieving cross-border recognition is a critical prerequisite for orderly resolution:
    - temporary restrictions or stays on early termination and cross-default rights in financial contracts; and
    - the "bail-in" of debt instruments that are governed by the laws of a jurisdiction other than that of the issuing entity.

Further information is available on the FSB website.

1.10 UK statutory audit services market - mandatory tendering of the statutory audit engagement

On 26 September 2014, the UK Competition and Markets Authority (CMA) published the final Order that will implement the recommendations made by the Competition Commission (one of the bodies the CMA has replaced) in respect of the market for statutory audit services.

The Order will commence on 1 January 2015 and applies in relation to financial years beginning on or after that date. The Order requires, among other things, FTSE 350 companies to put the statutory audit services engagement out to tender every ten years or earlier. It also sets out the audit committee's responsibilities in this regard and also in respect of other areas including, for example, the influence exerted over the appointment of the audit engagement partner.

The Order and an explanatory note are available on the CMA website.

1.11 Progress on post-crisis financial reforms

On 25 September 2014, banking supervisors and central bankers representing more than 100 jurisdictions met in Tianjin, China, to discuss a range of policy measures relating to the Basel Committee on Banking Supervision's post-crisis reform agenda. Participants also discussed the role of banking systems in promoting growth and making financial services safe so that they could support the real economy.

The key matters discussed were as follows:

(a) Dealing with global systemically important banks

The Basel Committee reviewed an updated list of global systemically important banks (G-SIBs) based on end-2013 data. A bank designated as a G-SIB based on the Committee's methodology for assessing global systemic importance is required to hold additional Common Equity Tier 1 (CET1) capital of between 1 and 2.5%. This higher loss absorbency requirement will be phased in from the start of 2016, and will be fully implemented from the start of 2019.

(b) Endorsement of the net stable funding ratio

The Committee endorsed the final details of Basel III's net stable funding ratio (NSFR). The NSFR limits the extent to which illiquid assets can be funded by volatile short-term borrowings and encourages banks to maintain more stable and longer-term sources of funding. The final standard will commence at the start of 2018.

(c) Revising corporate governance guidance

Effective corporate governance is critical to the proper functioning of the banking sector. The Basel Committee has revised its 2010 Principles for enhancing corporate governance (2010) and has published revisions for consultation (see above).

(d) Finalising securitisation standards

The Committee reviewed progress towards finalising revisions to the Basel framework's securitisation standard and agreed the remaining significant policy details that will be published by year-end. It also recognised work that is being conducted jointly by the Basel Committee and the International Organization of Securities Commissions (IOSCO) to review securitisation markets.

(e) Improving consistency in bank capital ratios

The Committee has been closely examining banks' risk weighting practices. At its meeting, the Committee discussed a range of policy and supervisory actions that it has initiated to address the issue of excessive variability of risk-weighted assets. These actions include a review of the standardised approaches (i.e. the non-internal model-based approaches), the introduction of capital floors, greater restrictions on modelling parameters and assumptions, and improved disclosure.

1.12 UK: Extending the regulation of financial benchmarks - consultation published

On 25 September 2014, the UK government launched a consultation on proposals to extend the regulatory regime recently introduced for LIBOR to other financial benchmarks. The consultation is based on the first set of recommendations released under the *Fair and Effective Markets Review*, which was formed in June 2014.

The consultation and the recommendations are available on the UK government website.

1.13 Abolition of the Corporations and Markets Advisory Committee

On 24 September 2014, the Australian Government released an exposure draft Bill and associated explanatory material to give effect to the 2014-15 Budget decision to abolish the Corporations and Markets Advisory Committee (CAMAC). The decision was made in the context of the broader Smaller and More Rational Government

reforms to reduce the number of Australian Government bodies and streamline the shape of government.

The abolition of CAMAC has been opposed by peak organisations such as the Law Council of Australia, the Governance Institute of Australia and the Australian Institute of Company Directors.

The exposure draft Bill proposes to abolish CAMAC by repealing Part 9 of the Australian Securities and Investments Commission Act 2001 (Cth), which provides for the establishment, functions and operation of CAMAC.

The draft Bill and draft explanatory material are available on the Australian Government website.

1.14 Mining companies should measure social investment programs better: report

On 23 September 2014, KPMG released Valuing social investment in mining (September 2014), a report on social investment by mining companies.

Together, ten of the world's largest mining, metals and engineering companies reported social investments valued at US$1.2 billion in 2013, according to research by KPMG International. Yet few of those companies are reporting the impact these investments are actually having on the people they are intended to help.

Only one of the ten reported any quantified outcomes, suggesting a lack of debate over the true impact of programs, both internally and with the communities they are serving. And only four of the mining companies surveyed published a detailed social investment strategy.

With 52 different types of programs across the group surveyed, the report finds that companies risk spreading their efforts too thinly, rather than focusing on a few priorities that can really make a difference. More money and a higher number of beneficiaries do not necessarily translate into greater impact.

The report is available on the KPMG website.

1.15 2014 European board diversity analysis

EgonZehnder has released its 2014 European Board Diversity Analysis (undated). The report profiles the boards of 356 of the largest companies across 17 European countries. The 2014 study also includes a global perspective, exploring gender diversity across 568 large company boards in other regions of the world.

The report has three main conclusions. First, boards across Europe and in select other geographies have become significantly more diverse in recent years, primarily in relation to gender and nationality. Second, the percentage of females in executive director and board leadership positions remains stagnant at a relative low level. Third, the world remains far from the tipping point where true board diversity is the established norm.

Gender diversity of European boards has increased substantially in recent years. More than 20% of directors on the boards included in the 2014 Europe study are women, a significant increase from 15.6% just two years ago, and a major jump from 8% in 2004.

On average, European boards now include 2.7 women, up from an average of just 1.5 female members per board as recently as 2008, suggesting that board service is steadily becoming a less isolating experience for women.

As a whole, European boards are now on par in gender diversity with the highest-ranking countries in the study's non-European sample: the United States (21.2% female directors) and Australia (22.6%). At 20.3% overall, European boards have nearly double the average (11.6%) of female representation on all boards in the comparative sample.

Further, the five countries with the highest levels of female board members worldwide are all European: Norway, Finland, France, Sweden, and the UK (tying with Australia).

Only 7.6% of the European boards studied in 2014 include no women members, as contrasted with the 32.2% that had no women members as recently as 2006.

From 2006 through 2010, only Denmark, Finland, Norway, and Sweden had at least one woman serving on 100% of the boards studied. France joined those Nordic frontrunners in 2012. In 2014 the UK, Austria, and Ireland also made the list. At this rate, one might foresee women represented on every large European company board in the 2016 study.

Nearly 90% of European boards now include at least one director from a country other than where the company is headquartered. in 2014, roughly a third (32.3%) of all directors serving on major European boards are non-nationals.

European boards' progress in gaining multinational perspective stems from steady gains since 2006, when just 22.7% of European directors were non-nationals.

Seven countries—Austria, Denmark, Finland, Ireland, Luxembourg, The Netherlands, and Portugal—have at least one non-national member, on 100% of the boards that were analysed.

While the 2014 European Board Diversity Analysis findings reveal significant gains in female participation on boards, women have yet to attain a corresponding share of board leadership roles. Across the European boards studied, less than 3% of board chair positions are held by women, a figure comparable to the average of 3.7% across all other regions. Women now hold just over 12% of committee chair positions in Europe, suggesting that as more women gain experience in board service, gender diversity in top board leadership roles may increase.

The 2014 European Board Diversity Analysis also finds that women currently fill relatively few (5.6%) executive director positions, with no significant gain being realised since preceding studies in 2010 and 2012. The small number of female executive directors reflects the ongoing challenge European companies face in diversifying their senior talent pipelines.

Not surprisingly, gender diversity varies substantially in boards around the world. In the United States, Canada, Australia, New Zealand, and South Africa—countries where board diversity has long been an important consideration—women's share of board seats is relatively high, while in other major economies—Japan, Russia, and South Korea—the data indicate little progress has been made. Hong Kong, India, Indonesia, Malaysia, Hungary, and Poland all now have at least one woman serving on 70% or more of the boards that were studied, a sign that boards in these countries may be poised to realize meaningful advances in gender diversity.

The report is available on the EgonZehnder website.

1.16 New book - *Directors' Duties: Principles and Application*

Directors' Duties: Principles and Application, by Dr Rosemary Teele Langford who teaches at Melbourne Law School, is a new book that outlines key fiduciary and statutory duties of Australian company directors, with detailed reference to the position in the United Kingdom. It resolves complex contemporary issues concerning

fiduciary classification and the relationship between the various duties, as well outlining the consequences of breach of duty and the significance of fiduciary classification. Particular focus is given to the duties that have traditionally been characterised as fiduciary and their statutory equivalents. These are the duties to avoid conflicts and profits, to act in good faith in the interests of the company and for proper purposes, to retain discretions and to disclose information. The duty of care is also examined and the book demonstrates why this duty is different to other key duties. The detailed judgments in the Bell group litigation are given comprehensive critical analysis. The book therefore provides certainty for practitioners, academics and students in the organisation and application of key directors' duties.

The book is available for purchase on the Federation Press website.

1.17 Latest Centre for International Finance and Regulation reports

Two new Centre for International Finance and Regulation reports that have been completed by academics at Melbourne Law School have been published.

(a) Superannuation knowledge, behaviour and attitudes in young adults in Australia

This report presents the results of a study examining superannuation knowledge, behaviour and attitudes in 994 young adult superannuation fund members (25–34 years old) in Australia. Respondents completed a 75-question online survey instrument which included questions on demographics and superannuation knowledge, behaviour and attitudes. It is the first large-scale study to focus exclusively on superannuation and the young adult population in Australia. The report concludes that there are serious deficiencies in knowledge, behaviour and attitudes among young adults. Knowledge of basic facts about superannuation is poor. Young adults are unengaged by and uninterested in superannuation or retirement planning. Attitudes can be described as worried and skeptical.

The report is available on the SSRN website.

(b) Financial products and short-form disclosure documents - Challenges and trends

Recent years have seen a trend in many jurisdictions towards the adoption of short-form disclosure documents for retail financial products. This report analyses the challenges and trends in relation to short-form disclosure documents from a comparative perspective. Developments in the following markets are examined for this purpose: Australia, New Zealand, the European Union, Hong Kong, Singapore and

Canada. The objectives of this report are to review the international trend towards short-form disclosure documents and the policy reasons behind the trend; to examine the different approaches that have been adopted by the selected jurisdictions; and to identify the criteria and the factors that should be taken into account when jurisdictions consider which approach to adopt. In this way, the report seeks to assist regulators in determining appropriate responses and strategies through a guide to the approaches in the selected jurisdictions, the legislative and policy underpinnings and the short-form disclosure documents themselves.

The report is available on the SSRN website.

2. Recent ASIC Developments

2.1 ASIC facilitates foreign companies offering securities

On 13 October 2014, ASIC released guidance to facilitate foreign companies making offers of CHESS Depository Interests (CDIs) over their shares and options to investors in Australia.

Regulatory Guide 253 - Fundraising: Facilitating offers of CHESS Depository Interests (October 2014) (RG 253) provides the market with certainty about how offers of CDIs over foreign shares and options are regulated under the Corporations Act 2001 (Cth).

Accompanying RG 253, ASIC also issued Class Order [CO 14/827] on offers of CHESS depository interests, which reflects current market practice, to ease the compliance burden for foreign companies as they will no longer need to approach ASIC for individual relief.

The regulatory guide is available on the ASIC website.

2.2 Higher standards needed for life insurance industry

On 9 October 2014, ASIC released a review of the life insurance industry. The review finds that the industry needs to improve the quality of advice and ensure that the interests of consumers are given priority.

ASIC's review of more than 200 advice files from large, medium and small Australian financial services (AFS) licensees finds that 63% were compliant. However, more than one third (37%) of the advice consumers received failed to comply with the laws relating to appropriate advice and prioritising the needs of the client.

ASIC's report sets out the various commission models that are used to remunerate advisers in the life insurance sector. The report finds that high upfront commissions are more strongly correlated with non-compliant advice, including in situations where the recommendation is to switch products.

Affordability of insurance is an important issue for consumers, and ASIC's report includes cases where clients were recommended insurance cover that was likely to be very difficult to afford given their financial circumstances.

ASIC's report confirms that the high rate at which life insurance policies are lapsing warrants consideration by the life insurance industry to ensure that industry practices are sustainable.

ASIC has made a number of recommendations for insurers, AFS licensees, advisers and their professional associations, including a focus on how to ensure client interests are met and balancing the issue of affordability versus cover.

The report is available on the ASIC website.

