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Index

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Legislation Hotline

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1. Recent Corporate Law and Corporate Governance Developments

1.1 Hedge funds survey report

On 11 December 2015, the International Organisation of Securities Commissions published its Report on the Third IOSCO Hedge Fund Survey. The aim of the IOSCO survey is to gather data from hedge fund managers and advisers about the markets in which they operate, their trading activities, leverage, funding and counterparty information.

The report highlights the following observations:

- the Survey captured data from 1,486 qualifying funds, an increase of 42% from the 1,044 funds that participated in the September 2012 survey;
- hedge fund assets under management were US$2.6 trillion, up 34% from the last Survey. Most of this growth can be attributed to changes in asset values, net inflows and fund structures. Some of this growth also reflects more widespread and accurate reporting across participating jurisdictions;
- the hedge fund industry is largely concentrated in the US, while the Cayman Islands continue to be the tax domicile of choice;
- hedge funds remain mostly US dollar based and predominantly invested in North American assets;
- the use of equity-based strategies remains the most popular amongst hedge funds;
- financial leverage is used by hedge funds across all jurisdictions, except in Japan; comparisons of synthetic and gross leverage continue to be hampered by the different leverage metrics used by jurisdictions;
- reported data suggests there is no significant liquidity mismatch in hedge funds; however, this is against the backdrop of "normal" market conditions;

and

- hedge funds seem aware of the market liquidity of their portfolio positions, and they can generally make use of suspensions and gating to manage investor redemptions.

1.2 SEC proposes rules for resource extraction issuers under Dodd-Frank Act

On 11 December 2015, the US Securities and Exchange Commission made available a proposed rule that would require resource extraction issuers to disclose payments made to the US federal government or foreign governments for the commercial development of oil, natural gas or minerals. The proposed rules, mandated by the *Dodd-Frank Wall Street Reform and Consumer Protection Act* (the Dodd-Frank Act), are intended to further the statutory objective to advance US policy interests by promoting greater transparency about payments related to resource extraction.

Under the proposed rules, an issuer would be required to disclose payments made to the US federal government or a foreign government if the issuer is required to file annual reports with the Commission under the *Securities Exchange Act*. The issuer would also be required to disclose payments made by a subsidiary or entity controlled by the issuer.

The disclosure would be made at the project level similar to the approach adopted in the European Union and proposed in Canada. The disclosure required by the proposed rules would be filed publicly with the Commission annually on Form SD.

1.3 SEC proposes new derivatives rules for registered funds and business development companies

On 11 December 2015, the US Securities and Exchange Commission a proposed new rule designed to enhance the regulation of the use of derivatives by registered investment companies, including mutual funds, exchange-traded funds (ETFs) and closed-end funds, as well as business development companies. The proposed rule would limit funds' use of derivatives and require them to put risk management measures in place which would result in better investor protections.

The *Investment Company Act* limits the ability of funds to engage in transactions that involve potential future payment obligations, including derivatives such as forwards, futures, swaps and written options. The proposed rule would permit funds to enter into these derivatives transactions, provided that they comply with certain conditions.

Under the proposed rule, a fund would be required to comply with one of two alternative portfolio limitations designed to limit the amount of leverage the fund may obtain through derivatives and certain other transactions. A fund would also have to manage the risks associated with its derivatives transactions by segregating certain assets in an amount designed to enable the fund to meet its obligations, including under stressed conditions. A fund that engages in more than a limited amount of derivatives transactions or that uses complex derivatives

would be required to establish a formalized derivatives risk management program.

1.4 Company-investor engagement

On 9 December 2015, the US Council of Institutional Investors (CII) released two publications highlighting the most effective ways to conduct and disclose investor-company engagement. The first report, CII Investor-Company Roundtable: Effective Engagement is the result of a roundtable convened by CII to discuss the most effective engagement practices for both types of representatives. The second CII publication, Best Disclosure: Company-Shareholder Engagement highlights 10 companies' 2014 or 2015 proxy disclosures of their engagement practices. The companies were identified as having exemplary disclosure by CII members who responded to a survey. The research found that half of the companies provide detailed information about the processes they employ to facilitate engagement; three included instructions and/or email addresses for shareholders wishing to engage with the companies and several companies quantify their engagement activities. Other companies listed reforms they made to their governance practices as a result of feedback from discussions with shareholders.

1.5 Report on business set-ups, transfers and closures

On 7 December 2015, the Australian Productivity Commission released its Inquiry Report: Business Set-ups, Transfers and Closures. The report was completed in September 2015.

Key points from the report:

- Businesses are set-up for a variety of reasons and in any one year there is a churn of business entries and exits in Australia that is comparable with other countries. Most businesses start and remain small, and a very low proportion can be described as innovative.
- While it is relatively easy to start a business, a number of longstanding issues with specific regulatory requirements, regulator engagement and funding remain unaddressed. These make entry for some new businesses unnecessarily complex or costly.
- There is a growing focus among governments on high growth potential start-ups and the role entrepreneurial communities play in start-up success. The significance of entrepreneurial communities requires a more nuanced role for government. Any assistance programs must work within, and not distort, existing entrepreneurial communities to enable the capture of knowledge and network spillovers, beyond what would otherwise occur.
- Access to finance is not a significant barrier for most new businesses - most, with good reason, do not seek finance from external sources.
    - New financing platforms, such as peer-to-peer lending, are helping to fill a gap in unsecured debt finance available from the major financial institutions.
    - The planned new regulatory framework for crowd-sourced equity should balance the financing needs of business against the risk preferences of different types of investors.

    - High growth potential start-ups are generally able to attract angel and venture capital funding from Australian or overseas markets.
- Most businesses are closed or transferred without financial failure. Governments' role in such situations should be limited to provision of clear guidelines on regulatory requirements and arrangements, and ensuring government processes are timely.
- Some specific reforms to Australia's corporate insolvency regime are warranted, but a wholesale change to the system, such as the adoption of the United States' "chapter 11" framework, is neither justified nor likely to be beneficial.
    - Formal company restructuring through voluntary administration should only be available when a company is capable of being a viable business in the future.
    - A "safe harbour" defence should be introduced to allow directors of a solvent company to explore, within guidelines, restructuring options without liability for insolvent trading.
    - A simplified liquidation process should be introduced to reduce the time and expense of winding up businesses with few or no recoverable assets.
    - All directors should be required to obtain a director identification number.
- The default exclusion period and restrictions on bankrupts in relation to access to finance, employment and overseas travel should be reduced from 3 years to 1 year, with the trustee and courts able to extend this period to prevent abuse. The obligation to repay debts should continue to be required for 3 years or until bankruptcy discharge.

1.6 Automation in financial advice

On 4 December 2015, the Joint Committee of the three European Supervisory Authorities (ESAs) - EBA, EIOPA and ESMA - launched a Discussion Paper on automation in financial advice, aimed at assessing what, if any, action is required to harness the potential benefits of this innovation and mitigate its risks.

The ESAs have seen, with the increasing digitalisation of financial services, a growing number of financial institutions offering automated tools when providing advice or recommendations to consumers, often referred to as robo-advisors. These could potentially change the way consumers and financial institutions interact when buying or selling financial products.

The Discussion Paper explains the concept of automation in financial advice, where a financial institution provides advice or recommendations to consumers without, or with very little, human intervention and relies instead on computer-based algorithms and/or decision trees, and highlights potential benefits and risks associated with this particular innovation.

The potential benefits the ESAs have identified include lower costs, higher consistency of advice and a bigger number of customers that can be reached. The potential risks could include the inability of consumers to talk to a human advisor who can guide them through the process and provide clarifications, as well as the increased vulnerability to various types of IT failures.

1.7 Insolvency Law Reform Bill introduced

On 3 December 2015, the Australian Government introduced the Insolvency Law Reform Bill 2015 (Cth) into Parliament.

The Bill proposes to amend the Corporations Act 2001 (Cth), the Australian Securities and Investments Commission Act 2001 (Cth) and the Bankruptcy Act 1966 (Cth) to create common rules that would:

- remove unnecessary costs and increase efficiency in insolvency administrations;
- align the registration and disciplinary frameworks that apply to registered liquidators and registered trustees;
- align a range of specific rules relating to the handling of personal bankruptcies and corporate external administrations; and
- improve the powers available to the corporate regulator to regulate the corporate insolvency market and the ability for both regulators to communicate in relation to insolvency practitioners operating in both the personal and corporate insolvency markets.

1.8 Report on insolvency in the Australian construction industry

On 3 December 2015, the Senate Economics References committee published 'I just want to be paid', the report of its inquiry into insolvency in the Australian construction industry.

This report makes forty-four recommendations which, if adopted, the committee believes would overcome many of the challenges the construction industry faces in dealing with its unacceptably high rate of business insolvency. The recommendations seek to deal with the unacceptable culture of non-payment of subcontractors for work completed on construction projects.

Of these recommendations, two mark an important change in the Commonwealth's role in regulating payment practices in the construction industry.

- The first of these is the recommendation that the Commonwealth enact uniform, national legislation for a security of payment regime and rapid adjudication process in the commercial construction industry.
- The second, related major recommendation is that, commencing in July 2016, the Commonwealth commence a two year trial of Project Bank Accounts on construction projects where the Commonwealth's funding contribution exceeds ten million dollars.

The committee further recommends that, following the successful completion of a trial of Project Bank Accounts on Commonwealth funded projects, the Commonwealth legislate to extend the use of a best practice form of trust account to private sector construction.

The industry's rate of insolvencies is out of proportion to its share of national output. Over the past decade the industry has accounted for between 8% and 10% of annual GDP and roughly the same proportion of total employment. Over the same period, the construction industry has accounted for between one-fifth and

one-quarter of all insolvencies in Australia.

1.9 Draft legislation on raising professional standards of financial advisers

On 3 December 2015, the Commonwealth Treasury published exposure draft legislation for consultation on measures to raise education, training and ethical standards for financial advisers.

Under the proposed legislation:

- New financial advisers will require a degree, undertake a professional year and pass an exam.
- The Government will recognise an independent industry-established standard setting body, operational from 1 July 2016, that will develop and set education standards, professional year requirements, continuing professional development requirements and develop a comprehensive code of ethics for financial advisers.
- Existing advisers will be provided a transition process and will be required to complete an appropriate degree equivalent (or have a recognised transition pathway determined by the independent standard setting body) and pass an exam.
- All advisers both new and existing will be required to undertake continuing professional development and be party to a code of ethics.
- The new education and training requirement will be effective from 1 July 2017, with the code of ethics requirements proposed to commence on 1 July 2019.

View Exposure Draft: Corporations Amendment (Professional Standards of Financial Advisers) Bill 2015

View Exposure Draft Explanatory Material

The Financial Planning Association of Australia (FPA) has welcomed the government's move to enshrine higher educational and professional standards for financial planners in legislation, but has cautioned that some elements are "not workable".

FPA CEO Mark Rantall said the draft legislation was a good starting point and he looks forward to consulting further with the Government to improve the details.

Mr Rantall remarked:

> In particular, the FPA is concerned about the proposal to require planners to sign up to a code of ethics, without having to do so as part of a professional body. This would create an inherent unworkable conflict for planners as they would be required to follow the code at the same time as sanctioning themselves for any breaches. This change would also not improve on the model we have today. The FPA has data that proves financial planners who are not subject to a professional framework through membership of a professional body are 90 times more likely to be involved in ASIC banning and enforcement action.

Mr Rantall said the FPA was also concerned about the proposed transition period for existing financial planners to meet higher educational standards.

View FPA media statement.

1.10 Corporations Amendment (Crowd-sourced Funding) Bill 2015

The Corporations Amendment (Crowd-sourced Funding) Bill 2015 (Cth) proposes to amend the Corporations Act 2001 (Cth) and the Australian Securities and Investments Commission Act 2001 (Cth). The Bill was introduced into the House of Representatives and received its second reading speech on 3 December 2015.

According to the explanatory memorandum, the objectives of the Bill are to:

- establish a regulatory framework to facilitate crowd-sourced funding (CSF) by small, unlisted public companies;
- provide new public companies that are eligible to crowd fund with temporary relief from the reporting and corporate governance requirements that would usually apply; and
- provide greater flexibility in the Australian market licence and clearing and settlement facility licensing regimes.

Specifically, Bill would establish a CSF regime which would include:

- eligibility requirements for a company to fundraise via CSF, including disclosure requirements for CSF offers;
- obligations of a CSF intermediary in facilitating CSF offers;
- the process for making CSF offers;
- rules relating to defective disclosure as part of a CSF offer; and
- investor protection provisions.

The Senate has referred provisions of the Bill to its Economics Legislation Committee for inquiry and report by 22 February 2016.

1.11 IFAC paper examines principles of good regulation

On 2 December 2015, the International Federation of Accountants (IFAC) launched a discussion paper on the evolving global regulatory environment and its role in improving growth, investment, and stability, From Crisis to Confidence: the Role of Good Regulation.

The paper focuses on the importance of globally consistent "good regulation" to underpin confidence in the global economy. It examines the impact, benefits, and costs of the current regulatory landscape, and compares internationally recognized principles of good regulation.