2.3 ASIC and US Commodity Futures Trading Commission sign memorandum of understanding to enhance supervision of cross-border regulated entities

On 1 October 2014, ASIC and the US Commodity Futures Trading Commission (CFTC) signed a memorandum of understanding (MOU) regarding cooperation and the exchange of information in the supervision and oversight of regulated entities that operate on a cross-border basis in the United States and in Australia.

The MOU is available on the ASIC website.

2.4 ASIC reports on corporate insolvencies

On 29 September 2014, ASIC published its annual overview of corporate insolvencies based on statutory reports lodged by external administrators for the 2013-14 financial year.

Report 412 - Insolvency statistics: External administrators' reports (July 2013 to June 2014) (September 2014) (REP 412) is ASIC's sixth report and provides information on the nature of corporate insolvencies, supplementing the monthly and quarterly statistics that ASIC publishes on its website.

The report summarises information from 10,073 reports received during the 2013-14 financial year and includes ASIC's response to reports of alleged misconduct from external administrators.

(a) Profile of insolvent companies

REP 412 includes information about the profile of companies placed into external administration, including:

- industry types;
- employee numbers;
- causes of company failure;
- estimated number and value of a company's unsecured creditor debts; and
- estimated dividends to unsecured creditors.

REP 412 shows small to medium size corporate insolvencies again dominated external administrators' reports. Of note, 86% had assets of $100,000 or less, 81% had less than 20 employees and 43% had liabilities of $250,000 (or less).

Ninety-seven percent of creditors in this group received between 0 and 11 cents in the dollar, reflecting the asset/liability profile of small to medium size corporate insolvencies.

(b) Allegations of misconduct

REP 412 details how often external administrators report alleged misconduct by company officers and the types of alleged misconduct most frequently reported.

In the 2013-14 financial year, 7,218 reports alleging misconduct were lodged with ASIC by external administrators.

ASIC asked external administrators to prepare 802 supplementary reports where external administrators alleged company officer misconduct. This accounted for 11.1% of all reports, which alleged misconduct, lodged in the financial year.

Supplementary reports are typically detailed, free-format reports, which set out the results of the external administrator's inquiries and the evidence they have to support

alleged offences. Generally, ASIC can determine whether to commence a formal investigation on the basis of a supplementary report. While only a portion of the offences reported may result in a formal investigation or surveillance, ASIC uses the information for broader intelligence and targeting purposes.

In both the 2012-13 and 2013-14 financial years, after assessment, ASIC referred 25% and 19% of these cases respectively for investigation or surveillance.

ASIC considers a range of factors when deciding to investigate and take enforcement action and this is detailed in Information Sheet 151 - ASIC's approach to enforcement (September 2013) (INFO 151) (further information).

(c) Future improvements: Reporting of alleged insolvent trading and other offences

To assist external administrators in their reporting obligations, ASIC anticipates releasing an amended report template for external administrators (Form EX01) in early-2015.

The amendments aim to capture more accurate information on alleged insolvent trading offences which might provide greater insight into the extent of insolvent trading and enable ASIC to focus its resources on matters that warrant further investigation.

The revised form is a further ASIC initiative to collect better information on corporate insolvencies in Australia.

It complements recent enhancements to other forms to capture data in electronic format such as:

- industry statistics for external administration appointments from Form 505 (notice of appointment);
- key information from deeds of company arrangement from an enhanced Form 5047; and
- key financial data from Form 524 (presentation of accounts and statement).

ASIC expects to continue its work with industry to improve reporting including on other offences, such as alleged breaches of director duties.

REP 412 is available on the ASIC website.

2.5 ASIC report on relief applications - February to May 2014

On 25 September 2014, ASIC released its latest report outlining decisions on relief applications covering the period 1 February - 31 May 2014.

Businesses frequently approach ASIC for assistance to help make the law work better for them. ASIC uses its discretion to vary or set aside certain requirements of the law where there is a net regulatory benefit or where ASIC can facilitate business or cut red tape without harming other stakeholders.

Between 1 February 2014 and 31 May 2014, ASIC approved 650 relief applications.

Report 411 - Overview of decisions on relief applications (February to May 2014) (September 2014) (REP 411), aims to improve the level of transparency and the quality of publicly available information about decisions ASIC makes when asked to exercise its discretionary powers to grant relief from provisions of the:

- the Corporations Act 2001 (Cth) (the Corporations Act);
- the National Consumer Credit Protection Act 2009 (Cth) (the National Credit Act); or
- the National Consumer Credit Protection (Transitional and Consequential Provisions) Act 2009 (Cth).

The report summarises examples of situations where ASIC has exercised, or refused to exercise, its exemption and modification powers under the Corporations Act and the licensing and responsible lending provisions of the National Credit Act. The report also highlights instances where ASIC has considered adopting a no-action position regarding specified non-compliance with statutory provisions.

Finally, the report provides examples of decisions that demonstrate how ASIC has applied its policy in practice which ASIC thinks will be of particular interest for capital market participants and for participants in the financial services industry. The report includes an appendix detailing the relief instruments referred to in the report.

REP 411 is available on the ASIC website.

2.6 ASIC seeks feedback to help clarify fee and cost disclosure requirements

On 24 September 2014, ASIC announced that it is seeking industry feedback to help clarify key fee and cost disclosure requirements for superannuation and managed investment products.

In particular, ASIC is seeking feedback and comments on proposed changes that aim to clarify the requirements for:

- indirect costs, double counting and fee issues for superannuation products;
- the disclosure of costs associated with investing through interposing entities by managed investment products; and
- the appropriate application of the consumer advisory warning for some products.

ASIC highlighted this work in Report 398 - Fee and cost disclosure: Superannuation and managed investment products (July 2014).

Further information is available on the ASIC website.

3. Recent ASX Developments

3.1 Consultation Paper: "Central counterparty recovery: Uncovered loss allocation and replenishment tools for clearing participant default"

On 2 October 2014, ASX released the consultation paper Central Counterparty Recovery - Uncovered loss allocation and replenishment tools for clearing participant default (October 2014). Through this consultation, ASX is seeking feedback on proposals to introduce new powers under the operating rules of ASX Clear and ASX Clear (Futures) to address fully any credit losses or liquidity shortfalls they may face as a result of clearing participant default, and to replenish their default funds following such events.

The consultation paper is available on the ASX website.

3.2 Corporations Act s. 444GA

The ASX has asked insolvency practitioners and their lawyers to make early contact with the ASX where it is proposed to rely on s. 444GA of the Corporations Act 2001 (Cth) to transfer shares of a listed company in administration.

The request has been made following some less than optimal outcomes realised by the industry with the reinstatement of Mirabela Nickel Ltd.

ASX specifically wants the opportunity to discuss the mechanics and timing involved in:

- having trading in the company's shares reinstated;
- giving clear notification to shareholders that some of their shares have been transferred to creditors; and
- dispatching holding statements to shareholders evidencing the transfer.

Further information is available on the ARITA website.

3.3 Update to ASX Listing Rules Guidance Note 12 - Significant changes to activities

On 20 September 2014, ASX released ASX Listing Rules Guidance Note 12 - Significant changes to activities (30 September 2014), which has been updated to include further guidance in ss. 3.2 (the main circumstances in which ASX will apply Listing Rules 11.1.2 and 11.1.3), 3.3 (prospectus/ PDS/ information memorandum), 3.6 (meeting the minimum spread test), 3.7 (meeting the profit test or assets test), 3.8 (escrow requirements for restricted securities), 3.9 (the 20 cent rule), 3.10 (minimum option exercise price), 3.12 (requirements for additional information), 3.13 (pre-emptive capital raisings), 4.2 (the application of Listing Rule 11.2) and 6.1 (the contents of the notice).

A footnote has also been added noting that putting out a notice of meeting with a *pro forma* statement of financial position that has not been reviewed by a registered company auditor or independent accountant may expose the entity and its directors to embarrassment and potential legal liability if the information in the reviewed version of the *pro forma* statement of financial position included in the entity's prospectus, PDS or information memorandum ultimately differs from the information included in the notice of meeting or if the reviewed version is subject to a material qualification.

The guidance note is available on the ASX website.

3.4 Online forms for announcing corporate actions

On 22 September 2014, ASX released online forms for announcing corporate actions. It will not be mandatory to use online forms for the first six months from implementation (that is, until Monday 23 March 2015). Given the benefits of the new process, however, ASX encourages listed entities to become familiar with the new forms and utilise this improved service in a timely manner.

Revised Listing Rules, Guidance Notes and Appendices applicable to the introduction of online forms are published on the ASX and ASX Online Companies websites.

The notice with information on training seminars is available on the ASX website.

3.5 Update to ASX Listing Rules Guidance Note 17 - Waivers and in-principle advice

On 22 September 2014, ASX released ASX Listing Rules Guidance Note 17 - Waivers and in-principle advice (22 September 2014), which has been updated to provide further guidance in ss. 4 (standard vs non-standard waivers), 6 (applications for waivers), 7 (reasons for decision) and 10 (appeals from waiver decisions).

The Annexure to the Guidance Note now includes three new standard waivers relating to Listing Rules 7.1 and 14.7, with some consequential amendments to the final standard waiver in the Annexure.

The guidance note is available on the ASX website.

3.6 Reports - September 2014

On 3 October ASX released the following reports (all dated 3 October 2014) for September 2014:

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

4. Recent Takeovers Panel Developments

4.1 Scantech Ltd - Panel declines to conduct proceedings

On 13 October 2014, the Takeovers Panel declined to conduct proceedings on an application dated 26 September 2014 from Scantech Ltd (Scantech) in relation to its affairs.

The application concerned (among other things) whether a Consortium had entered, or intended to enter, call option and share sale agreements to acquire shares in Scantech in contravention of the 20% takeovers prohibition and substantial holding provisions.

The Panel received an executed call option and share sale agreement in relation to approximately 6.05% of the voting shares of Scantech. Responses to the Panel's preliminary questions indicated that there may be, or may have been, agreements in relation to approximately another 16.96% of the voting shares in Scantech.

Given, however, that the amount of information in the application and other material provided to the Panel (including material provided in answer to questions asked by the Panel) did not present a clear picture, the most effective further investigation of the matter would be by way of ASIC investigation. Accordingly, the Panel declined to conduct proceedings and referred the matter to ASIC under r. 18 of the Australian Securities and Investments Commission Regulations 2001 (Cth) for it to consider making a further application to the Panel.

The reasons for the decision are available on the Panel website.

4.2 Aspen Parks Property Fund 01 and 02 - Panel declines to conduct proceedings

On 9 October 2014, the Takeovers Panel declined to conduct proceedings on two applications heard together, one dated 3 October 2014 from Discovery Parks and the other dated 7 October 2014 from Discovery Parks and Martin Cotterell as trustee for the Marlee Superannuation Fund.

The applications concerned (among other things) an entitlement offer made by Aspen Parks and whether disclosure should have been made earlier of an indicative and then final proposal by Discovery Parks to acquire assets of Aspen Parks, the control effect

of the entitlement offer and whether the independent board committee gave due consideration to the offer.

The Panel considered that there was no reasonable prospect that it would make a declaration of unacceptable circumstances. Given the lateness of the applications, the Panel considered that the facts presented were not such as to warrant further delaying the timetable of the entitlement offer which could be unfairly prejudicial.

The reasons for the Panel's decision will be published in due course on the Panel website.

5. Recent Research Papers

5.1 The impact of hedge fund activism: Evidence and implications

Hedge fund activism has increased almost hyperbolically. Some view this optimistically as a means for bridging the separation of ownership and control; others are more pessimistic, seeing mainly wealth transfers from bondholders or speculative expectations of a takeover as fuelling the spike. Equivalent division exists over the impact of this increased activism, with optimists seeing real gains that do not erode over time and improvements in operating performance, and pessimists predicting shortened investment horizons, increased leverage, and reduced investment in research and development.

The authors' perspective is analytic. They begin by surveying the regulatory and institutional developments that have reduced the costs and increased the expected payoff from activism for hedge funds. Here, they focus particularly on the formation of "wolf packs"—namely, loose knit associations of hedge funds that are formed prior to, or contemporaneously with, the filing of a Schedule 13D. They then look at other new institutional structures that are appearing, as typified by the alliance between Pershing Square Capital Management and Valeant Pharmaceuticals in their bid for Allergan.

The authors then survey the empirical evidence on the impact of activism, looking successively at (1) who are the targets of activism? (2) does hedge fund activism create real value? (3) what are the sources of gains from activism? and (4) do the targets of activism experience post-intervention changes in real variables? Although confident claims have been made by some researchers, the authors find the evidence decidedly mixed on most questions (other than the short-term stock price impact). In particular, they find the conclusions about improvements in target operating

performance that have been expressed by some to be overextended beyond their actual data and premature.