1.12 Reform of insurance disclosure

On 1 December 2015, the Insurance Council of Australia (ICA) published the report and recommendations of the ICA Effective Disclosure Taskforce on ways to better align the provision of policy information with customers' needs.

The Taskforce has made 16 recommendations including:

- Integrating insurance calculators into the sales process, especially for home insurance, and trying to achieve a common basis for them across the industry. This is designed to combat substantial levels of underinsurance in the community
- Exploring new forms of electronic disclosure that are more engaging and can better target the information most applicable to individual customers
- Encouraging government to create a central portal for the release of natural hazard data to help consumers determine their insurance needs and take steps to mitigate their level of risk

View Too Long; Didn't Read - Report of the Effective Disclosure Taskforce to the Insurance Council Board

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1.13 Assessment and review of financial market infrastructures

On 30 November 2015, the Committee on Payments and Market Infrastructures (CPMI) and the International Organization of Securities Commissions (IOSCO) released a report on the implementation of the Principles for financial market infrastructures (PFMI), the Assessment and review of application of Responsibilities for authorities. The PFMI are international standards for payment, clearing and settlement systems, and trade repositories. They are designed to ensure that the infrastructure supporting global financial markets is robust and well placed to withstand financial shocks.

This report presents the findings of the CPMI-IOSCO assessment of the completeness and consistency of frameworks and outcomes arising from jurisdictions' implementation of the Responsibilities for authorities in the PFMI. The assessments covered implementation of the Responsibilities across all financial market infrastructure (FMI) types in 28 participating jurisdictions.

Overall, the assessment revealed that a majority of the jurisdictions had achieved a high level of observance of the Responsibilities. Of the 28 jurisdictions assessed, 16 fully observed the five Responsibilities for all FMI types; an additional two jurisdictions either fully or broadly observed each of the five Responsibilities for all FMI types.

With respect to specific FMI types, jurisdictions most frequently fell short of a fully observed rating in the case of trade repositories (TRs). Five of the participating jurisdictions had TR regimes that were still in development and were therefore determined to be "not ready for assessment". In addition, several other jurisdictions lacked clear criteria and/or fully disclosed policies to support their regulation, supervision and oversight of TRs.

1.14 Global director network issues policy perspectives on cybersecurity and board renewal

On 27 November 2015, the Global Network of Director Institutes (GNDI), the international network of director institutes, issued papers on two governance issues that have dominated the board agenda globally this year.

In the first paper, Guiding Principles for Cybersecurity Oversight, GNDI proposes three areas of focus: people, processes and technology. Likening cybersecurity to the "fourth estate", the global network says that cybersecurity falls outside the traditional borders of oversight, accountability and control, and therefore requires a new approach.

The organisation is calling on boards to consider placing cybersecurity as a specific accountability of one of the officers reporting to the board, to inform themselves of specific operational, reporting and compliance aspects of cybersecurity, and lastly to consider adding a member with some knowledge of information technology (including digitalization and cybersecurity).

In the second perspectives paper, Renewing the Board, GNDI advocates for a performance management approach to board renewal to create long-term value and argues that the board should disclose these policies and processes to its shareholders and other stakeholders to allow for better engagement with these groups. The paper also argues that boards should cast a wide net when adding or replacing a director and should consider the need for diversity of thought, skills and experience on the board when considering appointments.

The paper further highlights that while term limits can act as a backstop against excessive tenure length, they should not be the only renewal mechanism used by boards as they can have the effect of substituting for difficult conversations with underperforming directors or can lead to the replacement of effective directors.

1.15 Governance and climate change

On 27 November 2015, the International Corporate Governance Network (ICGN) published a Viewpoint on Climate Change: Governance implications for companies and investors.

The ICGN takes the view that climate change is a corporate governance issue as well as a matter of social, economic, trade and public policy. In a governance context, this calls for diligent oversight by company boards as well as for investor awareness of what companies need to do to position themselves sustainably in a dynamic climate policy environment. To this effect, companies need to disclose the material business issues related to climate change.

ICGN believes that integrated reporting with its focus on sustainable value creation offers a good framework for how companies can disclose their strategic approach to addressing the risks and opportunities related to climate change (including public policy) to their investors and other stakeholders. Beyond disclosure, companies will need to enter into dialogue with investors and other relevant stakeholders.

1.16 CEO turnover - study

On 26 November 2015, PricewaterhouseCoopers (PwC) published findings from a study on CEO turnover in 2014.

Thirty-five of the ASX 200 companies saw a turnover in Chief Executive Officer (CEO) in 2014, almost 35% more than the global average, including 8 unplanned succession events which cost $8 billion in foregone shareholder value. The $8 billion in lost shareholder value is comprised of a loss leading up to an unplanned CEO turnover (-5.5%), as well as the year after the change (-11.4 percent). This is between two to three times the erosion in shareholder value compared to top global firms.

The number of incoming female CEOs in Australia also remains low despite tripling since 2013 - from one to three. However, the female Australian CEO representation at 8.3 percent still beats the low global average of 5.2% of incoming hires.

Other key findings from the study of the 2,500 largest public companies in the world include:

- ASX200 CEO tenure has increased to 5 years
- Leading Australian companies were subject to approximately 35 percent more CEO turnover events than global leading enterprises
- The incoming class of CEOs in top Australian companies was amongst the youngest globally, with a median age of 51. Globally it is 52
- 19% of incoming CEOs in Australia came from another region making Australia's newest CEOs significantly more diverse than the global average of 11 percent.

View Executive Summary for Australia

View full report PwC 15th Annual CEO Succession Study

1.17 APRA proposes revisions to prudential framework for securitisation

On 26 November 2015, the Australian Prudential Regulation Authority (APRA) released for consultation a Discussion Paper: Revisions to the prudential framework for securitisation for authorised deposit-taking institutions (ADIs). APRA has also made available Draft Prudential Standard APS 120 Securitisation (APS 120).

APRA's objective in revising the prudential requirements for securitisation is to establish a simplified framework, taking into account global reform initiatives and the lessons learned from the global financial crisis. One of these lessons was that securitisation structures had become excessively complex and opaque, and that prudential regulation of securitisation had become similarly complex.

APRA first consulted on initiatives to simplify its prudential framework for securitisation in April 2014. Following consideration of the issues raised in submissions, APRA has amended its proposals in some areas. APRA's amended proposals include:

- dispensing with a credit risk retention or "skin-in-the-game" requirement;

allowing for more flexibility in funding-only securitisation; and
- removing explicit references to warehouse arrangements in the prudential framework.

These amended proposals are expected to assist ADIs to further strengthen their funding profile and provide clarity for ADIs that undertake securitisation for capital benefits.

In December 2014, the Basel Committee on Banking Supervision (the Basel Committee) released its updated securitisation framework (the Basel III Securitisation Framework). The changes aim to enhance the Basel Committee's existing securitisation framework and to strengthen regulatory capital standards.

APRA's latest proposals incorporate the new Basel III Securitisation Framework, with appropriate adjustments to reflect the Australian context and APRA's objectives, and will be applicable equally to all ADIs. Subject to consultation on this discussion paper and draft prudential standard, APRA proposes to implement these changes in line with the Basel Committee's effective date of 1 January 2018.

1.18 Guidance on cyber resilience for financial market infrastructures

On 24 November 2015, the Committee on Payments and Market Infrastructures (CPMI) and the Board of the International Organization of Securities Commissions (IOSCO) released the consultative paper Guidance on cyber resilience for financial market infrastructures (the Cyber Guidance).

Financial market infrastructures (FMIs) play a critical role in promoting the stability of the financial system. Thus, the cyber risks faced by FMIs and their level of readiness to effectively deal with worst case scenarios have been considered top priorities by industry leaders and authorities alike. The Cyber Guidance aims to add momentum to and instil international consistency in the industry's ongoing efforts to enhance FMIs' ability to pre-empt cyber-attacks, respond rapidly and effectively to them, and achieve faster and safer target recovery objectives if they succeed.

The proposed Cyber Guidance sets out the preparations and measures that FMIs should undertake to enhance their cyber resilience capabilities with the aim of limiting the escalating risks that cyber threats pose to individual FMIs and thereby to financial stability. It also provides authorities with a set of internationally agreed guidelines to support consistent and effective oversight and supervision of FMIs in the area of cyber risk. The Cyber Guidance is primarily intended to create meaningful shifts in the FMI industry towards greater cyber resilience.

1.19 Report on digital currencies

On 23 November 2015, the Committee on Payments and Market Infrastructures (CPMI) released its report on Digital Currencies.

Innovations in the payments domain can have important implications for the safety and efficiency of the financial system and thus are monitored by many central banks. The emergence of digital currencies was noted in previous reports by the

CPMI on Innovations in retail payments (2012) and Non-banks in retail payments (2014).

There are two key features of digital currencies.

- The first is the assets themselves (such as bitcoins). These assets can have some of the characteristics of a commodity and some of a currency. Currently, their monetary features (such as their use as a means of payment) are often more prominent, yet, these assets are not typically issued in or connected to a sovereign currency, are not a liability of any entity, are not backed by any authority and have no intrinsic value.
- The second feature is the technology used. Particularly noteworthy is the use of distributed ledgers. Most financial transactions are made via a centralised infrastructure, where a trusted entity clears and settles transactions. Distributed ledgers are innovative because they allow transactions in the absence of trust between the parties and without the need for intermediaries.

The development of digital currencies using distributed ledger technology is an innovation with potentially broad applications. In the financial market infrastructures (FMIs) sector, wider use of distributed ledgers by new entrants or incumbents could have implications extending beyond payments, including their possible adoption by some FMIs and more broadly by other networks in the financial system.

1.20 ISS releases 2016 benchmark policy updates

On 20 November 2015, Institutional Shareholder Services Inc (ISS), a provider of corporate governance solutions to the global financial community, released 2016 updates to its benchmark proxy voting policies for the Americas, EMEA, and Asia-Pacific regions. The updated policies will generally be applied for shareholder meetings on or after 1 February 2016.

The changes include those for the following:

United States

Key US benchmark policy changes announced include that ISS is changing its director overboarding policy. For most directors except for standing CEOs, the maximum number of public company boards that a director can sit on before being considered "overboarded" is being reduced from six to five.

Europe

For the UK and Ireland, ISS's benchmark policy is being updated for share issuance authorities to clarify that a disapplication of pre-emption rights up to 10% of the issued share capital will be acceptable, provided that the extra 5% above the original 5 percent is to be used only for the purposes of an acquisition or a specified capital investment. The policy for the UK and Ireland is also changing with regard to overboarding to make explicit reference to a recommended maximum number of boards on which directors should sit, and that ISS may recommend against directors considered overboarded.

The policy changes also clarify how ISS assesses director attendance at board and

committee meetings. While ISS's policy does not state a hard-and-fast threshold for this market on the maximum number of directorships that are considered acceptable, the issue of time commitment is considered especially relevant to the role of board chair, particularly where a company is both complex and global in scale and furthermore if it operates within a highly regulated sector such as financial services. A director's board and committee attendance will also be considered when a director holding multiple board positions stands for election or re-election.

Asia-Pacific

For Asia-Pacific, ISS's benchmark policy changes for 2016 include the adoption of a new policy on director elections in Japan under which ISS will recommend against top executives of companies if the board, after the shareholders meeting, does not include at least two outsiders.

For additional details on these and other ISS 2016 benchmark policy updates, view the ISS Policy Gateway.

1.21 Publication of review into the failure of HBOS

On 19 November 2015, the UK Prudential Regulation Authority (PRA) and the UK Financial Conduct Authority (FCA) published their review into the failure of HBOS Group.

This review was originally started by the former regulator, the Financial Services Authority (FSA). Its purpose is to analyse the causes of the firm's failure, and to draw out lessons for the future, for both the industry and the regulatory system as a whole.

On 1 October 2008 HBOS was approaching a point at which it was no longer able to meet its liabilities as they fell due and so sought Emergency Liquidity Assistance from the Bank of England. This report seeks to explain why HBOS failed, the role that HBOS Board and senior management played in the failure and the FSA's supervision of HBOS.

The review concludes that ultimate responsibility for the failure of HBOS rests with the Board and senior management. They failed to set an appropriate strategy for the firm's business and failed to challenge a flawed business model which placed inappropriate reliance on continuous growth without due regard to risks involved. In addition, flaws in the FSA's supervisory approach meant it did not appreciate the full extent of the risks HBOS was running and was not in a position to intervene before it was too late.

View The failure of HBOS plc (HBOS): A report by the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA)

1.22 SEC proposes rules to enhance transparency and oversight of alternative trading systems

On 18 November 2015, the US Securities and Exchange Commission proposed

rules to enhance operational transparency and regulatory oversight of alternative trading systems (ATSs) that trade stocks listed on a national securities exchange (NMS stocks), including "dark pools."

The proposal would require an NMS stock ATS to file detailed disclosures on newly proposed Form ATS-N about its operations and the activities of its broker-dealer operator and its affiliates. These disclosures would include information regarding trading by the broker-dealer operator and its affiliates on the ATS, the types of orders and market data used on the ATS, and the ATS's execution and priority procedures.

In addition, the proposal would make Form ATS-N disclosures publicly available on the Commission's website, which could allow market participants to better evaluate whether to do business with an ATS, as well as to be better informed when evaluating order handling decisions made by their broker.

View SEC Fact Sheet: Regulation of Alternative Trading Systems

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1.23 Standards and processes for global securities financing data collection and aggregation

On 18 November 2015, the Financial Stability Board (FSB) published its report Standards and Processes for Global Securities Financing Data Collection and Aggregation.

Securities financing transactions such as securities lending and repurchase agreements (repos) play a crucial role in supporting price discovery and secondary market liquidity for a wide variety of securities. However, such transactions can also be used to take on leverage as well as maturity and liquidity mismatched exposures.

Enhanced data collection on securities financing markets is needed for authorities to obtain a more timely and comprehensive perspective on developments in these markets and detect financial stability risks. This data will be useful for the implementation of the FSB's Regulatory framework for haircuts on non-centrally cleared securities financing transactions. The data will also serve the needs of a wide range of market participants and the economy, increasing the transparency of these markets.

The finalised standards and processes define the data elements for repos, securities lending and margin lending that national/regional authorities will be asked to report as aggregates to the FSB for financial stability purposes. The standards and processes describe data architecture issues related to the data collection and transmission from the reporting entity to the national/regional authority and then from the national/regional to the global level.

1.24 Foreign investment into through managed investment trusts

The 2015 Australian Investment Managers Cross-Border Flows Report by the Financial Services Council (FSC) and Perpetual has revealed foreign investment into Australia through managed investment trusts (MITs) has more than doubled

from $20.3 billion at 1 January 2010 to an estimated $43.6 billion at 31 December 2014. Financial services exports have remained steady at 3.6% during the same five-year period.

View 2015 Australian Investment Managers Cross-Border Flows Report

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1.25 Finalising post-crisis reforms and Basel III implementation - Basel Committee reports to G20 Leaders

On 13 November 2015, the Basel Committee on Banking Supervision published two reports for the G20 Leaders at their Summit in Antalya on 15-16 November 2015.

The first report on Finalising post-crisis reforms: an update reviews the Basel Committee's work since the global financial crisis to strengthen the international regulatory framework for banks. The report also focuses on the Committee's substantial progress towards finalising its post-crisis reforms, which includes reducing excessive variability in risk-weighted assets.

The second report is an update on Implementation of Basel III standards: Progress report to the G20 Leaders. It notes that implementation has generally been both timely and consistent with the globally agreed standards. All Committee member jurisdictions have implemented the Basel III risk-based capital regulations. Final rules on the Liquidity Coverage Ratio are in force in almost all member jurisdictions. Efforts are continuing to adopt the Basel III standards for the leverage ratio and the Net Stable Funding Ratio as well as for systemically important banks.

1.26 Reports on shadow banking

On 12 November 2015, the Financial Services Board (FSB) published:

- Progress report on Transforming Shadow Banking into Resilient Market-based Finance: This report sets out actions taken to implement the FSB's two-pronged strategy to address financial stability concerns associated with shadow banking over the past year, and next steps.
- Global Shadow Banking Monitoring Report 2015: This report presents the results of the FSB's fifth annual monitoring exercise to assess global trends and risks of the shadow banking system, reflecting data as of end-2014. It covers 26 jurisdictions and the euro area, representing about 80% of global GDP and 90% of global financial system assets.
- Regulatory framework for haircuts on non-centrally cleared securities financing transactions: This report finalises policy recommendations in the framework for haircuts on certain non-centrally cleared securities financing transactions published in October 2014 to apply numerical haircut floors to non-bank-to-non-bank transactions and update the implementation dates of these recommendations. The framework aims to address financial stability risks in securities financing transactions.

The Financial Stability Board measure of shadow banking was US$36 trillion in 2014, increasing by US$1.1 trillion compared to 2013. This is equivalent to about

30% of the overall non-bank financial sector assets and 60% of the GDP of the 26 participating jurisdictions.

1.27 Institutional investor global stewardship code

The International Corporate Governance Network (ICGN) has published for consultation the ICGN Global Stewardship Code.

According to the ICGN, the purposes served by the Code include:

- Serving as an international "passport" for institutional investors seeking to signal their stewardship policies and practices either when investing in markets without stewardship codes or when they invest in multiple markets with differing stewardship codes.
- Serving as a point of reference for investors on what stewardship entails and how to implement it in practical terms.
- Serving as a point of reference to guide jurisdictions seeking to establish their own stewardship codes by providing an overarching model of stewardship that can be adapted to the individual situations of countries or regions.

1.28 Latest Centre for Corporate Law and Securities Regulation research papers

The following are the latest research papers published by members of Melbourne Law School's Centre for Corporate Law and Securities Regulation:

a. Financial Hardship: Insights from a Survey of Financial Counsellors (by Paul Ali, Evgenia Bourova and Ian Ramsay)
b. Quantifying Phoenix Activity: Incidence, Cost, Enforcement (by Helen Anderson, Ann O'Connell, Ian Ramsay, Michelle Welsh and Hannah Withers)
c. 'Short a Few Quid': Bankruptcy Stigma in Contemporary Australia (By Paul Ali, Lucinda O'Brien and Ian Ramsay)

2. Recent ASIC Developments

2.1 Audit inspection findings for 2014-15

On 15 December 2015, ASIC released the results of its audit firm risk-based inspections for the 18 months to 30 June 2015: Report 461 Audit inspection program report for 2014-15 (REP 461).

ASIC reviewed a total 463 key audit areas across 111 audit files at firms of different sizes. ASIC found that, in its view, in 19% of audit areas, auditors did not obtain reasonable assurance the financial report as a whole was free of material misstatement. This compares with 20% for ASIC's report covering the previous 18 months ending in December 2013. The findings are similar to those

of audit oversight regulators in other countries.

ASIC inspections suggest audit firms must continue to improve in the following three areas:

- the sufficiency and appropriateness of audit evidence obtained by the auditor
- the level of auditors' professional scepticism, and
- appropriate use of the work of experts and other auditors.

Many of ASIC's findings related to accounting estimates (including impairment of assets) and accounting policy choices.

2.2 Consultation on implementation of retail life insurance advice reforms

On 15 December 2015, ASIC released a consultation paper seeking feedback on proposals to implement reforms to the regulation of the life insurance industry: Consultation Paper 245 Retail life insurance advice reforms (CP 245).

On 3 December 2015, the Government released draft legislative amendments and explanatory material containing proposed amendments to the Corporations Act 2001 (Cth) (the Corporations Act) to remove the exemption from the conflicted remuneration provisions for life insurance advice, and to allow benefits to be paid to advisers if requirements imposed by ASIC are met.

The draft legislative amendments give ASIC power to make a legislative instrument to set out:

- a maximum level of upfront and ongoing commission payments permitted in relation to life insurance products, and
- the amount of upfront commissions to be repaid to life insurers (clawback).

The consultation paper seeks feedback on the policy ASIC proposes to give effect to in the instrument.

ASIC is also seeking feedback on the type of information that life insurers should report to it to enable ASIC to monitor the effect of the reforms and assist in understanding developments in the life insurance sector.

2.3 ASIC remakes instruments on takeovers and schemes of arrangement

On 15 December 2015, following public consultation, ASIC announced that it had remade six legislative instruments that facilitate takeovers and schemes of arrangements.

The relief applies to certain domestic and foreign takeover bids, accelerated rights issues, investor directed portfolio services (IDPS), share buy-backs and downstream acquisitions and is set out in the following new legislative instruments:

- ASIC Corporations (IDPS - Relevant Interests) Instrument 2015/1067

- ASIC Corporations (Minimum Bid Price) Instrument 2015/1068
- ASIC Corporations (Takeovers - Accelerated Rights Issues) Instrument 2015/1069
- ASIC Corporations (Unsolicited Offers - Foreign Bids) Instrument 2015/1070
- ASIC Corporations (Approved Foreign Financial Markets) Instrument 2015/1071.

ASIC remade these instruments without significant changes before they were due to sunset under the Legislative Instruments Act 2003 (Cth).

IDPS - Relevant interests in securities

ASIC has made the ASIC Corporations (IDPS - Relevant Interests) Instrument 2015/1067, which affords operators of an IDPS similar relief to that provided to bare trustees in s. 609(2) of the Corporations Act 2001 (Cth) (the Corporations Act) with respect to the acquisition of relevant interests in securities.

Minimum bid price

ASIC has made ASIC Corporations (Minimum Bid Price) Instrument 2015/1068, which addresses certain technical and practical difficulties that arise in the takeovers process where the value of quoted securities offered under the bid decreases between the day the bidder lodged its statement with ASIC and the first day of the offer.

Takeovers - Accelerated rights issues

ASIC Corporations (Takeovers - Accelerated Rights Issues) Instrument 2015/1069 creates an exception for persons who will, for technical reasons, temporarily exceed the takeover threshold in s. 606 of the Corporations Act merely as a result of participating in an accelerated rights issue.

Foreign bids and approved foreign financial markets

Foreign takeover bids regulated in certain jurisdictions are likely to be accompanied by adequate disclosure because these jurisdictions have takeover regimes that offer comparable levels of disclosure and investor protection to that provided in Australia. As such, these regulated foreign takeover bids should not be subject to the disclosure provisions in Division 5A of Part 7.9 of the Corporations Act.

ASIC has made the ASIC Corporations (Unsolicited Offers - Foreign bids) Instrument 2015/1070 to facilitate such foreign takeover bids by providing relief from the disclosure provisions in Division 5A of Part 7.9 of the Corporations Act.

ASIC has also made ASIC Corporations (Approved Foreign Financial Markets) Instrument 2015/1071 which creates a uniform list of approved overseas financial markets for the purposes of s. 257B(7) (on-market buy backs) and item 14 of s. 611 (downstream acquisitions through a listed foreign company).

2.4 Implementation of clearing regime in Australia for OTC derivatives

On 14 December 2015, ASIC released rules implementing Australia's mandatory

central clearing regime for over-the-counter (OTC) derivatives of financial institutions - the ASIC Derivative Transaction Rules (Clearing) 2015 (derivative transaction rules (clearing)) and explanatory statement.

The mandatory central clearing regime will assist to reduce systemic risk in OTC derivatives markets and applies to transactions in OTC interest rate derivatives denominated in Australian dollars (AUD interest rate derivatives), and in US dollars, euros, British pounds and Japanese yen (G4 interest rate derivatives) between OTC derivatives dealers.

In line with overseas mandatory clearing requirements, the regime also provides the basis for substituted compliance or sufficient equivalence determinations by foreign regulators. This will help to achieve substantial cost savings for Australian participants and facilitate access to global markets by Australian participants and infrastructures.

The final derivative transaction rules (clearing) follow ASIC's consultation earlier this year. In May 2015, ASIC released Consultation Paper 231 - Mandatory central clearing of OTC interest rate derivative transactions (CP 231) and the proposed draft derivative transaction rules (clearing).

The final derivative transaction rules (clearing) follow a Ministerial determination issued in August 2015 that imposed a clearing mandate on AUD and G4 interest rate derivatives, and regulations made in September 2015 that set high-level parameters for the mandatory clearing regime.

The derivative transaction rules (clearing) set out which entities and derivative contracts are covered by the clearing mandate, the eligible central counterparties that may be used, alternative clearing (allowing entities to comply with certain overseas clearing requirements) and certain exemptions from the clearing mandate. The clearing obligations will commence in April 2016.

This marks Australia's implementation of the second Group of 20 (G20) mandate in relation to OTC derivatives reform. The phased implementation of the first mandate on trade reporting of OTC derivatives began in Australia in July 2013, and was completed with the commencement of reporting obligations for Phase 3B firms on 4 December 2015.

To find out more see:

- ASIC Derivative Transaction Rules (Clearing) 2015
- Report 460 Response to submissions on CP 231 Mandatory central clearing of OTC interest rate derivative transactions
- Regulation Impact Statement
- the OTC derivatives reform section of the ASIC website

2.5 Findings from 30 June 2015 financial reports

On 14 December 2015, ASIC announced the results from a review of the 30 June 2015 financial reports of 240 listed and other public interest entities.

Following the review, ASIC has made enquiries of 35 entities on 48 matters seeking explanations of accounting treatments. The largest number of findings

continue to relate to impairment of non-financial assets and inappropriate accounting treatments.

More information about the findings from ASIC's recent reviews of the financial reports of listed entities and of unlisted entities with larger numbers of users is available on the ASIC website.

2.6 ASIC finds professional indemnity insurance for financial advisers stable and available but gaps exist

On 14 December 2015, ASIC published the results of research in which it found the market for professional indemnity (PI) insurance in Australia for financial advisers is stable and generally available, but gaps exist between what ASIC expects and some of the insurance products available.

All Australian financial services (AFS) licensees must have arrangements to compensate clients and generally this means holding adequate PI insurance. ASIC's minimum requirements for PI insurance are set out in Regulatory Guide 126 - Compensation and insurance arrangements for AFS licensees (RG 126).