Finally, the authors examine the policy levers that could encourage or chill hedge fund activism and consider the feasibility of reforms. The gains from hedge fund activism may be high both because such activity is relatively low risk (if asymmetric information can be exploited that is acquired before the filing of a Schedule 13D) and short-term (with the median hedge fund activist holding for approximately nine months). Still, the authors predict that the impact of most regulatory changes are likely to be marginal. Conversely, they believe that private ordering (through techniques such as a "window-closing" poison pill) could achieve at least as much as regulatory changes.

The paper is available on the SSRN website.

5.2 Do compensation consultants enable higher CEO pay? New evidence from recent disclosure rule changes

In July 2009, the SEC announced additional disclosure rules requiring firms that purchase other services from their compensation consultants to disclose fees paid for both compensation consulting and other services. This exogenous requirement dramatically increased both the turnover of compensation consultants and the number of specialist firms in the industry solely providing executive compensation consulting services. After the rule change, client firms that switched to specialist consultants paid their chief executive officers (CEOs) 9.7% more in median total compensation than a matched sample of firms that remained with multi-service consultants. Compensation consultants retained solely by the board are associated with 12.9% lower median pay levels than a propensity-score matched sample of firms with additional management-retained consultants. Finally, CEOs at firms that start hiring compensation consultants experience a 7.5% increase in median pay relative to a propensity-score matched sample. Overall, the study finds strong empirical evidence for the hiring of compensation consultants as a justification device for higher executive pay.

The paper is available on the SSRN website.

5.3 The Chinese "oppression" remedy: Creative interpretations of company law by Chinese courts

This is the first detailed study of the Chinese oppression remedy under the PRC Company Law (Article 20.1-2). Compared to UK, Canadian and Australian equivalents, the wording of the Chinese remedy is vague, and the Supreme People's Court has not clarified its meaning. Yet Chinese courts have created a body of *de facto* case precedents and made the remedy into an effective tool for minority shareholders to gain redress for a broad range of wrongs committed by abusive shareholders. Such use of case precedents should be formalized in China to bring more predictability to statutory interpretation.

The paper is available on the SSRN website.

6. Recent Corporate Law Decisions

6.1 Not-so-wide berth for s. 237 applicants seeking leave to bring proceedings on behalf of Marina Company

(By Jack Quirk, DLA Piper)

Jensen v RQYS Marina Ltd [2014] QSC 243, Supreme Court of Queensland, Applegarth J, 29 September 2014

The full text of this judgment is available online.

(a) Summary

This was an application under s. 237(1) of the Corporations Act 2001 (Cth) (the Corporations Act) in which the applicants sought leave to bring proceedings in the name of a company against two related companies and numerous former and current directors of the company. In dismissing the application, Applegarth J felt that the slim prospects of success of the proposed action were outweighed by the huge cost in litigating such an "enormously complex" matter. The application was not helped by what appears from the reasons to be an overly-lengthy and convoluted statement of claim. As such, it was not in the best interests of the company to grant the application and allow a derivative action to be brought in its name.

(b) Facts

The applicants were all berth holders of a few of the many berths at a marina in Manly, Queensland. All berth holders at the marina were required to be members of RQYS Marina Ltd (the Marina Company), a public company limited by guarantee. The Marina Company was initially set up to develop and operate the marina (Marina 1) on behalf of the Royal Queensland Yachting Squadron Ltd (Squadron). The first

object of the Marina Company as it appeared in its constitution (the Constitution) was as follows:

> To establish and support or to aid in the establishing or support of associations, institutions, trust funds or conveniences calculated to benefit the members of the Royal Queensland Yachting Squadron.

The Squadron had been an unincorporated association until it was registered as public company limited by guarantee in 1991. To ensure that the marina project was managed in a way that could not be adverse to the Squadron in the future, the Marina Company's Articles of Association provided that the Flag Officers of the Squadron would comprise the majority of the directors of the Marina Company.

From about 2002 onwards, discussions occurred among the directors and members of the Marina Company and the Squadron about the possibility of expanding the existing marina with the development of what is now known as Marina 2. The directors of the Marina Company wished to ensure that potential tax issues were addressed. They sought and obtained from the Australian Taxation Office (ATO) a private ruling in 2007. Following this ruling the directors of the Squadron and of the Marina Company agreed to proceed with the development of Marina 2, by establishing a corporate trustee holding assets on trust for the Squadron, a tax exempt entity. As a result, RQYS Nominees Pty Ltd (the Nominees) was incorporated and the New Marina Trust established at about the same time under which Nominees held the relevant lease for Marina 2 on trust for the Squadron.

The substance of the proposed proceeding, Applegarth J surmised, seemed to be that the other officers of the Marina Company were alleged to have subordinated the best interests of the Marina Company and the fiduciary duties they owed to it to the interests of the Squadron. The directors were said to have misused the Marina Company's assets and funds and failed to take advantage of opportunities which were alleged to have been available to it. The conduct in question occurred over a number of years and related to a number of "impugned transactions" involving the Marina Company, the Squadron, Nominees and the current and former directors of the Marina Company.

These transactions included the following:

- an alleged failure of the directors of the Marina Company to become the owner of Marina 2;
- an alleged failure of the directors of the Marina Company to obtain a future head lease over the Marina 1 seabed area and adjacent areas from 2029 to 2051;
- transactions in relation to a business known as the Yard Business and related facilities;

- alleged financial irregularities in relation to loans made to the Squadron which are said to have been on uncommercial terms and to have benefited the Squadron and Nominees; and
- the alleged misappropriation of monies known as the dredging fund in relation to the purchase of a dredge.

The applicants brought an application seeking leave pursuant to s. 237 of the Corporations Act to bring proceedings on behalf of the Marina Company against the Squadron, Nominees and certain current and former directors of the Marina Company.

(c) Decision

Applegarth J felt that while it would be "invidious" to address every claim made in the 93-page-long pleading, the five "impugned transactions" were worth consideration to the extent that they revealed the claim's prospects of success. In fact, the slim prospects of success proved crucial to the outcome of the application.

(i) Two central issues

Applegarth J felt that there were two central issues that went to the nub of each of the claims. His Honour weighed these up before turning to s. 237.

The first related to the Constitution of the Marina Company. Specifically, whether the Constitution allowed the Marina Company directors to make payments to the Squadron out of the assets of the Marina Company. Ultimately, his Honour found that not only did the Constitution allow for payments to be made from the Marina Company to the Squadron, but they were squarely within the purposes of the Constitution itself.

The second was whether the directors placed too much reliance on the ATO Tax Ruling of 2007, which led to the establishment of Nominees to develop and operate Marina 2. Ultimately, his Honour felt that it would have been remiss of the directors not to have been concerned with the ruling.

Each of the five impugned transactions related to a consideration of the two issues above. In his Honour's opinion, his disposition of these two issues left the proposed claim with slim prospects of success.

(ii) Section 237 of the Corporations Act

His Honour then turned to address the statutory leave application. There was no dispute as to the lack of probability that the Marina Company would bring the action itself. Nor was their dispute as to whether the notice required under s. 237(2)(e) had been satisfied.

As such, the contested issues before Applegarth J were those stated in ss. 237(2)(b), (c) and (d) which required his Honour to be satisfied that:

- the applicants were acting in good faith;
- it was in the best interests of the Marina Company that leave be granted; and
- there was a serious question to be tried.

In dismissing the application, his Honour dealt with each of the relevant subsections of 237(2) in reverse order. His reasons are summarised briefly below.

(iii) Serious question to be tried - s. 237(2)(d)

Applegarth J held it was "strictly unnecessary" to reach a conclusion on this issue on the grounds that the proposed claims had little, if any, prospect of success. His Honour felt that if the Marina Company did in fact have an arguable cause of action based upon the allegations made, this had not been demonstrated by the proposed statement of claim.

(iv) The best interests of the company - s. 237(2)(c)

On this issue, Applegarth J cited the comments made by Ball J in *Robash Pty Ltd v Gladstone Pacific Nickel Pty Ltd* (2011) 86 ACSR 432 (at [57]) with approval and also followed the statement of principle of the New South Wales Court of Appeal in *Oates v Consolidated Capital* (2009) 233 FLR 283:

> ... the sort of circumstance in which the bringing of the proceedings would be in the best interests of the company would be when the benefit that the company would derive from the bringing of proceedings outweighed the costs and risk that the company would suffer in bringing them.

In coming to his decision, his Honour weighed up a number of factors. His Honour felt that the slim likelihood of the success of the litigation, the cost of such and the risk of an adverse cost order, the lack of a personal indemnity from the applicants and the almost nugatory practical benefit of declaratory relief left him no choice but to find that the bringing of the proposed proceedings would not be in the best interest of the company.

(v) The applicant is acting in good faith - s. 237(2)(b)

On this point, his Honour followed the decision in *Coeur De Lion Investments Pty Ltd v Kelly* (2013) 302 ALR 771, citing Muir JA (at [57]):

> One would think it likely that an applicant under section 237, acting in good faith, would turn its mind to the question whether the amount

likely to be recovered in the litigation merited the expenditure of time, resources and money which litigation would necessitate.

When applying this reasoning to the present case, Applegarth J seemed more than wary of the applicants' intentions for bringing the derivative action. Since he had decided, however, to dismiss the application on another basis, namely the slim prospects of success of the proposed proceeding, his Honour reserved judgment on this issue of good faith.

6.2 Guidance as to the considerations relevant to an application for referral to a special referee under the Supreme Court of Victoria (General Civil Procedure) Rules 2005

(By Jared Lynch, Ashurst)

Bill Express Ltd (in liquidation) v Pitcher Partners (a Firm) [2014] VSC 482, Supreme Court of Victoria, Macaulay J, 26 September 2014

The full text of this judgment is available online.

(a) Summary

The Victorian Supreme Court has refused an application for an order under the Supreme Court (General Civil Procedure) Rules 2005 (Vic) (the General Civil Procedure Rules) referring questions to a special referee for the determination of an issue in litigation between Bill Express Ltd (by its liquidators) (Bill Express) and Pitcher Partners and KPMG. The Court also considered factors relating to the Civil Procedure Act 2010 (Vic) (the Civil Procedure Act).

Macaulay J found that the risk that referring the issue to a special referee would cause more delay and cost than it would avoid was real and not merely hypothetical. Further, the issue which Bill Express wished to have decided by an expert was, essentially, a question of law. Accordingly, to the extent that the issue that was to be referred was contentious, it was more appropriate that a court determine it, rather than a special referee.

(b) Facts

The application was made in respect of litigation between Bill Express and Pitcher Partners and KPMG. Pitcher Partners and KPMG audited the Bill Express financial

statements for various financial years before Bill Express went into liquidation on 12 August 2008.

In 2011, Bill Express sued Pitcher Partners and KPMG in relation to the audits of the company's financial statements. Bill Express claimed damages from each firm due to the allegedly defective conduct of those audits. No expert evidence concerning the key accounting and auditing issues on which the dispute turns had been produced and the full extent of the dispute about the accounting and auditing issues had not been fully illuminated.

The application related to assets that represented almost $50 million on Bill Express's balance sheet and their treatment in the financial statements of Bill Express. Bill Express applied under rl. 50.01 of the General Civil Procedure Rules for an order referring questions to a special referee (an accountant) for determination. The questions concerned the correct application of the Australian Accounting Standards (the Accounting Standards), made pursuant to s. 334 of the Corporations Act 2001 (Cth) (the Corporations Act), to the accounting treatment of particular assets in the company's financial statements.

Broadly, Bill Express alleged that the assets should not have been represented in Bill Express's balance sheet as its own assets. Both Pitcher Partners and KPMG denied that proposition. Bill Express tendered an expert report from Professor David Boymal (the Boymal Report).

Bill Express argued that the appointment of a special referee was appropriate and consonant with the overarching purpose to which a court must seek to give effect in the exercise of its powers (for example, the just, efficient, timely, and cost effective resolution of the real issues in dispute in civil proceedings, as provided for by the Civil Procedure Act).

Bill Express also proposed that the court make a series of directions to govern the procedure to be adopted by the special referee. Those directions would limit the involvement of legal representatives in the special reference and would maximise the referee's control of the conduct of the reference.

(c) Decision

In Macaulay J's view, the principal issues involved a consideration of the following factors:

- whether there was any utility in the proposed special reference;
- the extent to which the issue involved a legal question;
- the importance of the issue in the scheme of the dispute;
- the extent to which the facts necessary to determine the reference were uncontroversial;
- the extent to which there was a risk of re-litigation of the same issues; and

- the impact of each of the above factors on justice, efficiency, timeliness, and cost effectiveness.