While the market was basically sound, the ASIC review found some PI insurance policies do not meet the requirements in RG 126.

The review was carried out in response to AFS licensee concerns about securing PI insurance and the high level of unpaid external dispute resolution scheme determinations.

View Report 459 Professional indemnity insurance market for AFS licensees providing financial product advice (REP 459)

2.7 Consultation on remaking of "sunsetting" class orders for dealing in underlying investments

On 4 December 2015, ASIC released a consultation paper proposing to remake three class orders which cover relief for dealing in underlying investments that are due to sunset (expire) in April 2017.

ASIC is proposing to remake the following class orders:

- Class Order [CO 02/1161] Licensing relief (dealing) for public offer superannuation entities, which is due to sunset on 1 April 2017
- Class Order [CO 02/1073] Financial Services Guide: Dealing in underlying investments by responsible entities, which is due to sunset on 1 April 2017, and
- Class Order [CO 02/1074] Financial Services Guide: Dealing in underlying investments by superannuation trustees, which is due to sunset on 1 April 2017.

ASIC has reviewed these class orders and considers that they are operating effectively and efficiently, and continue to form a necessary and useful part of the legislative framework. The fundamental policy principles that underpin the three

class orders have not changed. ASIC proposes to remake these class orders without significant changes before they sunset, so that their ongoing effect will be preserved without any disruption to the entities who rely on them.

View Consultation Paper 244: Remaking ASIC class orders on dealing in underlying investments (CP 244)

2.8 ASIC remakes "sunsetting" class orders on real estate companies

On 25 November 2015, ASIC remade two class orders that were due to sunset (expire) in 2016.

Class Order [CO 00/213] Real estate companies and Class Order [CO 05/1243] Licensing relief for valuations of real estate companies have been remade and consolidated into ASIC Corporations (Real Estate Companies) Instrument 2015/1049.

ASIC Corporations (Real Estate Companies) Instrument 2015/1049 provides relief for vendors, licensed real estate agents and valuers from the licensing and disclosure requirements of the Corporations Act 2001 (Cth) with respect to real estate companies,

ASIC remade and consolidated the previous class orders without significant change before they sunset in 2016. The new instrument will continue the substantive effects of [CO 00/213] and [CO 05/1243] with some minor amendments. These minor amendments include:

- clarifying that the disclosure relief applies to general advice and dealing and the licensing relief applies to general advice only; and
- combining the relief provided under [CO 00/213] and [CO 05/1243] into one instrument, giving relief from s707 and 911A(1) and covering vendors, real estate agents and valuers of real estate companies.

2.9 Updated guidance for fee and cost disclosure requirements for superannuation and managed investment products

On 19 November 2015, ASIC released updated guidance on fee and cost disclosure for trustees of superannuation funds and responsible entities of managed funds and other managed investment schemes.

Regulatory Guide 97 Disclosing fees and costs in PDSs and periodic statements has been updated and amendments made to Class Order [CO 14/1252] which made clarifications to the requirements for disclosing fees and costs in the Corporations Regulations 2001.

The revised guidance and law amendments follow ASIC'S review of fee and cost disclosure practices in Report 398 - Fee and cost disclosure: Superannuation and managed investment products (REP 398). In this report inconsistencies were identified in industry practice as well as under-disclosure of fees and costs.

These measures will assist trustees and responsible entities in ensuring that the

fees and costs disclosed to investors are accurate and that fees and costs are disclosed more consistently across the industry.

The amendments include an extension of the transition period for the application of the new requirements. The class order will now apply to all PDS for superannuation and managed investment products from 1 February 2017. It will also apply to periodic statements that must be given for these products by 1 January 2018 or later.

ASIC also intends to further defer the start date for the consistency requirements in s. 29QC of the Superannuation Industry (Supervision) Act 1993 (Cth) until 1 February 2017 to align with the extension to the fee and cost transition for PDSs.

View:

- ASIC Corporations (Amendment and Repeal) Instrument 2015/876
- Regulatory Guide 97 Disclosing fees and costs in PDSs and periodic statements (RG 97)
- Report 457 Response to Submissions Disclosing fees and costs in PDSs and periodic statements (REP 457)

2.10 Consultation on "sunsetting" class orders on lodgement of reports

On 19 November 2015, ASIC released a consultation paper, CP243: Remaking ASIC class orders on electronic lodgement of financial reports and dual lodgement relief, proposing to remake its class orders on dual lodgement and electronic lodgement of directors' reports, financial reports and auditor's reports (reports). The class orders are due to sunset (expire) in 2016 and 2017.

The class orders proposed to be remade are:

- Class Order [CO 00/2451] Electronic lodgement of certain reports with the ASX: approval
- Class Order [CO 06/6] Dual lodgement relief for NSX-listed disclosing entities
- Class Order [CO 98/104] Dual lodgement relief for ASX-listed entities.

ASIC proposes to remake these class orders as they are operating effectively and efficiently, and continue to form a necessary and useful part of the legislative framework. No significant changes are proposed.

It is proposed to remake the class orders as a single instrument. Disclosing entities listed on NSX will be able to satisfy their obligation to lodge their reports with ASIC if they are lodged electronically with NSX. In addition, it is proposed to extend the relief to entities listed on Asia Pacific Stock Exchange Ltd.

2.11 Report on corporate insolvencies 2014-15

On 17 November 2015, ASIC published its annual overview of corporate insolvencies based on statutory reports lodged by external administrators for the 2014-15 financial year. The report summarises information from 8,354 reports

that ASIC received from external administrators during the 2014-15 financial year and includes ASIC's response to their reports of alleged misconduct.

View Report 456 Insolvency statistics: External administrators' reports (July 2014 to June 2015) (REP 456)

REP 456 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
- estimated dividends to unsecured creditors.

Consistent with past reports, REP 456 shows small to medium size corporate insolvencies again dominated external administrators' reports. Of note, 85% had assets of $100,000 or less, 79% had less than 20 employees and 43% had liabilities of $250,000 (or less). 97% of creditors in this group received between 0-11 cents in the dollar, reflecting the asset/liability profile of small to medium size corporate insolvencies.

REP 456 details how often external administrators report alleged misconduct by company officers and the types of alleged misconduct most frequently reported. In the 2014-15 financial year, external administrators lodged 6,561 reports alleging misconduct.

3. Recent ASX Developments

3.1 TORESS LEPOs rule amendments and Go-Live details

Following regulatory approval, ASX launched its new TORESS (TOtal REturn Single Stock) LEPOs (Low Exercise Price Options) on Monday evening, 30 November 2015, ready for trading on Tuesday 1 December 2015.

TORESS options have two distinguishing features which differentiate them from standard options currently available to trade on ASX:

- Ordinary dividends will be adjusted for via a cash transfer between the option seller and buyer. This feature allows for the better pricing of these options due to the removal of forecast dividends in pricing.
- The options will be cash settled upon exercise as opposed to physical delivery. This feature will remove some issues which clearers have expressed around Cash Market Margining on the back of exercises.

The ASX Notice and Rule amendments are available here.

3.2 Introduction of ASX 3, 5 and 10 year deliverable interest rate swap futures

ASX launched 3, 5 and 10 Year Deliverable Swap futures contracts on Monday 30

November 2015 at 8:34am (Trade Date 30 November 2015). The first contract month available to trade will be the March 2016 expiry. The June 2016 contract was available from 15 December 2015 at 5:14pm (Night session).

The 3, 5 and 10 Year Deliverable Swap Futures contracts have received Australian regulatory clearance. ASX Deliverable Swap Futures will not be available for trading by US based customers.

The ASX Notice and Rule amendments are available here.

3.3 Introduction of client account enhancements for ASX Clear

With effect from 30 November 2015, the ASX Clear Operating rules were amended to:

- enable excess client cash collateral for ETOs (Exchange Traded Options) to be held directly with ASX; and
- clarify that cash cover and excess cash recorded for an ETO client account cannot be used by ASX towards satisfaction of obligations of the Clearing Participant in respect of another client's account. This amendment will resolve any existing ambiguity in relation to the segregation of client cash collateral.

The client account enhancements have been introduced to comply with the regulatory guidance of the Reserve Bank of Australia.

The ASX Notice and Rule and Procedure amendments are available here.

3.4 Amendments to ASX Clear Operating Rules Procedure 4.4.3 and ASX Clear (Futures) Operating Rules Procedure Rule 8

ASX is amending the ASX Clear and ASX Clear (Futures) Operating Rules Procedures to enable participants that are foreign ADIs (authorised deposit-taking institutions) to prepare their accounts in accordance with the accounting standards that apply in their home jurisdiction, instead of Australian accounting standards.

The ASX Notice and Rule and Procedure amendments are available here.

4. Recent Takeovers Panel Developments

4.1 Guidance Note 23 on shareholder intention statements

On 11 December 2015, the Takeovers Panel published Guidance Note 23 "Shareholder Intention Statements".

The Panel issued a consultation draft of the Guidance Note on 7 July 2015. It received eight submissions and has taken them into account and made further changes.

The new Guidance Note provides shareholders who make statements of their intentions with respect to a control transaction, particularly a takeover bid, with an indication of the issues that might arise. The Guidance Note supplements ASIC's "truth in takeovers" policy (ASIC RG 25 - Takeovers: false and misleading statements).

The Guidance Note and the Public Consultation Response Statement are available on the Panel's website

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4.2 Revised Guidance Note 14 - Funding arrangements

On 26 November 2015, the Takeovers Panel published a revised version of Guidance Note 14 - Funding arrangements.

On 6 October 2015, the Panel issued a consultation paper in relation to proposed changes to Guidance Note 14. The Panel received three submissions in response. All supported the proposed change to address the recent decision of the Federal Court in *ASIC v Mariner Corporation* and clarify the policy basis for the guidance note.

4.3 Resource Generation Ltd - Declaration of unacceptable circumstances, orders and review application

On 19 November 2015, the Panel made a declaration of unacceptable circumstances and final orders in relation to an application dated 12 October 2015 by Resource Generation Ltd in relation to its affairs.

Background

Resource Generation Ltd is a company listed on ASX (ASX code: RES) and JSE (JSE code: RSG). Resource Generation's substantial holders include Noble Group Ltd, through its subsidiary Noble Resources International Pte Ltd, holding 13.69% and Altius Investment Holdings (Pty) Ltd, through its subsidiary Shinto Torii Inc, holding 10.69%.

On 28 September 2015, Resource Generation received a letter from Altius containing a notice from Shinto requisitioning a general meeting pursuant to s. 249D, to remove and replace the current four directors on the Resource Generation board with six new directors.

Resource Generation applied to the Panel for a declaration of unacceptable circumstances and submitted, among other things, that certain shareholders, including Noble and Altius, are associates and have failed to disclose their association.

The Panel considered that, since 25 August 2015, Noble and Altius are associated under s. 12(2)(b) for the purpose of controlling or influencing the composition of the board of Resource Generation or s. 12(2)(c) in relation to the affairs of Resource Generation, in respect of controlling or influencing the composition of Resource Generation's board.

As a result of the association, the voting power of each of Noble and Altius in Resource Generation's shares aggregates to 24.38%.

The Panel considered that the failure of Noble and Altius to disclose their association resulted in RES shareholders being unaware ahead of the requisitioned meeting that Noble and Altius are associates.

The Panel did not consider that it had been provided with sufficient evidence of a voting agreement to make a finding that Noble and Altius had acquired a relevant interest in each other's Resource Generation shares that would result in a contravention of s. 606.

Declaration

The Panel considered that the circumstances were unacceptable:

a. having regard to the purposes of Chapter 6 set out in s. 602 or
b. because they constitute or give rise to a contravention of s. 671B.

Orders

The Panel has made orders that Noble and Altius each provide a notice of change of interest of substantial holder disclosing the existence and nature of their association. It also ordered that they disclose their association in any communication Noble or Altius has with RES shareholders or the media in respect of Shinto's requisitioned meeting.

The Panel's reasons for its decision are available on the Panel website.

Review application

On 24 November 2015, the Panel announced that it had declined to conduct proceedings on a review application dated 18 November 2015 from Resource Generation Ltd in relation to its affairs.

The applicant sought a review Panel to find that there was a voting agreement between Noble Group Ltd, Altius Investment Holdings (Pty) Ltd and Public Investment Corporation SOC Ltd, or in the alternative a voting agreement between Noble and Altius. It sought orders (among others) restricting voting based on the relevant finding.

The Panel considered that there was no reasonable likelihood that it would make any finding more favourable to the applicant than was made by the initial Panel and declined to conduct proceedings.

The review Panel's reasons for its decision are available on the Panel website.

5. Recent Research Papers

5.1 Anti-Primacy: Sharing power in American corporations

Prominent theories of corporate governance frequently adopt primacy as an organising theme. Shareholder primacy is the oldest and most used of this genre. Director primacy has grown dramatically, presenting in at least two distinct

versions. A variety of alternatives have followed - primacy for CEOs, employees, creditors. All of these theories can't be right. This article asserts that none of them are. The alternative developed here is one of shared power among the three actors named in corporations statutes with judges tasked to keep all players in the game. The debunking part of the article demonstrates how the suggested parties lack legal or economic characteristics necessary for primacy.

View Anti-Primacy: Sharing Power in American Corporations

5.2 Opportunistic proposals by union shareholders

Effective corporate governance requires mechanisms that allow shareholders to influence corporate decisions. This paper investigates the use of shareholder proposals, an increasingly prominent governance mechanism, by labour unions. Activist union pension funds are subject to cross-pressures: they wish to increase fund returns to help beneficiaries but also to aid current union workers. The authors show theoretically that shareholder proposals can be used as bargaining chips in contract negotiations. Empirically, the authors use variation in the expiration of collective bargaining agreements to identify exogenous changes in the value of making proposals.

The authors find that during contract negotiation years, unions increase the number of proposals they make by about one-quarter (and by about two-thirds during contentious negotiations), and change the subject of proposals to focus on matters personally costly to managers. They do not find similar changes in proposal behaviour by nonunion shareholders. Opportunistic union proposals are also associated with better wage agreements for the union. The evidence suggests that some union proposals are intended to influence collective bargaining outcomes rather than maximize shareholder value, and that increasing proposal rights will not necessarily help shareholders at large if some shareholders use those rights to advance their private interests.

View Opportunistic Proposals by Union Shareholders

5.3 Shareholder voting and corporate governance around the world

Using a sample of non-US firms from 43 countries, the authors investigate whether laws and regulations as well as votes cast by US institutional investors are consistent with an effective shareholder voting process. The authors find that laws and regulations allow for meaningful votes to be cast as shareholder voting is both mandatory and binding for important elections. For votes cast, the authors find there is greater dissent voting when investors fear expropriation. Further, greater dissent voting is associated with higher director turnover and more M&A withdrawals. The results suggest that shareholder voting is an effective mechanism for exercising governance around the world.

View Shareholder Voting and Corporate Governance Around the World

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5.4 The 'New' G20/OECD principles of corporate governance: More than meets the eye

This article reviews the new G20/OECD Principles of Corporate Governance, highlighting substantive discussions and notable changes including:

- Emphasis on a robust and well-functioning regulatory framework;
- Prominence given to proportionality of application;
- Expanded treatment of related party transactions;
- Analysis of intermediation in the investment chain, particularly the corporate governance roles of institutional investors and proxy advisors;
- Focus on the board's role in risk oversight; and
- Expanded definition of materiality.

View The 'New' G20/OECD Principles of Corporate Governance: More than Meets the Eye

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5.5 Hedge fund activism and long-term firm value

This paper investigates the association of hedge fund activism and long-term firm value. The authors show that the positive long-term association documented in prior studies is likely affected by selection bias, as activist hedge funds tend to target poorly performing firms. Second, once the authors incorporate such selection bias using a matched sample approach, they find that firms targeted by activist hedge funds improve less in value after activist hedge fund campaigns than ex-ante similarly poorly performing control firms that are not subject to hedge fund activism. This suggests that hedge fund activism decreases, rather than increases, a firm's long-term value, relative to non-targeted control firms that have similar characteristics as the targeted firms.

To explain their results, the authors explore whether the ability of activist hedge funds to substantially influence a firm's investment policy may exacerbate a firm's limited commitment problem toward long-term value creation and stable stakeholder relationships. Consistent with this hypothesis, they find that the reduction in value after hedge fund campaigns is more pronounced for firms where the limited commitment problem is more severe, namely firms that are more engaged in innovation and where stakeholder relationships are more important for long-term value creation.

View Hedge Fund Activism and Long-Term Firm Value

6. Recent Corporate Law Decisions

6.1 The trend continues: Liquidators disclaimer of leases extinguishes the leaseholders' interest in the land

(By Lauren Jayne Bracewell, Clayton Utz)

Re Williams Corporation Pty Ltd (in liq) [2015] QSC 324, Supreme Court of Queensland, McMurdo J, 24 November 2015

(a) Summary

The Supreme Court of Queensland confirmed that a liquidator of a landlord can disclaim a lease, and the leaseholder's interest in the land, without prior approval from the court. The court may grant approval retrospectively.

This decision follows the reasoning in *Willmott Growers Group Inc v Willmott Forests Ltd* (2013) CLR 592 (*Willmott Growers*) and gives liquidators certainty that where a contract is disclaimed the lessee's interest ceases. It also highlights leaseholders' tenuous right to enforce their interest in leasehold property where there is potential for the landlord to go into liquidation.

(b) Facts

Williams Corporation Pty Ltd (Williams Corporation) leased and subleased berths in its Port Hinchinbrook development marina. In 2011, Cyclone Yasi caused significant destruction to the marina. Due to a lack of funds, there was no prospect of rebuilding the marina berths. Williams Corporation did not elect to terminate the leases.

The applicants were appointed voluntary administrators of Williams Corporation and Hinchinbrook Reso Cruises Pty Ltd (HRC) (both companies ultimately owned by Keith Williams). When creditors resolved to place the companies into liquidation, the applicants were appointed liquidators.

A conditional contract was signed for the sale of all assets owned by Williams Corporation. The contract required that the property was free of any claim, right or interest over the marina berths. The same purchaser entered into a contract for the sale of the HRC assets, conditional upon the completion of the contract for Williams Corporation's assets.

Pursuant to s. 477 (2B) of the Corporations Act 2001 (Cth), a liquidator must obtain approval from the court, company creditors or inspection committee to enter into a contract on behalf of the company that exceeds three months. No such approval was obtained prior to entering into the conditional contracts.

The applicants sought retrospective approval of the conditional contracts and a direction that they would be justified in disclaiming leases granted by Williams Corporation. This direction was resisted by 21 of the leaseholders (the respondents). The respondents argued that leave to disclaim is required.

(c) Decision

McMurdo J applied the High Court's reasoning in *Willmott Growers*, namely, that a lease entered into by a company as lessor was a "contract" within the meaning of s. 568(1)(f) of the Corporations Act and could be disclaimed by the company under that section.

In reaching this decision, McMurdo J made the following findings:

- within the context of s. 511 (2) of the Corporations Act "just and beneficial" should be read in light of what will be advantageous in the liquidation;
- disclaiming the leases did not prejudice the leaseholders as their leases were effectively worthless. The structure of the marina no longer existed, and there was no prospect of rebuilding. Accordingly, there was no prospect of the enjoyment of the right to exclusive possession which was the subject of

the lease;
- a leaseholder's interest arises from the lease contract and is extinguished upon the landlord disclaiming the lease;
- the requirement for the court's leave pursuant to s. 568(1A) of the Corporations Act does not extend to situations where the subject of the disclaimer is an unprofitable contract or a lease of land; and
- in order to facilitate expeditious and beneficial administration of the winding up of companies, approval under s. 477(2B) of the Corporations Act may be granted retrospectively (nunc pro tunc).

A disclaimer may be set aside where the court is satisfied that the prejudice caused by the disclaimer would be grossly out of proportion to the prejudice that setting aside the disclaimer would cause the company's creditors. McMurdo J did not see it necessary to assess these prejudices in any detail, other than to note, based on the evidence, there was no apparent prospect of the disclaimer of the leases being set aside.

6.2 Unfair preference transactions: When transactions with a company that is being wound up are voidable

(By Ian Hedberg, Ashurt)

Rexel Electrical Supplies Pty Ltd v Morton (as liquidator of South East Queensland Machinery Manufacturing and Distribution (Mining No 1) (in liq) [2015] QCA 235, Supreme Court of Queensland, Court of Appeal, Fraser and Phillippides JJA and Ann Lyons J, 20 November 2015

(a) Summary

This decision concerns an application for leave to appeal a decision of the District Court that the applicant pay the respondent (the Liquidator) the sum of $132,811.01 representing transactions that the trial judge found to be voidable under s. 588FE of the Corporations Act 2001 (Cth) (the Act). The transactions were found to be voidable because they were "unfair preference" transactions made during a period when South East Queensland Machinery Manufacturing and Distribution, formerly known as Aran Management Pty Ltd (Management) was insolvent.

The applicant sought leave to appeal on eight grounds, including Management was solvent during the relevant period and that the transactions formed a "running account" and could be taken to be a single transaction, for the purposes of s. 588FA(3) of the Act, which was not an unfair preference transaction. The application for leave was refused and the applicant ordered to pay the respondent's costs.

(b) Facts

Rexel Electrical Supplies Pty Ltd, formerly Inaco Automation Controls (Inaco) supplied electrical components to Management for a fee. Between 26 March 2012 and 6 June 2012, Management made payments of $193,469.16 to Inaco.

On 14 August 2012 (the Relation Back Date), the Liquidator commenced the winding up of Management. The Liquidator brought a claim against Inaco

alleging that the transactions entered into were "insolvent transactions of the company" for the purposes of s. 588FE of the Act and were voidable.

Section 588FC of the Act defines "insolvent transactions of a company" as transactions involving "an unfair preference given by the company" if the transaction is entered into when the company is insolvent. A transaction between a company and an unsecured creditor is an unfair preference if it results in the creditor receiving more than the creditor would receive if the transaction were set aside and the creditor sought to prove their debt in a winding up of the company.

Under the Act, those transactions will be voidable if:

- they were entered into within six months of the Relation Back Day, being the period between 14 February 2012 and 14 August 2012; and
- the company was insolvent during that period.

Section 588E of the Act creates a presumption that, where a company is being wound up and is proven to have been insolvent at any point within the preceding twelve months from the Relation Back Day, it was insolvent throughout that twelve month period.

The trial judge found for Management on the basis that Management was insolvent during the relevant period and accordingly the transactions were voidable, but allowed for a setoff of $64,658.15 in favour of Inaco. The Liquidator was entitled to recover $132,811.01 from Inaco.

Inaco sought leave to appeal on the grounds that the trial judge erred in:

a. admitting into evidence all of the annexures to the Exhibit 3 in circumstances where the Liquidator, in his submissions, conceded that certain annexures to his report were not admissible;
b. finding that the determination of the Liquidator that Management was insolvent was well founded on the evidence before the Liquidator, rather than the evidence before the Court;
c. not considering the matters raised by Inaco in its submissions about insolvency;
d. finding that Management was insolvent when it was an entity that incurred debt and paid creditors and was provided with funds for that purpose by a related entity as and when required;
e. finding that the matters in the Liquidator's report were of sufficient probative force to justify the conclusion that Management was insolvent;
f. finding insolvency but failing to take into account any of the matters contained in Ivaco's submissions (This was dealt with together with ground (c) above);
g. his findings of fact; and
h. failing to address or consider the substance of the matters raised by the appellant in its submissions.

Fraser JA found that there were two relevant issues to be decided:

- whether the trial judge erred in finding that Management was insolvent at the time of the payments on the evidence; and
- whether the trial judge erred in finding that the transactions did not form a running account for the purposes of s. 558FA(3) of the Act.

(c) Decision

Fraser JA, with whom both Phillippides JA and Ann Lyons J agreed, considered each of the grounds identified above, in reaching the conclusion that leave to appeal should be refused because the trial judge did not err in finding that Management was insolvent and did not err in finding that the transactions formed a running account.

(i) Appeal ground (a)

Fraser J found that the Liquidator did not concede that the annexures were inadmissible and that Inaco did not press its objection to the annexures being admitted into evidence.

(ii) Appeal ground (b)

Fraser J dismissed this ground of appeal on the basis that "if the evidence before the liquidator established insolvency the same conclusion must follow upon the evidence at the trial".

(iii) Appeal grounds (c) and (f)

Inaco argued that the trial judge failed to consider all of the matters considered in *ASIC v Plymin, Elliott & Harrison* [2003] VSC 123, in which Mandie J paraphrased a checklist of common features in situations of insolvency. Fraser J found that the checklist was not intended to act as a proxy for the test of insolvency set out in s. 95 of the Act.

(iv) Appeal ground (d)

Fraser J found that Management's related entity was not, on the evidence, willing and able to supply Management with money to pay its debts as they fell due. Accordingly, this was not a valid ground for arguing that the trial judge erred in his finding of insolvency.

(v) Appeal ground (e)

Fraser J held that the Liquidator's evidence that "given the lack of real assets and the high level of debts, it appears highly unlikely that [Management] would have been able to source funds from any other party" was given without objection and was of sufficient probative force to establish Management's insolvency.

(vi) Appeal ground (g)

Fraser J found that ground (g) did not involve a contention that Inaco was denied procedural fairness and was merely seeking to reargue the merits of a reasoned decision.

(vii) Appeal ground (h)

Fraser J found that the trial judge did not fail to address or consider the substance of the matters raised by Inaco in its submissions because he fairly summarised both parties' submissions, explained the relevant legislative principles, and explained why the Liquidator's arguments were persuasive.

6.3 Determining pecuniary penalties under the National Credit Act and Code

(By Luca Moretti, Herbert Smith Freehills)

Make it Mine Finance Pty Ltd, in the matter of Make it Mine Finance Pty Ltd (No 2) [2015] FCA 1255, Federal Court of Australia, Beach J, 18 November 2015

(a) Summary

This decision provides guidance for courts on the approach to be taken and principles to be considered in determining pecuniary penalties under:

- Schedule 1 (National Credit Code) to the National Consumer Credit Protection Act 2009 (Cth)-the Code; and
- National Consumer Credit Protection Act 2009 (Cth)-the National Credit Act.