(i) Utility

The Boymal Report identified 11 different issues concerning the proper application of Accounting Standards, of which the issue relating to the assets was only one. Macaulay J considered that the utility of the special reference was to be placed in a wider context. Ultimately, there was no special reason why the issue needed to be determined by a special referee, especially as the court would have to undertake a similar task in respect of the remaining accounting issues.

(ii) The extent to which the reference involves a legal question

In Macaulay J's view it was not appropriate to refer a question that involved the interpretation and construction of a legal standard before applying it to facts to a special referee, rather than a court. Further, the issue required findings of fact that would depend upon decisions about the admissibility of evidence and the credit of witnesses. As such, the critical analytical tools required legal reasoning and forensic experience and would be more appropriately dealt with by a court.

(iii) The importance of the issue in the scheme of the case

Macaulay J considered the importance of the issue as merely one factor to take into account in conjunction with the other matters. On balance, Macaulay J was not persuaded that, in the circumstances, this factor favoured the granting of the application.

(iv) The need to determine controversial facts

Generally, the greater the importance of the issue, the more latitude may be afforded to parties to engage in more forensically intensive, and potentially more time consuming and costly processes to advance or defend their interests.

Accordingly, other matters that are relevant in analysing this factor include:

- the extent to which matters are in controversy;
- the capacity of the parties to make effective representations to the referee in relation to matters in dispute without being afforded the traditional forensic processes; and
- the experience and qualification of the special referee in determining disputed factual matters.

(v) Risk of re-litigation

Macaulay J considered the risk that the opinions placed before the special referee may influence the determination of the other accounting issues, whether the referee's findings might impinge upon findings a court would need to make, and the risk of inconsistent findings of fact by the referee and the court. In Macaulay J's view, there was a potential risk that the auditors would be barred from conducting a full forensic testing of the relevant facts and the issue may have to be re-litigated.

(vi) Impact on justice, efficiency, timeliness, and cost effectiveness

Macaulay J analysed the impact on justice, efficiency, timeliness, and cost effectiveness in light of the uncertainty as to the degree of factual dispute and the prospect that the special reference may produce greater inefficiencies, particularly given the estimates provided to the Court by Bill Express assumed the Court would adopt the series of directions to govern the procedure to be adopted by the special referee.

(vii) Orders

Taking the above factors into account, Macaulay J decided that the questions of law that would potentially have to be determined would be more appropriate for determination by a judge than a special referee and refused Bill Express's application.

6.3 Costs order made in commercial litigation against successful party for misconduct overturned

(By Lachlan Salt, Ashurst)

Knight Frank Australia Pty Ltd v Paley Properties Pty Ltd [2014] SASCFC 103, Full Court of the Supreme Court of South Australia, Sulan, Blue and Parker JJ, 22 September 2014

The full text of this judgment is available online.

(a) Summary

Citing misconduct both before and during the trial, a trial judge made costs orders against a successful party to a contract dispute arising out of a failed commercial property transaction. The decision was successfully appealed, with the Full Court of the Supreme Court of South Australia finding that the trial judge had failed to identify the conduct said to constitute the relevant misconduct, and also finding that there was an inherent inconsistency in the trial judge's orders as to costs between the parties at

first instance. A cross-appeal against the trial judge's costs orders as they related to the unsuccessful party at first instance was also allowed.

(b) Facts

The plaintiff, Paley Properties, retained Mr Gambranis, an employee of the land agent Knight Frank Australia, to sell a commercial property. Mr De Chellis made an offer to purchase the property in the name of De Chellis Homes Pty Ltd (De Chellis Homes). The sale did not proceed. Paley Properties sued De Chellis Homes (the first defendant), Mr De Chellis (the second defendant), Knight Frank Australia (the third defendant) and Mr Gambranis (the fourth defendant). De Chellis Homes also brought a third party claim against the land agents, Knight Frank Australia and Mr Gambranis. The trial judge dismissed the action and consequentially the third party action.

The trial Judge made orders that, despite their being successful, Knight Frank Australia and Mr Gambranis pay the costs of action of Paley Properties against Mr De Chellis, and Mr De Chellis's solicitor and client costs on the basis of Mr Gambranis's misconduct. Paley Properties was to pay De Chellis Homes' costs of action. No order as to costs of the third party action was made.

Neither party on appeal sought to disturb the costs orders in so far as they were made in favour of De Chellis Homes or Mr De Chellis. Knight Frank Australia and Mr Gambranis (who were jointly represented) appealed against the other cost orders of the trial Judge, and Paley Properties cross-appealed the other costs orders.

The arguments on appeal of Mr Gambranis and Knight Frank Australia were that the alleged misconduct variously identified by the trial Judge as taking place before and during the trial did not amount to misconduct as recognised by the authorities and did not justify them being deprived of costs as against Paley Properties, and further that the trial Judge was inconsistent in her identification of the alleged instances of misconduct. Paley Properties' arguments on cross-appeal were that the trial Judge acted inconsistently and erred in ordering that Mr Gambranis pay its costs of action as against Mr De Chellis but not ordering that Mr Gambranis also pay its costs of action as against him, and further that the trial Judge erred in not making an order that Mr Gambranis pay its costs of action against De Chellis Homes and that it be indemnified by Mr Gambranis for De Chellis Homes' costs of action which it was required to pay.

(c) Decision

Blue J allowed both the appeal and the cross-appeal, delivering a judgement with which Sulan and Parker JJ agreed. The costs orders of the trial judge were set aside (except for the order that there be no order as to costs of the third party action (and possibly the orders made in favour of the De Chellis parties)).

Blue J commenced by noting the general rule that costs follow the event, except in

situations such as when the costs of litigation have been incurred or increased by a party's misconduct.

His Honour said that the first step is to determine whether the conduct of a party constitutes misconduct within the meaning of established authorities. The second step, if there is misconduct, is to analyse whether, and if so, the extent to which, the misconduct caused the litigation, its continuation or extent. The third step, if there is causation, is to determine the appropriate costs order.

Blue J considered that the trial Judge's discretion miscarried because she did not clearly identify the precise conduct of Mr Gambranis said to amount to misconduct, why this caused costs to be incurred in the litigation and finally whether the land agents should be deprived of their own costs, pay their opponents' costs on a party and party basis or pay their costs on a solicitor and client basis.

His Honour also concluded that there was an inherent inconsistency in the trial Judge ordering the land agents to pay Paley Properties' costs of action as against Mr De Chellis but not ordering the land agents to pay Paley Properties' costs of action as against the land agents.

Although Mr Gambranis's conduct of deliberately misleading Paley Properties to believe that he had communicated acceptance to Mr De Chellis on 20 August 2009 constituted both relevant misconduct and one cause of the proceedings being instituted, Paley Properties was also found to be at fault in instituting the proceedings even though it should have been obvious that its action for breach of contract and for breach of warranty was bound to fail. Accordingly, given there were two concurrent causes of the litigation against the De Chellis parties and both Paley Properties and the land agents were at fault, his Honour considered it appropriate that each of the parties bear their own legal costs.

As neither party sought to disturb the costs orders by the trial Judge in favour of the De Chellis parties, Blue J said the parties should be heard on whether the Court should order each party to pay 50% of the De Chellis parties' costs of action or each party should indemnify the other as to 50% of the costs payable to the De Chellis parties.

6.4 Court grants orders relating to the liquidation of companies in the RiverCity MotorWay Group

(By Daniel Kornberg, DLA Piper)

Owen, in the matter of RiverCity Motorway Limited (Administrators Appointed) (Receivers and Managers Appointed) [2014] FCA 1008, Federal Court of Australia, Greenwood J, 18 September 2014

The full text of this judgment is available online.

(a) Summary

On 11 September 2014, the Federal Court of Australia made orders in relation to the liquidation of ten companies in the RiverCity Motorway Group (RCM Group).

A week later, Greenwood J pronounced reasons for some of the orders given. His Honour confirmed that the liquidators should continue to monitor and investigate the claims made in three separate proceedings in NSW (the NSW Proceedings) relating to some of the companies in the RCM Group and approved the remuneration of the liquidators out of the trust assets of a managed investment scheme.

Additionally, his Honour held that liquidators are not "officers" of the company being liquidated for the purposes of the Corporations Act 2001 (Cth) (the Corporations Act), extended the time by which the liquidators had to comply with their reporting obligations under the Corporations Act and confirmed the validity of the appointment of the Committee of Inspection (COI).

(b) Facts

Eight of the ten companies in the RCM Group have had receivers and managers appointed to them. Of the two entities in the RCM Group that have not yet had receivers and managers appointed, one is RiverCity Management (RC Management), which is responsible for two managed investment schemes. The other is RiverCity Holdings (RC Holdings), the entity that wholly owns RC Management. The applications for orders by the former administrators of companies in the RCM Group in this matter principally concern RC Management and RC Holdings.

Greenwood J gave his reasons for the orders on 18 September 2014. His Honour did not give reasons for each of the orders given, but addressed the rationale behind some of the orders he granted on the basis of the following topics:

- directions and orders as to the conduct of the NSW Proceedings to which companies in the RCM Group are or may become party;
- approval of certain remuneration (and consequential orders);
- whether the liquidators of RC Management are "officers" of that company for the purposes of the Corporations Act;
- the validity of the appointment of two Committees of Inspection; and
- ancillary procedural orders.

(c) Decision

The reasons for the orders of Greenwood J are addressed in accordance with the topics as listed above.

(i) Directions related to proceedings in NSW

Previously, court orders were granted under s. 447D of the Corporations Act to the effect that it was a proper exercise of the powers and functions of the administrators to cause RC Management to engage in monitoring and investigating the claims made in the NSW Proceedings. They were, therefore, entitled to take such steps as might be ordered by the Court as well as taking steps regarding insurance and legal advice. As those administrators have since become the company liquidators, they now seek directions under s. 511(1) of the Corporations Act to the same effect as those previously granted.

Under s. 511 of the Corporations Act, a liquidator may apply to the Court to determine any question arising in the winding up of a company. For the Court to give directions in regard to liquidation, per Goldberg J in *Re Ansett Australia (No 3)* (2002) 115 FCR 409, there must be more than the making of a business or commercial decision, and concern power, propriety or reasonableness. The applicants here stated that a question of propriety and reasonableness arises here as there are two courses of action available to the liquidator in relation to the NSW Proceedings; they could either take no further role or continue to monitor and investigate in the ways described above.

Greenwood J held that as it was in the best interests of the creditors for the liquidators to monitor and investigate the claims made in the NSW Proceedings, it is proper and reasonable for the liquidators to take such a course.

(ii) The right of indemnity out of the trust assets and apportionment

The liquidators of RC Management will necessarily incur costs and expenses in carrying out some of the orders, including the monitoring and investigation of the claims in the NSW proceedings. They will subsequently have a right to be, and priority in being (under s. 556 of the Corporations Act), remunerated in respect of the work that gave rise to those costs.

As RC Management is a trustee of the two managed investment schemes, they would be entitled to be indemnified out of the trust fund so long as they have properly performed and discharged their duties in relation to the trusts.

The responsible entity of a registered scheme, in this case RC Management, according to s. 601GA of the Corporations Act, only has rights to be indemnified out of scheme property in relation to liabilities or expenses incurred in relation to the performance of its duties if those rights are specified in the scheme's constitution. In this instance the

provisions in the scheme's constitution stipulated that if the responsible entity is found by a court to be in breach of trust or negligent, those costs are to be repaid.

This provision led to concerns from the liquidators that if RC Management is found to be have breached the trust or acted negligently, the liquidators may be put in a position where they would have to make repayments from their personal funds to RC Management to reinstate the trust funds.
The liquidators, therefore, sought an order to confirm whether they are entitled to be indemnified directly out of the assets of each trust for the expenses and costs in complying with the orders, rather than relying on RC Management's right of indemnity as set out under the constitution.
Greenwood J agreed with the applicants that it is appropriate to allow the liquidator direct recourse from the assets of the trust as the work that is required to be undertaken by the liquidators to comply with the orders will benefit the trusts and their beneficiaries. Further, the liquidators are better placed than anyone else to undertake any work in relation to this in a cost-efficient manner.

Additionally, his Honour held that the costs, expenses and remuneration of the liquidators be applied proportionately from the assets held by each of the two trusts at the time in which the liquidators exercise a right of direct indemnity in order to ensure that the trusts share the burden of remuneration between them.

(iii) Are the liquidators of RC Management "officers" for the purpose of the Corporations Act?

The Corporations Act provides that an officer of a responsible entity of a registered scheme must, as a priority, act in the best interests of the members, even if it conflicts with the interests of the responsible entity.

As the liquidator owes its duties to the general body of creditors, not to the scheme members, a contrary intention to the general definition of "officer" under the Corporations Act arises. As such the liquidator of a responsible entity will not be considered an officer.

Additionally, Greenwood J granted an extension of the time by which RC Management had to comply with its reporting obligations under the Corporations Act as his Honour deemed that no substantial injustice has been or was likely to be caused to any person in doing so.

(iv) Questions concerning the validity of the appointment of the Committees of Inspection

The Corporations Act provides that the liquidator of a company must, if so requested by a creditor or contributory, convene separate meetings of the creditors and

contributories for the purposes of determining whether a COI should be appointed and who should be appointed to it.

The liquidators sought orders to ensure that the COI had been validly appointed.

His Honour concluded that as there was no request for separate meetings from the creditors or contributories, no separate meetings needed to be held for these purposes, and as such made the order that the COI had been validly appointed.

(v) Additional procedural orders

Greenwood J determined that as no resolution was passed fixing the former administrator's remuneration, it must be fixed by a court. His Honour was satisfied that the information contained in the affidavit supplied by the applicants was sufficient to make such an order.

Additionally, his Honour made a non-publication order to preserve the confidentiality of particular material contained in the affidavit and submissions on the ground that the order is necessary to prevent prejudice to the proper administration of justice.

6.5 Court orders compensation against a director involved in a misappropriation of company funds and a trustee who knowingly participated in the misappropriations

(By Tom Ward, Minter Ellison)

MHM Metals Ltd v Rogers [2014] FCA 1006, Federal Court of Australia, Davies J, 18 September 2014

The full text of this judgment is available online.

(a) Summary

This is a case involving both a director improperly using his position as director to gain benefits for himself and entities with which he was associated, and a trustee knowingly assisting the director with knowledge of the director's dishonest and fraudulent design.

(b) Facts

MHM Metals Ltd (MHM) alleged that Mr Frank Rogers, its former managing director misappropriated company funds and breached his statutory and fiduciary duties to

MHM during his tenure as managing director. MHM also alleged that Rogers Southern Pty Ltd (Rogers Southern), which Mr Rogers controlled, knowingly participated in the misappropriations and breaches of duty.

The claims arose in relation to a contract that MHM entered into with Tasmanian Adventure Cruises Pty Ltd (TAC) in May 2008 to supply MHM with a survey vessel named the Ocean Voyager for $350,000. Subsequent to the purchase from TAC, the Ocean Voyager was to be refitted to MHM's specifications. TAC engaged Rogers Engineering, of whom Mr Rogers was a director, to do the refit on the vessel.

MHM claimed that the Ocean Voyager was a worthless wooden vessel owned by Mr Rogers's family trust, and that Mr Rogers, through the contract with TAC, procured MHM to purchase the Ocean Voyager, without disclosing to the Board the true ownership of vessel or that Rogers Engineering was to undertake the refit.

MHM further alleged that Mr Rogers used the funds paid by MHM to buy a replacement yacht for the family trust called Taurus II.

The second respondent was Rogers Southern who is the trustee of Mr Rogers family trust. MHM claimed that by reason of Mr Roger's directorship with Rogers Southern, Rogers Southern had knowledge of Mr Rogers's breach of fiduciary duty and knowingly participated, induced and/or assisted Mr Rogers with the misappropriations.

MHM elected to pursue a claim against both Mr Rogers and Rogers Southern for compensation pursuant to s. 1317H of the Corporations Act 2001 (Cth) (the Corporations Act) to recover the damage it claimed to have suffered. MHM quantified that loss as $584,581. Section 1317H of the Corporations Act provides that a Court may order a person to compensate a corporation for damage if the person has contravened a corporation civil penalty provision in relation to the corporation and the damage resulted from the contravention.

(c) Decision

Davies J ordered that both Mr Rogers and Rogers Southern pay MHM $548,581 compensation pursuant to s. 1317H of the Corporations Act.

Davies J was satisfied Mr Rogers, by his conduct, brought about the sale of a vessel owned by his family trust to MHM, without disclosure to the Board of his family trust's ownership of the vessel or his interest in the transaction or that Rogers Engineering would be doing the refit.

It was therefore held that Mr Rogers, in procuring and committing MHM to purchase the Ocean Voyager, improperly used his position as director of MHM to gain benefits for himself and entities with which he was associated. Accordingly, Davies J found that Mr Roger's conduct was in breach of his duties under ss. 181 (good faith), 182

(use of position) and 183 (use of information) of the Corporations Act and that through the TAC contract Mr Rogers misappropriated MHM's funds.

Davies J considered that the claim against Rogers Southern was based on the second limb of *Barnes v Addy* (1874) LR 9 Ch App 244 (*Barnes*). Lord Selbourne held in *Barnes* at 251 that:

> [The responsibility of a trustee] may no doubt be extended in equity to others who are not properly trustees, if they are found ... actually participating in any fraudulent conduct of the trustee to the injury of the *cestui que* trust. But, on the other hand, strangers are not to be made constructive trustees merely because they act as the agents of trustees in transactions within their legal powers, transactions, perhaps, of which a Court of Equity may disapprove, unless those agents receive and become chargeable with some part of the trust property, or unless they assist with knowledge in a dishonest and fraudulent design on the part of the trustees.

Davies J stated that to succeed under the second limb it must be shown that the person gave assistance to a fiduciary with knowledge of a "dishonest and fraudulent design on the part of the trustee or fiduciary" (*Farah Constructions Pty Ltd v Say-Dee Pty Ltd* [2007] HCA 22). Given that Mr Rogers was the controlling mind of Rogers Southern, Davies J found that his knowledge of his own dishonest and fraudulent design was to be imputed to Roger Southern.

Finally, Davies J held that the finding that Rogers Southern had knowledge of Mr Rogers's dishonest and fraudulent design was sufficient to support a finding that Rogers Southern was "knowingly concerned" in Mr Rogers's breaches and by s. 79(c) of the Corporations Act, was therefore "involved in" Mr Rogers's contraventions for the purposes of s. 1317H(1) of the Corporations Act (*Chameleon Mining NL v Murchison Metals Limited* [2010] FCA 1129 at [1101] - [1104].

Accordingly, both Mr Rogers and Rogers Southern were ordered to pay MHM compensation in the amount of $548,581.

6.6 Can a company's constitution oust the discretion of directors to pay dividends?

(By Stan Lewis and Katrina Sleiman, Corrs Chambers Westgarth)

Wambo Coal Pty Ltd v Sumiseki Materials Co Ltd [2014] NSWCA 326, Supreme Court of New South Wales, Court of Appeal, Bathurst CJ, Beazley P, Barrett JA, 17 September 2014

The full text of this judgment is available online.

(a) Summary

The case concerned an appeal brought by Wambo Coal Pty Ltd (Wambo) and its sole ordinary shareholder, Peabody Australia Mining Ltd (PAML), against a decision of the primary judge in which it was held that Wambo had failed to pay its sole B class shareholder, Sumiseki Materials Co Ltd (Sumiseki), dividends to which it was entitled under Wambo's constitution.

The decision is noteworthy for several reasons, including that the constitution could vary the usual discretion of directors in determining if a dividend should be paid and the Court's rejection of the argument that it could order rectification of a company's constitution.

In dismissing the appeal, the Court considered whether on its proper construction, a provision in Wambo's constitution mandating the payment of dividends had the effect of ousting the discretion of the directors as to whether or not dividends should be paid. The Court considered that it did, subject to any obligations arising under law.

The Court also held that Wambo's conduct in entering into a loan agreement with PAML which included certain debt covenants designed to assist Wambo in denying the payment of dividends to Sumiseki, amounted to oppressive conduct.

(b) Facts

Wambo has two shareholders. PAML held all of the ordinary shares and Sumiseki held all of the B class shares. Sumiseki's holding was obtained in accordance with a written contract dated 29 June 2001 referred to as the "restructure agreement". The parties to that contract were Sumiseki, Wambo and Hunter Coal Co Pty Ltd (Hunter). At that time, Hunter was Wambo's sole shareholder.

Article 2.1B of Wambo's constitution stated that "[d]espite any provision in this Constitution to the contrary" the holder of a B class share had the right "to receive a dividend in respect of the six month period commencing [date stated] and ending [date stated] equal to" a particular fraction of "an amount equal to the profit of the Company available for dividend purposes for" the period "based on" the company's accounts for the period, which dividend was "to be paid" by a specified date following the expiration of the period. Article 2.1B was inserted into Wambo's constitution in 2001 pursuant to the restructure agreement.

Other provisions of the constitution (which predated article 2.1B) empowered the directors to "declare and pay such interim and final dividends as, in their judgment, the financial position of the company justifies"; to capitalise profits and effect bonus share issues; to set aside out of profits such "reserves or provisions" as they thought fit and carry forward so much of the profits remaining as they considered ought not to be distributed as dividends or capitalised without transfer to a "reserve or provision".

On 27 March 2010, Wambo and PAML entered into a loan agreement (the Loan Agreement) containing a debt service cover ratio covenant. The covenant did not exist in any prior loan agreement between the parties.

Wambo's directors did not pay dividends on B class shares in respect of five half-year periods between 2009 and 2011. Wambo's accounts for each of the periods disclosed profits. On each occasion, Wambo's directors approached the dividend right attached to the B class shares on the basis that profits were, as referred to in article 2.1B, "available for dividend purposes" only if and to the extent the directors determined they were so available and it was for the directors to determine whether there should be any distribution of those profits by way of dividend. For three of the five periods, non-satisfaction of financial covenants in the Loan Agreement was expressed to be one of the reasons for the board's decision not to pay dividends on the B class shares.

Sumiseki brought proceedings in the Equity Division against Wambo alleging an entitlement to dividends in respect of those periods. The primary judge found that article 2.1B conferred a right on Sumiseki, as the holder of the B class shares, to be paid dividends for the relevant periods regardless of any decision of Wambo's directors that such dividends should be paid, that Wambo's failure to pay the dividends in respect of those periods amounted to oppressive conduct within s. 232 of the Corporations Act 2001 (Cth) (the Corporations Act) and that an order should be made pursuant to s. 233(1)(b) to vary Wambo's constitution to better secure Sumiseki's dividend rights. A claim by Sumiseki for an order rectifying Wambo's constitution (or, alternatively, the restructure agreement) was dismissed. Wambo appealed.

(c) Decision

(i) Did Wambo's constitution entitle Sumiseki to the right to receive a dividend to the exclusion of any discretion given to Wambo's directors?

Wambo and PAML submitted that article 2.1B, on its correct construction, incorporates the long-standing and well understood power of directors to decide whether the interests of the company require all or some of profits otherwise distributable to be retained rather than being made available as dividends. They pointed out that article 2.1B does not regulate or control all aspects of the process and that missing components can be supplied by article 9.1(a) which leaves discretion with the directors, which discretion, it was submitted, is maintained in relation to dividends on B class shares as well as other dividends. It was submitted that profits of a period

are "available for dividend purposes" only if the directors have not determined to deal with them in some other way.

The Court held that while distribution of profits as dividends is usually a matter for the internal management of a company, on a proper construction of Wambo's constitution, the B class dividend was a mandatory dividend that becomes payable by Wambo on each date for payment specified in article 2.1B, and did not require any separate decision that it should be declared or paid, and absent any legal prohibition preventing it from doing so, the company was obliged to pay it.

The Court considered a number of authorities in considering the phrase "profits available for dividend purposes" and concluded it cannot be said the decided cases indicate some fixed meaning of that phrase. Rather, the meaning depends very much on context. In this context, the phrase refers to the period's net profit attributable to members undiminished by any discretionary applications of the directors' powers conferred by other provisions of the constitution but subject to such diminution, if any, as is required by law.

(ii) Did the decision of Wambo's directors not to pay dividends amount to oppressive conduct within the terms of s. 232?

The Court held that objectively fair behaviour within Wambo entailed adherence to the established course of conduct with respect to B class dividends. Sumiseki had a right that made it unfair on equitable principles for Wambo to depart from that course and, in particular, to resort to the proposal for revision of the Loan Agreement put forward by PAML as a means of doing so. While the Loan Agreement covenants did not play a direct part in two of the five relevant decisions not to pay B class dividends, the adoption of the contractual constraint was a means of unfairly bolstering the asserted ability of Wambo to deny dividends.

The Court upheld the primary judge's finding that Wambo's conduct was within the composite description in s. 232 of the Corporations Act ("oppressive to, unfairly prejudicial to, or unfairly discriminatory against, a member").