(b) Facts

Make it Mine Finance (MIM) provides credit to customers, whose main source of income is Centrelink payments.

On 28 April 2015 Beach J handed down judgment, declaring that:

- MIM had committed four contraventions of the disclosure requirements in s. 17 of the Code in respect of each of 24,377 credit contracts entered into between 1 July 2010 and 1 March 2013.
- MIM entered into credit contracts while unlicensed, contravening items 4(1) (in relation to 1,830 credit contracts entered into between 1 July 2010 and 31 December 2010) and 6(1) (in relation to credit contracts between 1 January 2011 and 20 April 2011) of Part 2 of Schedule 2 to the National Consumer Credit Protection (Transitional and Consequential Provisions) Act 2009 (Cth).
- MIM had committed four contraventions of the responsible lending obligations under s. 128(c), (d) and s. 130 of the National Credit Act in respect of 20,763 credit contracts entered into between 21 April 2011 and 1 March 2013.

In this decision Beach J determined the pecuniary penalties, stating they should be fixed by reference to the three categories of contravention (applying *ASIC v The Cash Store Pty Ltd (in liquidation) (No 2)* (2015 FCA)).

(c) Decision

(i) Maximum penalties

Though there were technically two separate licensing breaches, to avoid duplication the maximum penalty for both was set at $1.1 million.

Beach J concluded that there were in substance two breaches of the responsible lending provisions in the National Credit Act. MIM breached s. 128(c) by failing to assess the unsuitability of each credit contract in accordance with s 129. The breach of s. 128(d) involved two sub-categories of contravention, being a failure to make reasonable inquiries about the consumer's financial situation (s. 130(1)(b)) and a failure to verify the consumer's financial situation (s. 130(1)(c)). However there was such substantial overlap that the s. 128(d) breaches were

considered together with a maximum penalty of $2.2 million. The maximum penalty for the disclosure breaches was $2 million.

(ii) General principles in imposing pecuniary penalties under this legislation

Beach J held that while the concept of "truth in lending" should not be disregarded, it is not appropriate to analyse the statutory framework through a catchphrase drawn from social philosophy (citing *Australian Finance Direct Ltd v Director of Consumer Affairs Victoria* (2007) 234 CLR 96 at [19]). Instead Beach J outlined general principles to be considered to the extent they are not overridden by statute:

- Deterrence is the principal object of imposing a pecuniary penalty. Judges should ensure that penalties are neither too small, so that they become a strategic business cost, nor too oppressive.
- The process applied in determining penalty figures in criminal sentencing in *Markarian v The Queen* (2005) 228 CLR 357 provides guidance for pecuniary penalties under the National Credit Act and the Code.
  - Assessment of the penalty is a discretionary judgment.
  - It is rarely appropriate to start with the maximum penalty and make proportional deductions.
  - The Court "may not add and subtract item by item from some apparently subliminally derived figure" (citing *Wong v The Queen* (2001) 207 CLR 584).
- Penalties imposed for analogous contraventions (both of other respondents and in other cases) should not be unequal, however such comparisons require close consideration of the facts.
- Specific deterrence will require greater penalties for contraveners with greater resources.
- The total penalty for all offences should not exceed what is appropriate for the conduct considered together.
- Considerations for determining penalties under s. 224 of Schedule 2 (The Australian Consumer Law) to the Competition and Consumer Act (2010) 1974 (Cth) (the CCA) may also be of assistance.

(iii) Disclosure contraventions

In determining the penalties the general principles above were considered along with the relevant factors in s. 113 of the Code. Of particular note were the following points:

- Beach J stated that the intended penalty would not significantly alter the prudential standing of MIM (s. 113(3)).
- In reference to its conduct MIM argued first that it believed that it was operating a consumer leasing business. This was rejected on the basis of evidence in MIM's application for a credit licence and its correspondence with lawyers (s. 113(4)(a)). Secondly MIM argued that the conduct was the result of MIM's complete dependence on advisers. However Beach J refused to accept this because the breaches occurred due to MIM's failure to seek comprehensive regulatory advice in 2008 (lawyers were engaged for only 3.5 hours) and then it acted inconsistently with legal advice in 2011 (MIM removed details required by the Code from contracts drafted by different lawyers).
- Beach J did not accept ASIC's contention that MIM acted deliberately. Rather he concluded that MIM acted with reckless indifference to its

statutory obligations (s. 113(4)(b)).
- While customers may have lost opportunities to pursue lower cost credit options and were deprived of statutory protections, there was no evidence of specific loss for the debtors (s. 113(4)(c)).
- MIM first became aware of the contravention by October 2012, and ought to have become aware when lawyers advised on their contracts with customers. Despite this MIM continued to use non-compliant contracts until March 2013 (s. 113(4)(d)).
- MIM's application was not made in a timely fashion and though there was co-operation with ASIC, it cannot be said the application was unprompted by potential regulatory action (s. 113(4)(h)).

Having particular regard to these matters Beach J concluded that $500,000 was an appropriate penalty.

(iv) Licensing and responsible lending

While s. 167 of the National Credit Act does not prescribe relevant factors it is appropriate to apply both the general principles and considerations in s. 113 of the Code outlined above in calculating penalties. Of particular note were the following points:

- Beach J concluded that the licensing breaches arose through MIM's inadvertence, while the responsible lending breaches were the result of MIM's reckless indifference to its statutory obligations.
- MIM's significant net profits and assets for the 2014 financial year of $8.7 million and $15.3 million respectively were discussed. While the business may have had some cash flow issues, this did not mean the penalties imposed would have a crippling effect.
- Beach J emphasised the importance of general deterrence in the growing consumer lease industry and while he accepted that MIM had changed its conduct significantly that did not eliminate the need for specific deterrence.

Beach J fixed penalties of $250,000 for the licensing breaches and $500,000 for the responsible lending breaches. Though responsible lending breaches are often considered more serious than disclosure breaches the same penalty was imposed because the disclosure breaches resulted from legal advice that was ignored.

Having regard to proportionality, the importance of deterrence (particularly general deterrence), discounts for MIM's co-operation with ASIC, MIM instituting one of the proceedings and recent changes to its procedures, Beach J was satisfied both that the total penalty of $1.25 million was appropriate for the contraventions as a whole and that MIM had the capacity to pay the penalty.

6.4 Relevant factors considered in insider trading sentencing

(By Robert Wright and Emma Reed, King & Wood Mallesons)

Kamay v The Queen [2015] VSCA 296, Supreme Court of Victoria, Court of Appeal, Warren CJ, Redlich and Kaye JJA, 13 November 2015

(a) Summary

Between August 2013 and May 2014, Kamay and Hill, the two co-offenders, had an agreement whereby Hill, an analyst with the Australian Bureau of Statistics (ABS) would provide to the applicant, an associate director with the National Australia Bank, sensitive and unpublished ABS "main economic indicators" (MEI) information. Kamay would use that information to conduct trades of margin foreign exchange (FX) contracts on the foreign exchange derivatives market. Kamay pleaded guilty and was sentenced to seven years imprisonment at trial on four counts of insider trading. Kamay appealed the sentence on the following grounds:

- imposing individual sentences, a total effective head sentence and non-parole period, that were manifestly excessive and which were further particularised on two accounts:
  - failing properly to discriminate between the applicant's four separate counts of insider trading;
  - failing properly to take into account the profit derived by the applicant on each separate account of insider trading and placing too great an emphasis on this profit;
- there was disparity between his sentences and that of his co-offender, Hill, for substantially the same offences;
- the sentencing judge erred in ordering cumulation on the sentence imposed in respect of charge 11 which related to the offence of dealing in the proceeds of crimes greater than $100,000.

The Court of Appeal granted leave to appeal, but dismissed the appeal, concluding that the sentences were not manifestly excessive, and that the other grounds were also not made out.

(b) Facts

The agreement between Kamay and Hill extended to trades over a period of approximately 12 months with the aim of each of Kamay and Hill receiving $50,000 (based on a balance of $200,000 after tax). Pursuant to that agreement, Kamay opened an account with a foreign exchange provider and completed 21 trades between September 2013 and May 2014 based on MEI information provided by Hill. These trades resulted in a net profit of around $195,000.

Kamay, independent from Hill, also opened three further accounts. The applicant traded on MEI information provided by Hill in these other accounts. Hill was not aware of these accounts, nor was he aware of the trades made through them. In total, the applicant made a gross profit of more than $8 million (and net profit of $7 million). Less than $200,000 of that amount was obtained in accordance with the initial agreement with Hill. The applicant received a combined sentence of seven years in total, the largest sentence ever imposed in Australia for insider trading.

(c) Decision

The Court of Appeal considered the following factors in determining whether the sentences imposed were manifestly excessive:

(i) Weight attached to profits

The applicant submitted that the sentencing judge erred in placing too much weight on profits, and instead should have relied on the amount invested. The Court of Appeal rejected this argument, drawing upon the reasoning in *R v*

Glynatsis [2013] NSWCA 131 where Hoeben CJ observed that profit will be especially relevant where "for a comparatively small investment, a very large profit [was] made"; and noted that the nature of margin FX derivative trading is such that "[Kamay] only needed to invest a small amount of the [his] own money to make very substantial profits". As such, relying solely on the amount invested as opposed to profits generated (amongst other factors) for the purposes of sentencing would have been inappropriate.

(ii) Duration of trading period and the number of trades

The applicant also submitted that where the offence occurred over a shorter period of time, or over a smaller number of trades, the gravity of the offence was diminished. The Court of Appeal rejected this submission, adopting the reasoning of T Forrest J in *O'Reilly* [2010] VSC 138, who distinguished between circumstances in which profit rested largely upon chance, and those where profits were nearly certain. Where gains are nearly certain, as in this case, profit will be an important if not prime indicium of the objective seriousness of the offence (as opposed to trading duration or volume which were not considered prime indicia of the gravity of offending).

(iii) The quality of the inside information

The Court of Appeal also drew on the reasoning of Hulme J in *R v Joffe* [2015] NSWSC 741 who considered that the quality of the inside information was a relevant consideration for sentencing purposes. The total number of contracts entered into by the applicant, combined with the ratio of profit to the number of transactions, demonstrated the high quality of the information. Due to the quality of the information the applicant was able to make calculated and predictable transactions, as evidenced by the evolving trading patterns over the course of the offending. The Court of Appeal found that the confidence and certainty of outcome in the context of the profits made by the applicant justified disparity in sentencing.

(iv) Ease of trading

The Court of Appeal also rejected the applicant's submission that the use of a mobile phone to trade for short periods of time diminished the degree of criminalisation. The speed and efficiency of the trading through the use of smartphone trading "apps" was held to require sentences which would satisfy the principles of general deterrence and denunciation.

(v) Size and liquidity of the market

The Court of Appeal also rejected the role the nature of the market could play in measuring the objective gravity of the offence where it was clearly possible in that market for an offender to make large profits in an exceptionally short period of time, often a matter of minutes or even seconds.

(vi) No identifiable victims

The Court of Appeal found that since certain counterparties made a corresponding loss to each of Kamay's profitable trades, there was in fact an "identifiable victim" which may not have otherwise suffered that loss had the trade not occurred. The Court of Appeal also endorsed the views expressed in *Hartman v Director of Public Prosecutions (Cth)* [2011] NSWCCA 261 that the "integrity of the market" is also an identifiable victim in the context of insider trading.

(vii) Relevance of youth, good character and loss of profession

The Court of Appeal dismissed the role such factors could play in sentencing discretion, noting that such factors are unexceptional in white collar crimes. Following *Director of Public Prosecutions (Cth) v Gregory* (2011) 34 VR 1 the Court of Appeal also highlighted the importance of general deterrence in white collar crime, especially given the "fear" that the prospect of incarceration may instil in such offenders. They also noted increases to the maximum criminal penalties for insider trading, which supported deterrence for white collar crime in these circumstances.

The Court of Appeal rejected the argument that parity principles could be invoked between Kamay's and Hill's sentences. Hill obtained and passed on such information in the hopes of making $50,000 for himself, while the applicant's use of information went well beyond this plan. It was held that the stark differences between Hill and the applicant demonstrated that the "notion of equal justice" was not offended by the sentences imposed on Hill and the applicant.

The applicant submitted that the sentencing judge erred in ordering a three month cumulation on the sentence imposed in respect of the money laundering charge. This ground was also not made out. It was held that the applicant's use of the funds including the purchase of property was the very type of conduct the offence was intended to capture, supporting the decision that some cumulation was necessary in the circumstances.

6.5 Court considers the obligation to provide information and documentation in a partnership agreement

(By Isabelle Paton and Chanelle Douglas, Corrs Chambers Westgarth)

Leximed Pty Ltd v Morgan [2015] QSC 318, Supreme Court of Queensland, McMurdo J, 12 November 2015

(a) Summary

Leximed Pty Ltd, as trustee for each of the McCosker Trust and the Medicolegal Trust respectively, brought proceedings against a director, Dr Morgan, seeking information and documentation from Dr Morgan as to the number of his medico-legal appointments during 2008 to 2014 inclusive. Leximed also applied to the court for the special referee that had been previously appointed to provide a further report or an explanation or for the question originally referred to him to be remitted for further consideration. Leximed argued that Dr Morgan was obliged to provide the requested information by reason of his duties as a director of Leximed under ss. 180, 181 and 182 of the Corporations Act 2001 (Cth) (the Corporations Act) which require Dr Morgan to act with reasonable care and diligence and in the best interests of the company and to not use his position as a director of Leximed to gain an advantage for himself.

The court accepted the findings made in the special referee's report and held that Dr Morgan was under no obligation to provide the information sought, but that in any event, the information sought by Leximed had since been provided by virtue of the special referee's report and evidence from an employee of Dr Morgan.

(b) Facts

The applicant, Leximed Pty Ltd (Leximed), is a company which conducts a business as a trustee of two trusts providing medico-legal opinions. The two trusts are the McCosker Trust, controlled by Debra McCosker, and the Medicolegal Trust, controlled by the respondent, Dr Morgan, who is an orthopaedic surgeon and a provider of medico-legal services. Ms McCosker and Dr Morgan were and are the only directors of Leximed.

In October 2009, Leximed in its capacity as trustee for the McCosker Trust (McCosker) and Leximed in its capacity as trustee for the Medicolegal Trust (Medicolegal) entered into a partnership agreement (the Agreement).

By the Agreement, Leximed contracted with Dr Morgan to provide medico-legal opinions. Under the terms of the Agreement, Dr Morgan is also permitted to provide medico-legal services in the course of the Brisbane Private Hospital business, subject to a qualification that the number of appointments for medico-legal opinions does not exceed 10 per cent from year to year.

Ms McCosker became concerned that Dr Morgan's medico-legal practice outside Leximed's business had increased by more than the permitted rate.

In light of her concerns, Ms McCosker obtained the court's leave under s. 237 of the Corporations Act to bring proceedings in the name of, and on behalf of, Leximed in its capacity as trustee for the McCosker Trust and in its capacity as trustee for the Medicolegal Trust, against Dr Morgan, seeking information and documentation from him, including the number of Dr Morgan's medico-legal appointments for each calendar year from 2008 to 2014 inclusive (the Requested Information and Documentation).

By an affidavit dated 6 March 2015, Ms Bowker, Dr Morgan's private secretary, calculated the number of medico-legal patient appointments in the Brisbane Private Hospital business between, *inter alia*, 2008 and 2014 inclusive as 3,203.

In April 2015, a special referee, Mr Brian McDonald, a chartered accountant, was appointed by the court pursuant to rl. 501(1)(b) of the Uniform Civil Procedure Rules 1999 (Qld) (the UCPR) to provide a written opinion in relation to the number of medico-legal patient appointments Dr Morgan conducted in the course of the Brisbane Private Hospital business for each calendar year between 2008 to 2014 inclusive. The purpose of Mr McDonald's appointment was to enable the court to assess the accuracy of Ms Bowker's calculations.

Rule 501(1)(b) of the UCPR provides that:

1. The court may- ...
    b. (b) make an order or give judgment in the proceeding on the basis of the opinion, decision or findings in the report as it considers appropriate.

On 25 May 2015, Mr McDonald produced a report which provided that the total number of medico-legal appointments in the calendar years 2008 to 2014 inclusive was 3,191, which substantially corresponded with Ms Bowker's evidence.

In these proceedings, Leximed also made an application that Mr McDonald provide a further report or an explanation or for the question originally referred to

him to be remitted for further consideration.

(c) Decision

Despite criticisms made by Leximed of Mr McDonald's report, the court found that his methodology was logical and sound. The court ultimately accepted the special referee's findings (except as to the number of appointments for the 2014 calendar year due to a minor omission). On this basis, the court held that Leximed's application for orders that the special referee provide a further report or an explanation or for the question originally referred to him to be remitted for further consideration is refused.

In support of the relief sought in its Originating Application, Leximed argued that it was entitled to the Requested Information and Documentation on two main grounds, namely, that:

a. Ms McCosker and Dr Morgan are parties to the Agreement and the Agreement requires Dr Morgan to provide the Requested Information and Documentation; and/or
b. Dr Morgan is obliged to provide the Requested Information and Documentation by reason of his duties as a director of Leximed under ss. 180, 181 and 182 of the Corporations Act which require Dr Morgan to act with reasonable care and diligence and in the best interests of the company and to not use his position as a director of Leximed to gain an advantage for himself.

In relation to Leximed's first argument, the court held that Dr Morgan was not obliged to provide the Requested Information and Documentation but that, in any event, the information sought has now been provided through the evidence of Ms Bowker and Mr McDonald's report.

Under cl. 18.1(b) of the Agreement, each Partner agrees to be just and faithful to the other Partners and Directors who are associated with a Partner and give to them, *inter alia*, full information and truthful explanations of all matters relating to the affairs of the Partnership. Leximed argued that Dr Morgan was a party to the Agreement and therefore bound by cl. 18.1(b) to provide the Requested Information and Documentation. The court rejected Leximed's construction of the Agreement given its clear and consistent demarcation between the terms "Partner" and "Directors who are associated with a Partner". As the Agreement defined McCosker and Medicolegal as "the Partners", the court held that McCosker and Medicolegal were the parties to the Agreement, rather than Ms McCosker or Dr Morgan as individual directors. In addition, the court concluded that even if Dr Morgan was bound by the Agreement, given he was not exceeding the 10% limit, the information as to Dr Morgan's practice could not be relevant to the affairs of the Partnership.

The court also held that no contractual obligation could be imposed on Dr Morgan to provide the Requested Information and Documentation on the basis that Ms McCosker and Leximed have now been provided with the relevant information contained within the referee's report and there would be no utility in requiring that it be provided again.

In considering this argument, the court analysed whether a party could validly contract with itself (as Leximed had arguably done here), however the court did not reach a concluded view on this question as it was unnecessary.

The court rejected Leximed's second argument to the effect that Dr Morgan had breached his duties as a director. The effect of both of Ms Bowker's evidence and Mr McDonald's report is that Dr Morgan has not exceeded the 10% limit provided for in the Agreement. In light of this, Leximed's interests could not be affected by whether or not the information about Dr Morgan's practice is disclosed.

The court also rejected an argument to the effect that Dr Morgan breached his duties as a director by causing Leximed to enter into the Agreement because the Agreement was clearly made between two distinct interests (namely, the two capacities in which Leximed acted as a trustee) where Ms McCosker acted for Leximed in its capacity as trustee for the McCosker Trust and Dr Morgan acted for Leximed in its capacity as trustee for the Medicolegal Trust. The court held that, in such circumstances, neither was obliged to protect the interests of the other trust.

The court ultimately dismissed the Originating Application.

6.6 Directors' duties owed to company and not to shareholders

(By Jason Choi, DLA Piper)

Sharp v Blank [2015] EWHC 3220 (Ch), England and Wales High Court, Chancery Division, Nugee J, 12 November 2015

(a) Summary

This judgment is the last of a series of judgments that Nugee J has given relating to shareholder litigation arising out of Lloyds Banking Group plc (Lloyds-then called Lloyds TSB plc) acquisition of Halifax Bank of Scotland (HBOS). The claimants alleged that Lloyds' directors owed to Lloyds' shareholders various fiduciary duties, and the defendant directors applied for summary judgment under rl. 24.2 of the *Civil Procedure Rules (UK)* (the CPR) and/or strike out of various parts of the claimants' pleading under Rule 3.4(2)(a) of the CPR.

Nugee J held that directors may owe fiduciary duties to a company's shareholders only where, on the facts of the particular case, a special relationship exists between the directors and the shareholders. In this case, the claimants had failed to plead any special relationship between the directors and the shareholders. All the pleaded facts amounted to was that the directors, who knew more about HBOS's financial position than the shareholders, gave the shareholders advice and information to enable them to decide how to vote at an Extraordinary General Meeting (EGM). As such, his Honour was not satisfied that the directors owed fiduciary duties to the shareholders.

(b) Facts

Nugee J provided the facts of this case in an earlier judgment: *Sharp v Blank* [2015] EWHC 3219 (Ch). In early 2009 Lloyds acquired HBOS. An EGM of Lloyds shareholders was called to approve the proposed acquisition in November 2008. Prior to the EGM Lloyds' directors published a circular to the shareholders. The claimants brought proceedings against the directors alleging, *inter alia*, that the directors were in breach of fiduciary duties that they owed to them (as Lloyds' shareholders). In particular, the claimants alleged that:

- the circular which Lloyds sent to its shareholders ahead of the EGM contained material misstatements and omissions which made it misleading; and
- the directors' recommendation to shareholders that they vote in favour of the resolutions at the EGM was in breach of their fiduciary duties, given their knowledge of HBOS's financial position at the time.

The claimants alleged that the fiduciary duties which the defendants owed to the shareholders included, *inter alia*, the following duties (the Fiduciary Duties):

a. a duty to act in good faith;
b. a duty to act in the best interests of the shareholders and to prevent them from suffering loss;
c. a duty not to mislead the shareholders or conceal material information from them;
d. a duty not to place themselves in a position where their duties to the shareholders conflicted with their personal interests or their duties or obligations to any third party;
e. a duty to act for a proper purpose;
f. a duty to advise and inform the shareholders in clear, and readily comprehensible terms.

The defendants argued that directors of a company owe fiduciary duties to the company and, in general, do not owe such duties to individual shareholders. While accepting that there are exceptions to this general principle, the defendants argued that the claimants had not identified any special circumstances which gave rise to fiduciary duties being owed by Lloyds' directors directly to the shareholders in the period leading up to the EGM.

The defendants did however accept that they owed the shareholders a duty in equity to provide them with sufficient information to enable them to make an informed decision as to how to vote at the EGM (sufficient information duty). As such, the defendants did not dispute that they did owe the shareholders Fiduciary Duties (c) and (f) above as part of their sufficient information duty, but contended that they did not owe the shareholders any other equitable duty than the sufficient information duty.

(c) Decision

(i) Fiduciary duties owed by directors

Nugee J held that Lloyds' directors did not owe fiduciary duties to the shareholders and struck out the fiduciary duty claims.

Nugee J said it was established law that directors of a company owe fiduciary duties to the company. However, Nugee J stated that directors generally do not, solely by virtue of their office of director, owe fiduciary duties to the shareholders, collectively or individually. His Honour said that it was only where, on the facts of the particular case, a "special relationship" exists between the directors and shareholders that directors may owe fiduciary duties to the shareholders.

His Honour considered a number of authorities and stated that the sort of relationship that will give rise to a fiduciary duty will be where there has been "some personal relationship or particular dealing or transaction between them".

Nugee J commented that it will not be enough if the "director, as a director, has more knowledge of the company's affairs than the shareholders" or that "the actions of the directors will have the potential to affect the shareholders". This is because both those factors will almost inevitably exist in all relationships between directors and shareholders.

In this case, the claimants had failed to plead any special relationship between the directors and the shareholders. All the pleaded facts really amounted to was that the directors, who knew more about HBOS's financial situation than the shareholders at the relevant time, gave the shareholders advice and information to enable them to decide how to vote at the EGM. That was the only relationship pleaded and it did not give rise to the alleged fiduciary duties. His Honour found nothing to suggest that the relationship was one where the directors had "undertaken to act for or on behalf of the shareholders in such a way as to give rise to a duty of loyalty, or have undertaken an obligation to put the interests of shareholders first, or are themselves entering into transactions with the shareholders, or where there are any of the other hallmarks of a fiduciary relationship."

(ii) Was the "sufficient information duty" a fiduciary duty?

Nugee J expressed doubt as to whether it was appropriate to describe the sufficient information duty as a fiduciary duty at all.

The claimants argued the Fiduciary Duties were inherent in any fiduciary duty and that once it was accepted that the sufficient information duty was a fiduciary duty, that duty entailed all of the pleaded Fiduciary Duties. Nugee J rejected this argument, and stated that it was an error to label a particular duty as a fiduciary duty and then use that label to determine what the content of the duty is. Rather, his Honour held that it was only possible to characterise a duty as being fiduciary after identifying the content of that duty in the particular factual circumstances. As such, his Honour stated that "the correct starting point is to identify what the content of the sufficient information duty is" and said (at [21]):

> The wellspring of this duty is not that the directors have agreed to put the interests of the shareholders first, but the much more simple one that if they are going to invite the shareholders to a meeting, common fairness requires that they explain what the purpose of the meeting is. That includes being clear and comprehensible and not misleading or tricky; but the reason for this is one of fairness, not of loyalty.

Accordingly, his Honour held that, save for duties (c) and (f) of the Fiduciary Duties that were not in dispute, the other Fiduciary Duties did not form part of the defendants' sufficient information duty and struck them out on the basis that they were not sustainable in law.

(iii) Calling of the EGM

A final question for Nugee J was to decide whether to strike out the claimants' plea that Lloyds' directors acted in bad faith and contrary to the best interests of Lloyds' shareholders by permitting the EGM to take place without providing full information.