(iii) Was the order under s. 233(1)(b) that article 2.1B be modified in a way to give more certainty of meaning "as and from 29 June 2001" of any force or effect, having regard to s. 137?

Wambo and PAML submitted that the Court had no power to make the order amending the constitution under s. 233(1)(b) of the Corporations Act which says that the court can "make any order under this section that it considers appropriate in relation to the company", including an order "that the company's existing constitution be modified or repealed". They pointed to s. 137 of the Corporations Act which says that if an existing constitution is modified or repealed, the modification or repeal takes effect:

b. if it is the result of a Court order made under s. 233:
    i. on the date on which the order is made if it specifies no later date; or
    ii. on a date specified by the order.

It was submitted that, because of s. 137(b) and the statement in the order that the constitution was to be modified from a past date, that is, "as and from 29 June 2001", the modification purportedly effected by the order was in terms not authorised by the legislation and was therefore ineffective. This submission was rejected.

In the present case, the order specified 29 June 2001 as the date on which the modification was to have effect. Because the order specified a past date "as and from" which the modification was to be effective, s. 137(b)(i) caused the modification to have effect from the date on which the order was made, thereby depriving the order of the retrospective operation envisaged by its express terms.

The Court, however, held the fact that one provision of the Corporations Act (s. 137(b)(i)) caused an order made by a court under another provision (s. 233(1)(b)) to have an effect not wholly coinciding with the express terms of the order does not call into question the validity or regularity of the order. Since the specification of the past date in the primary judge's order had no force, for the sake of good order and clarity, the Court varied the order by omitting the words "as and from 29 June 2001".

(iv) Did the primary judge err in holding that equity's rectification jurisdiction does not extend to a company's constitution?

The Court held that notwithstanding recent statutory developments, equity's rectification jurisdiction still does not extend to a company's constitution.

(v) Did the primary judge err in declining to make an order rectifying the restructure agreement?

The Court held that the fact that rectification of the restructure agreement could not produce any result beyond that already achieved by the judge's s. 233(1)(b) order, coupled with the principle that equity does not act in vain, means that the discretionary jurisdiction should not be exercised.

The Court dismissed the appeal.

6.7 A controller, who is really a receiver, who is not anymore because he is not a registered liquidator

(By Flora Ho, Clayton Utz)

Yarrawonga Earthmoving & Garden Supplies Pty Ltd v Clem Court Pty Ltd [2014] VSC 439, Supreme Court of Victoria, 11 September 2014

The full text of this judgment is available online.

(a) Summary

The plaintiffs and the defendants entered into a series of transactions, which the plaintiffs later argued were voidable for the defendants' breach of fiduciary duties owed to the plaintiffs. The Court accepted that there was an arguable case of breach and that, on the balance of convenience, injunctive relief should be granted to restrain the defendants from exercising a charge and enforcing a debt against the plaintiffs. Further, pursuant to a charge granted by the plaintiffs, the defendant had appointed a "controller" over certain charged property. The Court found that the controller was in fact a receiver, but since he failed to meet the statutory criteria for receivers, his appointment was declared invalid.

(b) Facts

Two companies, Yarrawonga (the first plaintiff) and Clem Court (the first defendant), entered into a Deed of Charge (the Charge) in 2007, whereby Yarrawonga charged in favour of Clem Court the whole of its undertaking and assets, both present and future. The Charge was entered into as part of a series of transactions between Yarrawonga and Bodycoat (the second plaintiff) on the one hand and Clem Court and Allan Walker (the second defendant) on the other. Notably, Mr Walker, who controlled Clem Court, was also the accountant and financial advisor of Yarrawonga.

The series of transactions involved a transfer of land (Yarrawonga Property) from Bodycoat to Clem Court, a loan from Clem Court to Yarrawonga, the Charge, a lease of the Yarrawonga Property to Yarrawonga and several money transfers between the parties. They were entered into the advice of Mr Walker, at time when Yarrawonga was short of cash.

Upon default by Yarrawonga under the Charge in February 2014, Clem Court appointed Keith Sutherland as receiver and manager to the company and Allan Walker as controller over the charged property. Mr Sutherland subsequently resigned as receiver and Mr Walker was replaced by Neil Viney as controller.

In April 2014, pursuant to the appointment of Mr Viney as controller, Clem Court took possession of the Yarrawonga Property. In addition, in August 2014, Mr Viney proposed to auction Yarrawonga's earth moving equipment, which proceeds were anticipated to go to Clem Court in extinguishment of Yarrawonga's loan.

The plaintiffs sought three forms of interlocutory relief:

- firstly, a declaration pursuant to s. 418A of the Corporations Act 2001 (Cth) (the Corporations Act) that Mr Viney's appointment was invalid;
- secondly, an injunction, pending the outcome of proceeding, prohibiting the defendants from enforcing particular security interests against the plaintiffs; and
- thirdly, an order requiring the defendants to deliver up possession of the Yarrawonga Property pending the outcome of proceeding.

(c) Decision

(i) Was Mr Viney's appointment valid?

The plaintiffs sought a declaration, pursuant to s. 418A of the Corporations Act, that Mr Viney's appointment was invalid on the basis that he was not a registered liquidator and therefore failed to meet the statutory criteria for receivers under s. 418 of the Corporations Act. That section relevantly provides that "a person is not qualified to be appointed, and must not act, as receiver of property of a corporation if a person ... (d) is not a registered liquidator".

The defendant argued that s. 418 of the Corporations Act did not apply to Mr Viney, because he was appointed as a "controller" and not a "receiver". That argument was rejected by Chief Justice Warren of the Supreme Court of Victoria. Her Honour noted that the definition of "controller" in s. 9 of the Corporations Act includes those acting as receivers, but is not limited to them. For example, a mortgagee in possession and its agent can be a "controller" for the purposes of the Corporations Act.

To determine the nature of Mr Viney's appointment, it was considered necessary to pay close attention to the terms of the Charge, being the source of Clem Court's power to appoint a receiver or controller. Under the Charge, extensive provisions were made for the appointment (and powers) of a "receiver". Whilst the word "controller" was not used in the Charge, clause 8 provided that "the Chargee may exercise the power and discretions conferred on the receiver whether or not such a receiver has been appointed under the Charge". "Chargee" was in turn defined to include the Chargee's "successors and assigns", but not its employees or agents. From these provisions, the Court inferred a power of Clem Court to appoint a "controller" to the charged property of Yarrawonga. Nevertheless, the appointee, the subject of such power, must either be a successor or an assign of Clem Court's security interest over Yarrawonga. In the present case, Mr Viney was neither.

In those circumstances, and having regard to the fact that the property covered by the Charge was the whole of Yarrawonga's present and future assets and undertakings (which means the appointment of Mr Viney would affect all of Yarrawonga's creditors, whose interests are intended to be protected by the criteria for receivers set out in s. 418 of the Corporations Act), the Court found that Mr Viney must be taken to

have been appointed as a receiver, notwithstanding the notification to ASIC and the Deed of Appointment which purported to appoint him as a controller. It followed that s. 418(1)(d) applied and required that Mr Viney be removed as a receiver of Yarrawonga. The declaration sought under s. 418A of the Corporations Act was accordingly made.

(ii) Injunctive relief and order to deliver up possession

As regards the application for injunction and the order for possession of the Yarrawonga Property, the plaintiffs were able to establish an arguable case that:

- Mr Walker, being the plaintiffs' accountant and financial advisor, was the fiduciary of Yarrawonga and Bodycoat. This was the especially the case since Mr Walker was in charge of the bank accounts, tax returns and bookkeeping for Yarrawonga and, as such, occupied a position of trust within Yarrawonga;
- Yarrawonga and Bodycoat entered into the series of transactions with Clem Court (a company owned and controlled by Mr Walker) on the advice of Mr Walker;
- the transfer of the Yarrawonga Property and the loan agreement between Clem Court and Yarrawonga were liable to be set aside in equity because Walker was a fiduciary, and he had acted contrary to the interests of the plaintiffs and the legal principle that a fiduciary must not enter into a transaction with its principal unless the principal has given its fully informed consent. The decision in *Maquire & Tansey v Makaronis* (1997) 188 CLR 499 was relied upon as the authority for that principle; and
- significant money had flowed both ways, and it was impossible to ascertain who owed what amount of money to whom. It followed that an account between the parties was necessary and the Charge should not be exercised until that account occurred.

Given the circumstances of the transaction, in particular, the lack of evidence of informed consent (in respect of which the defendants bore the onus of proof), the Court was satisfied that the plaintiffs had an arguable case such that the injunction sought and the order for delivery of possession should be granted into order to preserve the status quo until matters were able to be resolved at trial.

The Court was also satisfied that the balance of convenience fell in favour of the plaintiffs, in that:

- the auction of the earth moving equipment was proposed by an invalidly appointed receiver;
- the auctioneer was likely to act on the instructions of the invalidly appointed receiver;
- any proceeds received from the auction would go to Clem Court to extinguish a debt that was potentially voidable;
- the auction would be conducted under a charge that might be set aside;

- the basis on which Clem Court re-entered the Yarrawonga Property had changed; and
- the flows of money between the parties should be investigated and brought to account.

The Court therefore ordered that the defendants be restrained from exercising the Charge and from enforcing the debt against the plaintiffs. The Court further ordered that the defendants deliver up possession of the Yarrawonga Property.

6.8 Breach of fiduciary duty by director intending to act on behalf of corporate group

(By Rebecca Hahn and Will Heath, King & Wood Mallesons)

Allco Funds Management Limited (Receivers and Managers Appointed) (In Liquidation) v Trust Company (RE Services) Limited (in its capacity as responsible entity and trustee of the Australia Wholesale Property Fund) [2014] NSWSC 1251, Supreme Court of New South Wales, Hammerschlag J, 11 September 2014

The full text of this judgment is available online.

(a) Summary

The plaintiff entered into a deed of amendment with the defendant that had the effect of making the payment date of the loan agreement at the defendant's discretion. The directors of the appellant who executed the deed were also directors of the plaintiff. Receivers of the plaintiff sought rescission of the amending deed on three alternative grounds: (1) the directors had breached their fiduciary duties to the plaintiff; (2) the directors had breached ss. 181(1) and 182(1) of the Corporations Act 2001 (Cth) (the Corporations Act); and (3) the defendant was acting unconscionably.

Hammerschlag J ordered that both the amending deed and the original loan agreement be rescinded as the directors had breached their fiduciary duties and breached the Corporations Act when entering into both contracts.

(b) Facts

Allco Funds Management Ltd (AFML), the plaintiff, was a subsidiary of the failed Allco group. In 2008 receivers were appointed to AFML and in 2009 AFML was placed into liquidation. The receivers brought these proceedings on behalf of AFML. The defendant was Trust Company (RE Services) Limited (TCL) acting as the responsible entity of the Australia Wholesale Property Fund (the Fund). TCL became

the responsible entity of the Fund in February 2009; before this the responsible entity of the Fund was Record Funds Management Limited (RFML).

AFML held 109,687,077 units in the Fund. On 15 December 2006 a loan agreement was entered into between AFML and RFML (the Loan Agreement). Under the Loan Agreement AFML lent RFML $109,687,077 with a fixed repayment date of 31 January 2009. RFML immediately redeemed AFML's unit holdings to the value of $109,687,077. The rate of interest was equal to the amount unit holders would expect to receive on distribution. The effect of the Loan Agreement was to convert AFML's beneficial equity interest into a loan. Its purpose was to avoid stamp duty. Two directors committed AFML to the Loan Agreement, one of who was Timothy Rich, who was also a director of RFML. A director and a company secretary committed RFML to the Loan Agreement; the director was Christopher West who was also a director of AFML.

On 1 February 2007 AFML and RFML entered into a deed of amendment (the Deed of Amendment) to alter the repayment date from 31 January 2009 to the earlier of the date upon which the fund was to be terminated or the date upon which RFML received proceeds of subscription for further units which could be used to fully repay the loan and any accrued interest (the Repayment Date). The purpose of the agreement was to reclassify the loan as equity for the Fund and therefore improve profitability ratios. The Repayment Date had not arrived at the date of this judgment. Mr West was one of the two directors who committed AFML to the Deed of Amendment whilst Mr West and Mr Rich committed RFML to the Deed of Amendment. Mr Rich and Mr West gave evidence as to their belief that what they were doing was in the interests of the Allco group, including AFML.

AFML sought rescission of the Deed of Amendment.

(c) Decision

AFML sought rescission based on three discrete grounds. Hammerschlag J addressed these in turn. His Honour's analysis carried across the Loan Agreement and the Deed of Amendment, noting that AFML could not cherry pick which agreement it wished to have rescinded. His Honour emphasised throughout that the economic and legal rights of AFML had to be looked at isolated from the Allco Group.

(i) Fiduciary duty and conflict of interest

In relation to the Deed of Amendment Hammerschlag J concluded that Mr Rich and Mr West were clearly in a position of conflict as AFML has disparate economic and legal interests to RFML. This was so as by entering into the Deed of Amendment AFML had lost the right to be paid on 31 January 2009; instead the repayment date effectively became at RFML's discretion. It was irrelevant that by entering into the

Deed of Amendment the parties were enacting the intention present at the creation of the Loan Agreement (as TFC submitted).

Similarly, with regards to the Loan Agreement his Honour concluded that Mr Rich and Mr West had been in a position of conflict. As a unit holder, AFML was in a fiduciary relationship with RFML. Furthermore under the Corporations Act RFML was obliged to act in the best interests of the members at all times. By entering into the Loan Agreement AFML lost these benefits. Given these breaches of fiduciary duty by the directors, the fairness or unfairness of the transaction was irrelevant.

Hammerschlag J observed that, unless a company's constitution provides otherwise, a contract made in breach of fiduciary duty by a director will be voidable at the option of the company unless the director makes full disclosure of their interest to the company's members, who must approve the contract by ordinary resolution.

On these bases Hammerschlag J held that both agreements should be rescinded. Despite this his Honour considered in obiter the two alternative arguments raised.

(ii) Statutory duties

AFML alleged that Mr Rich and Mr West had breached ss. 181(1) and 182(1) of the Corporations Act. Section 181(1) requires directors "to exercise their powers and discharge their duties: (a) in good faith in the best interests of the corporation; and (b) for a proper purpose". Similarly s. 182(1) states that a director "must not improperly use their position to: (a) gain an advantage for themselves or someone else; or (b) cause detriment to the corporation". His Honour noted that these tests were both objective and therefore it was irrelevant that Mr Rich and Mr West had been acting *bona fide* in entering into both contracts. His Honour further observed that a transaction brought about by directors in breach of these duties will, if the counter-party entered into it with knowledge of the breach, be voidable at the instance of the company and rescission is available.

His Honour held that as the Deed of Amendment was clearly entered into to benefit the Fund and its members "no reasonable person in the position of Mr Rich and Mr West could reasonably and rationally have concluded that the Deed of Amendment was in the best interests of AFML". It could also be concluded from this that Mr Rich and Mr West had not acted for a proper purpose and in doing so had gained an advantage for RFML.

In the case of the Loan Agreement his Honour noted that it had caused economic detriment to AFML as it lost the opportunity to ever receive more than $1 per unit. AFML also lost its ability to vote with regards the management of the fund (although at the time this right was unavailable due to AFML's association with RFML). A further detriment caused was that AFML had been unable to participate in a prior capital reconstruction. His Honour emphasised that Mr Rich and Mr West had put their minds to the Allco group as a whole and in doing so had subordinated AFML's

economic and legal interests. Therefore, as with the Deed of Amendment, Mr Rich and Mr West were found to have breached ss. 181(1) and 182(1) of the Corporations Act.

Section 187 of the Corporations Act, allowing directors of a wholly owned subsidiary to vote in favour of the holding company, was considered irrelevant as it did not apply to ss. 181 and 182 of the Corporations Act and general law duties.

(iii) Unconscionability

Finally AFML argued that TCL had acted unconscionably in treating AFML as a bare lender when the intention of the dual agreements had been to have them treated as an equity holder. His Honour quickly dismissed this argument, noting that the assumptions of the parties were embodied in the contracts and these had not been departed from.

Hammerschlag J made two final observations: (1) that the existence of the unconscionability claim highlights that the agreements were not in the best interests of AFML; and (2) that although the argument was not raised, TCL had acted unconscionably under s. 12CB of the Australian Securities and Investments Commission Act 2001 (Cth).

6.9 Company's claim for restitution from a recipient of company funds rejected

(By Annabelle Crowe, Herbert Smith Freehills)

Russell Gould Pty Ltd v Ramangkura [2014] NSWCA 310, Supreme Court of New South Wales, Court of Appeal, Bathurst CJ, Barrett JA and Ward JA, 9 September 2014

The full text of this judgment is available online.

(a) Summary

A common law action for money had and received did not succeed because the appellant company could not demonstrate that the respondent recipient had received the company's legal property.

(b) Facts

An elderly couple, Mr Gould and Mrs Gould, and their son, were the only directors and shareholders of Russell Gould Pty Ltd, a family investment company (the

Company). Mr and Mrs Gould had substantial loan accounts in the Company's books since 2007, when they deposited with the Company the proceeds from the sale of their family home. Vilailaksana Ramangkura (the Defendant) was, from about 2002, a companion and carer to Mr and Mrs Gould.

On 12 April 2010, Mr Gould and the Defendant went to the Mosman Junction branch of Australia and New Zealand Banking Group Ltd. Mr Gould directed the bank to withdraw from a Company term deposit account $227,820.71 and to deposit that amount in the Defendant's home loan account (the Transaction). The Transaction cleared the Defendant of her home loan debt so that she held the associated property free from indebtedness. There is no doubt that Mr Gould was, as against the bank, authorised to direct the Transaction.

(c) Decision

(i) At first instance

The Company brought proceedings in the Equity Division of the Supreme Court of New South Wales against the Defendant alone and claimed judgment of $227,820.71. The Company also claimed that the Defendant held the associated property on constructive trust for the Company to the extent required to satisfy the judgment debt, including interest and costs.

The trial judge, Lindsay J, held that the Company had no claim against the Defendant because Mr Gould did no more than require payment by the Company of money owing and payable to him or to Mrs Gould (or both) and he or she (or they) then made a gift to the Defendant. The basis for Lindsay J's decision was a finding that by consensus among the three directors and shareholders of the Company, Mr Gould had implied authority to appropriate Company funds for his own use as and when he wanted, by way of partial repayment of the loan amounts owed to him (or to him and Mrs Gould).

(ii) On appeal

The Company appealed the trial judge's finding that Mr Gould had implied authority to direct the Transaction without the approval of the other directors.

The Company argued the following two alternative cases, both founded on Mr Gould's lack of authority to draw the magnitude of funds in the particular circumstances:

- that, if the Transaction was correctly characterised as a payment by the Company to Mr Gould (or Mrs Gould or both) by way of reduction of loan account, coupled with an immediate on-payment by that recipient to the Defendant, Mr Gould lacked the authority of the Company to cause it to make the payment to the initial recipient (or recipients); and

- that, if the Transaction was correctly characterised as a gift by the Company to the Defendant, Mr Gould lacked the authority of the Company to cause it to make such a gift.

Barrett JA (Bathurst CJ and Ward JA agreeing) dismissed the appeal and held that because the Company argued lack of authority, and did not allege any breach by Mr Gould of any duty owed by him to the Company as director, common law rules alone applied. Accordingly, the Company's claim rested on the common law restitutionary action for money had and received in which a money judgment is sought against the Defendant.

The court held that an action for money had and received lies principally against a receiving party (i.e. here, Mr Gould). In order to succeed in this action against another party to whom the initial recipient has in turn made payment (i.e. here, the Defendant) the Company had to prove that the Defendant held the Company's property. The crucial question was whether the money the Defendant received was Mr Gould's or the Company's. Mr Gould did not consider whether he was exercising his authority at the bank to withdraw the Company funds with or without reference to the loan amount owed to him. Because of the common law rule giving effect to the common morality of the community, it was inferred that Mr Gould withdrew the money that he was entitled to receive subject to his own demand and the Company's (here, evident) capacity to pay.

Neither at common law nor in equity can money be traced into the payment of an overdrawn account that remains overdrawn after the payment. Barrett JA noted therefore that the transaction gave the Defendant the benefit of freedom from indebtedness, but that does not constitute property. His Honour also noted in obiter that had equitable principles applied, tracing into the Defendant's real property might have been possible on the basis that the provider of money that caused the mortgage debt to be discharged was subrogated to the property right of the mortgagee whose debt was paid out; and an action for money had and received may lie against Mr Gould but it does not lie against the Defendant.

6.10 Security for costs order granted against plaintiff company: Consideration of relevant factors

(By James Siemon, Minter Ellison Lawyers)

In the matter of Elsmore Resources Ltd [2014] NSWSC 1247, Supreme Court of New South Wales, Black J, 8 September 2014

The full text of this judgment is available online.

(a) Summary

This case examines the basis for an application for security for costs against a plaintiff company, the approach that the courts will take in considering such an application, and the factors that the courts will take into account in determining whether to grant security for costs.

(b) Facts

Elsmore Resources Ltd (the Company), in a separate action, brought proceedings against the defendants in relation to matters arising from its listing on the Australian Securities Exchange, including claims that $2,209,000 in share subscriber fees held on trust by the second defendant, Periwinkle Investments Pty Ltd, had not been remitted to the Company on its listing. Summary judgment was granted by Brereton J (in *Re Elsmore Resources Ltd; Elsmore Resources Ltd v Ashley Grant Howard* [2014] NSWSC 953) against the first, second and fourth defendants, but not against the third defendant, Harry Fung, who is associated with the second defendant company.

The Company's claim against Mr Fung initially relied on his signing of a document purporting to set out terms of a settlement reached between the parties, including a personal guarantee given by Mr Fung, but subsequently expanded to include a claim against him for breach of trust and/or knowing assistance for breach of trust. Mr Fung therefore brought an application seeking orders for security for costs of $95,000 and that the proceedings be stayed until the security was provided.

(c) Decision

Black J referred to three bases with the potential to support the application for security for costs. These included the inherent power of the Court "to order security as an incident of its control over its own practice and procedure" and s. 1335 of the Corporations Act 2001 (Cth), which provides that "if it appears ... that there is reason to believe that the corporation will be unable to pay the costs of the defendant ... [the court may] require sufficient security to be given for those costs and stay all proceedings until the security is given".

The application was, however, primarily supported by rl. 42.21 of the Uniform Civil Procedure Rules 2005 (NSW) (the UCPR), which provides, in particular, at paragraph (1)(d) that:

> If, in any proceedings, it appears to the court on the application of a defendant ... that there is reason to believe that a plaintiff, being a corporation, will be unable to pay the costs of the defendant if ordered to do so ... the court may order the plaintiff to give such security as the court thinks fit, in such manner as the court directs, for the defendant's

> costs of the proceedings and that the proceedings be stayed until the security is given.

His Honour also noted the parties' agreement that the issues arising in this type of application were those identified in *Polstead Pty Ltd (in liq) v Shah* [2009] NSWSC 560 at [6], being:

- whether the grounds referred to in the rule are established;
- if those grounds are established, whether an order for security for costs should be made as a matter of discretion; and
- the quantum of any order to be made and the terms on which it should be made.

(i) Reason to believe that the Company may be unable to pay a claim for costs

In answering the question raised by rl. 42.21(1)(d) of the UCPR, Black J considered (by reference to various authorities) that the requirement would be satisfied "if there is a real chance, in events that are reasonably possible, that the relevant corporation will be unable to pay those costs", with the defendant bearing the initial onus of proving that there was reason to believe that possibility would occur and the plaintiff subsequently bearing the onus of establishing why security for costs should not be granted.

On the basis of concessions made by counsel for the Company, his Honour was satisfied that there was "reason to believe that the Company may be unable to meet an order for costs against it", given substantial net losses that had been reported by the Company and its involvement in other litigation.

(ii) Discretionary factors

His Honour then turned to examine discretionary factors by which the Company might establish that security for costs should not be ordered. Those factors included those set out by rl. 42.21(1A) of the UCPR, which his Honour considered to be broadly consistent with the guidelines identified in *KP Cable Investments Pty Ltd v Meltglow Pty Ltd* (1995) 56 FCR 189 at 197-198.

In the present case, his Honour particularly considered:

- whether the application had been brought in good faith;
- whether there had been any delay in bringing the application
- the strength and bona fides of the Company's case, including the complexity of the Company's case and the likelihood of its success against Mr Fung; and
- whether an order for security for costs would stultify the proceedings.

Finally, Black J considered the quantum of security that was appropriate on the facts of the case, including costs already incurred by Mr Fung in the proceedings. His

Honour therefore ordered the provision of $80,000 of security for costs to be paid in two tranches of $40,000, the first to be paid within 28 days and the second to be paid no later than 21 days prior to the final hearing of the proceedings. His Honour also ordered that the proceedings be stayed if security was not provided in accordance with those orders.

6.11 Court confirms validity of receivers acting in best interests of third parties: Application of the Personal Property Securities Act 2009 (Cth) to goods being held on bailment or consignment by a company in receivership and liquidation

(By Alex Cook and Adrienne Trumbull, King & Wood Mallesons)

Re Arcabi Pty Ltd (Receivers & Managers Appointed) (in liq); ex parte Theobald & Herbert in their capacities as receivers & managers of Arcabi Pty Ltd (Receivers & Managers Appointed) (in liq) [2014] WASC 310, Supreme Court of Western Australia, Master Sanderson, 4 September 2014

The full text of this judgment is available online.

(a) Summary

Theobald & Herbert (the Receivers) were appointed as receivers to Arcabi Pty Ltd (the Company). Some of the rare coins and bank notes (the Goods) held by the Company were not owned by the Company. The Receivers incurred costs insuring all Goods held by the Company and investigating the ownership of those Goods.

The court considered:

- the application of the Personal Property Securities Act 2009 (Cth) (the PPSA) to Goods being held on bailment or consignment by a company in receivership and liquidation; and
- the Receivers' rights to be indemnified for costs and expenses related to investigating and protecting the property of third parties.

(b) Facts

On 17 July 2013, the Receivers were appointed to the Company. The Receivers investigated the ownership of all Goods and found that some of the Goods were neither owned by the Company, nor were subject to security under the PPSA. The Receivers contended that these Goods should be returned to investors. To confirm this

view, and other proposed conduct, the Receivers sought directions from the Supreme Court of Western Australia under s. 424(1) of the Corporations Act 2001 (Cth).

In separate orders on 17 December 2013 and 15 May 2014, Master Sanderson gave directions to the Receivers. In this judgement, Master Sanderson gave reasons for his earlier directions and discussed the following legal issues:

- whether the PPSA affected the ownership of Goods stored on behalf of investors at the Company's premises (the Mixed Storage Goods);
- whether the PPSA affected the ownership of Goods held by the Company following requests by investors that the Company attempt to sell those Goods (the Consignment Only Goods);
- whether the Receivers were entitled to an indemnity supported by an equitable lien over the Company's assets where not all of the costs incurred related to the Company's Goods;
- whether insurance costs were incurred in the course of the receivership; and
- whether a contribution for insurance costs could be sought from investors.

(c) Decision

(i) Ownership of Mixed Storage Goods

The Mixed Storage Goods were held pursuant to bailments between the Company and investors. Master Sanderson considered whether these bailments of Goods constituted registrable "security interests" under ss. 12(1) or 12(3) of the PPSA. In doing so, Master Sanderson sought to determine whether s. 267 of the PPSA applied to vest ownership of these Goods in the Company.

Master Sanderson considered whether the bailments secured payments or obligations, and therefore constituted "in substance" security interests under s. 12(1) of the PPSA.

On these facts, the bailments were not "in substance" security interests because:

- the Goods did not vest in the Company on expiry of the bailments;
- the Company was not obliged to purchase the Goods;
- the bailments were not for the major part of the Goods' economic lives; and
- the nominal bailment fee did not equate to the Goods' capital costs.

Master Sanderson went on to consider whether the bailments were PPSA lease security interests under ss. 12(3)(c) and 13 of the PPSA. Under s. 13, a bailment will only be a PPSA lease where the bailor regularly engages in the business of bailing goods. Given that majority of the investors did not earn income from the bailment of Goods, Master Sanderson found that they did not regularly engage in the business of bailing goods (*Rabobank New Zealand Ltd v McAnulty* [2011] NZCA 212). If at all, any business conducted by the investors was limited to dealing in Goods.

The bailments did not constitute registrable security interests under the PPSA. As such, s. 267 of the PPSA did not apply to vest title in the Mixed Storage Goods to the Company. The investors were entitled to retrieve the Mixed Storage Goods.

(ii) Ownership of Consignment Only Goods

The Receivers argued that some of the Goods were provided to the Company on consignment and should therefore be returned to investors. As "consignment" is not well defined in Australian law, Master Sanderson drew on Canadian case law to determine whether the Goods had been consigned (*Re Stephanian's Persian Carpets Ltd and Access Cash International v Elliot Lake Inc* (*Re Stephanian's*)). On balance, Master Sanderson felt that a reasonable interpretation of the arrangements justified the recognition of consignments pursuant to which investors retained title.

In coming to this conclusion, Master Sanderson relied on the following key facts:

- resale request forms provided that the Goods remained property of investors;
- Consignment Only Goods were capable of being specifically identified; resale request forms provided that Goods could be retrieved at any time; and
- investors were required to pay storage fees for Consignment Only Goods.

Having recognised these consignments, Master Sanderson considered whether they created registrable security interests under ss. 12(2)(h) or 12(3)(b) of the PPSA.

Under s. 12(2)(h) of the PPSA, a consignment will be a registrable security interest where it secures a payment or performance of an obligation. Analogising these facts to the Canadian case of *Re Stephanian's*, there was no logical reason why the consignments secured debts due by the Company. The Company's obligation to pay investors only materialised upon the sale of Goods. Unsold Goods remained the property of investors and could be retrieved at any time. The consignments were mutually advantageous to the Company and the investors, and were not intended to secure any payment or other obligation by the Company.

Master Sanderson considered whether the parties' arrangements constituted commercial consignments under s. 12(3) of the PPSA. Similar to the position for bailments under s. 13, under s. 12(3)(c) of the PPSA, in order for a consignment to be commercial, the parties must regularly deal in goods of that kind in the ordinary course of business. Whilst consignments constituted a large part of the Company's business, a majority of the investors did not deal in Goods in the ordinary course of their business. As such, the consignments were not commercial under s. 12(3).

The PPSA did not apply to render the consignments registrable security interests. Accordingly, no security interest vested in the Company under s. 267 of the PPSA. Master Sanderson concluded that the Consignment Only Goods should be returned.

(iii) Entitlement of Receivers to an indemnity and equitable lien

It was settled law that Receivers have a right of indemnity and equitable lien over a Company's property to cover remuneration, costs and expenses. The issue in this context was the scope of the Receivers' indemnity, given that some of the Receivers' costs were incurred identifying investors' Goods.

Applying *Thackray v Gunns Plantations*, Master Sanderson found that the work undertaken by the Receivers in identifying and returning the investors' Goods was work forming part of the care and preservation of the Company. Without this process, the Receivers would not have been able to identify the Company's assets. The Receivers were entitled to be fully indemnified, supported by an equitable lien.

(iv) Insurance costs

The Receivers insured all Goods held by the Company before determining the Goods' owners. Master Sanderson considered that this approach was beneficial to all parties. Investors benefited as their Goods were protected. Additionally, the Company was protected from claims in relation to Goods being lost or destroyed. Given this, Master Sanderson confirmed that the Receivers should be indemnified for the insurance costs.

(v) Contribution from investors for insurance costs

In a situation where an Investor had expressly asked for insurance over their Goods to be continued, the Receivers had a *prima facie* case for requesting contribution. In other situations, the Receivers could only seek contributions on a restitutionary basis.

6.12 Delay in commencing proceedings and prejudice to third parties prevent an unfairly treated golfer from receiving a remedy

(By Peter Sise, Clayton Utz)

Re Peninsula Kingswood Country Golf Club [2014] VSC 437, Supreme Court of Victoria, Robson J, 3 September 2014.

The full text of this judgment is available online.

(a) Summary

A member of a golf club sought relief under s. 233 of the Corporations Act 2001 (Cth) (the Corporations Act) for alleged oppression and unfair prejudice arising from the merger of two golf clubs and the proposed sale of a golf course belonging to one of the

clubs. The member also sought relief under the Court's equitable jurisdiction. Robson J concluded that the member had been unfairly treated but declined to grant a remedy due to delay by the member in commencing proceedings and the effect a remedy would have on third parties.

(b) Facts

Kingswood Golf Club Ltd (Kingswood) was a company limited by guarantee. It owned an 18-hole golf course in Dingley Village, a suburb of Melbourne located approximately 25 kilometres from the central business district (CBD). If rezoned as residential land, the golf course would be worth approximately $71 million. Peninsula Country Golf Club (Peninsula) was an incorporated association that owned two 18-hole golf courses in Frankston, a suburb of Melbourne approximately 45 kilometres from the CBD and 20 kilometres from Dingley Village. If rezoned as residential land, the two courses would be worth approximately $72 million.

On 26 August 2013, an information booklet was circulated to members of Kingswood explaining that a special general meeting would be convened to vote on a proposed merger of Kingswood and Peninsula. The booklet said both Kingswood and Peninsula were facing financial difficulties and the merger would be for their benefit. A central feature of the merger was the sale of Kingswood's golf course in Dingley Village to a property developer in the next three to five years. Thereafter, all members of Kingswood would be expected to play golf in Frankston. In 2013, there were 1,705 members of Peninsula and approximately 900 members of Kingswood. If the merger were implemented, Kingswood would serve as the corporate entity of the merged clubs. It would acquire the golf courses of Peninsula, admit those members of Peninsula who wished to become members of the merged club and sell the golf course at Dingley Village.

William Falkingham was a member of Kingswood who opposed the merger. He had been a member of Kingswood for over 30 years and played golf at the Dingley Village course on almost a daily basis.

At a special general meeting held on 17 September 2013, the members of Kingswood voted in favour of the merger of Peninsula and Kingwood to become Peninsula Kingswood Golf Club Ltd (Peninsula Kingswood). 63% of Kingswood members voted in favour, 27% against and 10% abstained. At a separate meeting of Peninsula members, 98% of members voted in favour of the merger. On 2 October 2013, the board of Peninsula Kingswood admitted approximately 1,000 members of Peninsula as members of Peninsula Kingswood.

In March 2014, Ernst & Young were engaged by the board of Peninsula Kingswood to sell the golf course at Dingley Village. In the same month, Mr Falkingham engaged a solicitor with a view to commencing proceedings to challenge the merger and sale. His solicitor advised him that between $20,000 and $30,000 would be needed to fund proceedings. Mr Falkingham took part in a community campaign to raise these funds.

In early May 2014, Mr Falkingham was informed by Peninsula Kingswood that Ernst & Young had been engaged to conduct the sale. By this stage, $5,000 had been raised for contemplated proceedings. By 14 August 2014, there were four preferred bidders for the golf course. They were to present their final bids by 30 August 2014.

On 24 August 2014, Mr Falkingham commenced proceedings in the Supreme Court of Victoria claiming that the merger and proposed sale were oppressive of him as a member. Robson J heard the matter on 1 and 2 September 2014 and delivered judgment and *ex tempore* reasons on 3 September 2014. Mr Falkingham sought orders in equity and pursuant to s. 233 of the Corporations Act, including orders preventing the sale of the Dingley Village golf course and removing members of Peninsula from the register of Peninsula Kingswood.

(c) Decision

Robson J concluded that the board of Peninsula Kingswood breached its fiduciary duties as it had exercised its power under the constitution to admit members for an ulterior purpose. His Honour found that the substantial object of the board in admitting the members of Peninsula was to give effect to the merger, when the board had no power under the constitution to effect a merger that involved the admission of approximately 1,000 members from another club and selling the golf course at Dingley Village so that members were required to play in Frankston. His Honour's conclusion was not altered by the fact that a resolution of Kingswood members passed on 17 September 2013 had directed the board to effect the merger, including by admitting the Peninsula members. This was because the members, by ordinary resolution, did not have the power to amend the provisions of the constitution regarding the admission of members—a special resolution was required for a constitutional amendment. His Honour concluded that the actions of the board in depriving Mr Falkingham of the protection of a constitutional amendment to effect the merger was unfair because he lost the use of the golf course he had played at for decades. His Honour accordingly concluded that the Court's jurisdiction to grant a remedy under s. 233 and in equity had been enlivened.

Peninsula Kingswood opposed any remedy on the basis of laches, acquiescence and delay. Unchallenged evidence was given by a partner of Ernst & Young that the preferred bidders had spent between $100,000 and $200,000 on the sale process and that an injunction of the sale would adversely affect the sale price by $10–20 million. Robson J concluded that Mr Falkingham had not brought proceedings for some five months when he knew the sale process was under way and that Peninsula Kingswood and the bidders were incurring significant expenses. His Honour said that the delay could be explained by the time needed to gather funds for the proceeding, but "[n]o submission or authority was tendered ... that made this factor of great significance". His Honour stated that delay in itself was an insufficient reason for denying a remedy; instead, one must weigh the delay by Mr Falkingham against the potential damage to Peninsula Kingswood and third parties. Robson J concluded that the delay had "not been great" but would place third parties in an "inequitable and unreasonable" position

if the merger were set aside. These third parties were the bidders for the Dingley Village golf course, the members of Kingswood who had voted in favour of the merger and the members of Peninsula who had joined Peninsula Kingswood. Accordingly, his Honour exercised his discretion to refuse any remedy under s. 233 or in equity.