Since the only bases for the claimants' plea were breach of Fiduciary Duties (a) and (b) and given Nugee J held that the claimants' fiduciary duty claims were not sustainable in law, his Honour held that the plea was unsustainable and struck it

out.

6.7 "The more appropriate forum": Court examines cross-vesting principles

(By Lauren Jayne Bracewell, Clayton Utz)

Kadac Proprietary Ltd v Complete Health Products Pty Ltd [2015] VSC 613, Supreme Court of Victoria, Sifris J, 9 November 2015

(a) Summary

The Victorian Supreme Court found it was appropriate, and in the interests of justice to transfer a small company oppression proceeding to the Supreme Court of Queensland. It found that the events and conduct which were the subject of the proceeding were particular to Queensland rather than Victoria.

Despite the plaintiffs' submissions that the strict legal issues did not require transfer to another State, it was held that evidence adduced would likely go beyond these contentions and that Queensland was the natural home of these proceedings.

(b) Facts

The plaintiff, Kadac, was a 50% shareholder of Complete Health Products (CHP) and brought an oppression proceeding against CHP and the directors of CHP (the defendants).

The question before the court was whether it was appropriate to grant the defendants' application to transfer the matter from the Supreme Court of Victoria to the Supreme Court of Queensland pursuant to s. 1337H(2) of the Corporations Act 2001 (Cth). Section 1337L requires the court to have regard to:

- the principal place of the business concerned in the application; and
- where the events and conduct took place that are the subject of the application.

CHP was incorporated in Queensland, and the company books, operations and directors were based in Queensland. The plaintiff resided in Victoria. The plaintiff submitted that the evidence relied on by the defendants, such as the company's location, was not relevant to the context of the dispute. The issues, namely excessive directors fees, failure to declare dividends and failure to appoint directors to the board were all matters that could be dealt by reference and analysis of the Share Purchase and Shareholders Agreement between the parties.

(c) Decision

Sifris J held it was in the interests of justice to transfer the proceeding to the Supreme Court of Queensland. Sifris J conceded that it is the nature of these applications that one side will suffer some disadvantage; however, the plaintiffs did not demonstrate that they would be unable to deal with the case if it was transferred.

In his judgment he applied the principles enunciated in *Resource Equities Ltd (Subject to Deed of Company Management) v Carr* [2007] WASC 246 and *BHP*

Billiton Ltd v Schultz [2004] HCA 61; (2004) 221 CLR 400. These key principles are:

- it is not necessary that the transferor court be a "clearly inappropriate" forum but only that, in the interests of justice, a transferee court is "more appropriate";
- determining the appropriate jurisdiction is a "nuts and bolts" management decision;
- the most appropriate court is the natural forum, as determined by factors connecting the proceeding to that forum including matters of convenience and expense, the places where the parties respectively reside or carry on business, and the law covering the relevant transaction; and
- the weight of connecting factors will vary from case to case.

6.8 Non-compliance with a statutory demand after an application to wind up gives rise to a presumption of insolvency

(By Meagan Ryan, MinterEllison)

Simpson v CT Partners Australia Pty Ltd [2015] FCA 1191, Federal Court of Australia, Gilmour J, 6 November 2015

(a) Summary

Gilmour J allowed an application for winding up on grounds of insolvency following two events which independently gave rise to the presumption of insolvency under s. 459C of the Corporations Act 2001 (Cth) (the Act). The first event involved a failure by CTP Australia (CTP) to comply with a statutory demand pursuant to s. 459C(2)(a) of the Act. The second event involved a secured creditor taking possession of CTP's assets pursuant to ss. 459C(e) and (f). The presumptions of insolvency were not rebutted.

(b) Facts

On 30 June 2015 the plaintiffs made an application to wind up CTP on the basis of insolvency. CTP owed the first plaintiff "at least $176,922.67" in unpaid bonuses and the second plaintiff was owed $867,539.00, an amount which represented half of the purchase price listed under a share agreement between CTP and the plaintiffs. Accordingly, the plaintiffs had standing pursuant to ss. 459P(1)(b) and 462(2)(b) of the Act as creditors of CTP.

A signed letter, addressed to the "Former clients of CTPartners Executive Search, Inc" was sent on 1 July 2015, advising CTP's clients that CTLiquidation LLC (CTL) had purchased the collateral from CTPartners Executive Search, Inc, and that DHR Worldwide, Inc was to collect any unpaid accounts that CTL was now entitled to (at [30]).

On 2 July 2015, a "notice of default and enforcement" was issued to CTP by JP Morgan, which was acting as a secured creditor. In an attached letter, JP Morgan advised CTP that it had "exercised its power ... to purchase and sell the Collateral" and that it had entered into an agreement with CTL to do so (at [29]).

On 8 July 2015, Johnson Executive Search Pty Ltd served CTP with a statutory

demand for $1,973,695.20. The 21-day period in which CTP was to pay the debt expired on 29 July 2015.

(c) Decision

Relevantly, s. 459C(2) of the Act permits the Court to presume that a company is insolvent if:

> during or after the 3 months ending on the day when the application was made:
>
> a. the company failed (as defined by s. 459F) to comply with a statutory demand; or ...
>
> c. a receiver, or receiver and manager of, property of the company was appointed under a power contained in an instrument relating to a circulating security interest in such property; ...
>
> e. a person entered into possession, or assumed control, of such property for such a purpose; or
> f. a person was appointed so to enter into possession or assume control (whether as agent for the secured party or for the company).

Pursuant to s. 459A of the Act, the Court can order an insolvent company be wound up. The onus of rebutting the presumption of insolvency rests with the defendant. CTP did not enter an appearance. Gilmour J considered whether or not the actions of JP Morgan as secured creditor and CTP's non-compliance with the statutory demand entitled the plaintiffs to rely on the rebuttable presumption of insolvency.

(i) First event giving rise to the presumption of insolvency

Gilmour J was satisfied that JP Morgan's actions on 1-2 July 2015 in enforcing its security interest, issuing the notice of default and enforcement, selling CTP's accounts receivable (assets) and directing any unpaid accounts to be paid to DHR Worldwide, Inc, gave rise to a presumption that CTP was insolvent pursuant to ss. 459C(2)(e) or (f) of the Act.

(ii) Second event giving rise to the presumption of insolvency

Independent of the first event and ss. 459C(2)(e) or (f), Gilmour J was satisfied that CTP could also be presumed to be insolvent due to its noncompliance with the statutory demand served by Johnson Executive Search Pty Ltd on 8 July 2015, pursuant to s. 459C(2)(a) of the Act. The failure to comply with the statutory demand occurred on 29 July 2015, after the winding up application had been made on 30 June 2015.

Gilmour J noted (at [35]) that there have been "differing judicial views" in respect of the s. 459C(2) requirement that an event giving rise to the presumption of insolvency occurs "after the 3 months ending" [on the day when the application is made].

His Honour cited with approval McMurdo J's analysis and interpretation of the timing of noncompliance with statutory demands and s. 459C(2) in *Equititrust Ltd v Willaire Pty Ltd* [2012] QSC 206 (*Equititrust*). Specifically, McMurdo J's

comments in *Equititrust* at [87], "there is no authority for the proposition that in a case ... where the application is filed originally upon other events giving rise to the presumption [of insolvency], a subsequent failure to comply with the statutory demand must be disregarded ... the effect of section 459Q is to make it 'impermissible to file an originating process on (the basis of non-compliance with a statutory demand) until the failure has occurred and the particulars of it can be stated', but that s. 459Q does not preclude a reliance upon a failure to comply with a demand which occurs after an application is duly commenced".

Accordingly, Gilmour J considered CTP's non-compliance with the statutory demand satisfied the requirements of s. 459C(2) of the Act and gave rise to a presumption of insolvency.

(iii) Alternative grounds and orders

The application for winding up was alternatively made on grounds that it would be just and equitable to do so, pursuant to s. 461(k) of the Act. While Gilmour J considered it unnecessary in the circumstances to consider the just and equitable ground he opined that there was enough material before the Court for CTP to be wound up on that basis.

His Honour considered the two events were sufficiently independent to make an order for winding up CTP in insolvency given CTP did not take any steps to rebut the presumption, arising from both events, that it was insolvent or to appoint an administrator.

Gilmour J made orders for CTP to be wound up on the grounds that it was insolvent. His Honour appointed liquidators to CTP and ordered the costs incurred by the plaintiffs in making the application for winding up of CTP be "agreed or taxed and reimbursed" by the liquidators of CTP pursuant to s. 466(2) of the Act.

6.9 Lack of member approval will not invalidate agreements

(By Tracy Albin, Herbert Smith Freehills)

Mutual Holdings Pty Ltd v Adam Shepard in his capacity as administrator of Quest Minerals Ltd [2015] WASC 412, Supreme Court of Western Australia, Mitchell J, 5 November 2015

(a) Summary

This case considered whether a Deed of Company Arrangement (DOCA) is capable of contravening s. 208(1) of the Corporations Act 2001 (Cth) (the Act) as well as the effect of contravention on the enforceability of agreements. Mitchell J held that DOCAs are entered into by the members of a company through the administration process and therefore cannot contravene s. 208(1). It was also held that contravention of s. 208(1) does not render an agreement invalid or unenforceable. Therefore the defendant in these proceedings did not have grounds to refuse to admit the plaintiff's proof of debt for the DOCA.

(b) Facts

The deed administrator refused to approve the proof of debt from the two

companies based on an alleged contravention of s. 208(1) of the Act which requires public companies to gain member approval before entering into transactions that give financial benefit to related parties. Specifically, the deed administrator claimed that both Mutual Holdings Pty Ltd (Mutual) and Corporate Admin Services Pty Ltd (CAS) were related entities of Quest and that the relevant financial benefits did not fall within any exception to the requirements of s. 208(1).

The defendants claimed that the DOCA agreement, the execution of which extinguished all previously existing agreements relating to the relevant debts, was in contravention of s. 208(1). This was because it made provision for the future payment of financial benefits to related parties by Quest, without member approval. The defendant asserted that the sole director and company secretary of both Mutual and CAS, Vladimir Nikolaenko, was also the director of Quest, despite not formally being appointed to the position.

(c) Decision

Mitchell J found that a DOCA could never be in contravention of s. 208(1) because it is a statutory instrument brought into existence by a resolution of creditors, and Quest had a statutory obligation to enter into such an arrangement under the terms of the administration. Therefore, no contravention could be established because the administration process, and by implication the DOCA, was entered into and approved by the members.

Mitchell J turned to the relevant sections in the Act outlining the consequences of a contravention, to determine the enforceability of the agreements. These included ss. 103(2)(a) and 209(1)(a) which state that a contravention of s. 208(1) does not render a contract invalid or unenforceable. Mitchell J also referred to s. 207 of the Act, which provides that the rules in Chapter 2E are designed to protect the interests of a public company's members as a whole by requiring member approval for the giving of financial benefits to related parties that could endanger those interests.

Mitchell J then considered whether an enforceable debt existed at 9 May 2014. The decisions in *HCK China Investments Ltd v Solar Honest Ltd* (1999) 165 ALR 680 and *Winpar Holdings Ltd v Goldfields Kalgoorlie Ltd* (2001) 166 CLR 144 were both followed. These held that it would be inconsistent with the legislative scheme to treat agreements that are in contravention of s. 208(1) as invalid or unenforceable. A number of cases were also distinguished, including *Orrong Strategies Pty Ltd v Village Roadshow Ltd* (2007) 207 FLR 245 which held certain agreements invalid on policy grounds. Mitchell J declined to follow this decision, opining that it is up to Parliament to determine policy issues through the use of statute. It was held that because the sanctions for a contravention of s. 208 are expressly and adequately provided for by the statute, there is no discretion for the court to consider further matters such as policy when deciding these types of cases.

Mitchell J allowed the plaintiff's appeal and accordingly reversed the decision of the deed administrator. The plaintiff's claim from 11 September 2004 for $1,407,485 (Mutual) and $768,040.31 (CAS) was therefore admitted to proof under the DOCA and the Creditor's Trust Deed. Furthermore, the defendant's application for set-off of their liability to Mutual and CAS where a contravention of s. 209(2) arose was refused because this issue had not been considered by the court.

6.10 Who is the proper plaintiff in a second limb *Barnes v Addy* claim?

(By Katrina Sleiman and Natasha Cameron, Corrs Chambers Westgarth)

Nicholson Street Pty Ltd (receivers and managers appointed) (in liquidation) v Letten [2015] VSC 583, Supreme Court of Victoria, Judd J, 4 November 2015

(a) Summary

The plaintiffs sought leave to file a further amended statement of claim to include a claim that the defendants' conduct was in breach of trust under the second limb of *Barnes v Addy*.

The Court found that so long as the plaintiffs maintained the case based on the second limb of *Barnes v Addy*, the interests of beneficiaries must be transparently protected by joining an independent representative beneficiary or beneficiaries.

The Court also found that the plaintiffs failed to make sufficiently precise allegations that the defendants' conduct was in breach of trust or established required knowledge that the defendants' conduct made a difference, in the sense that it advanced the primary breach in some way. Application for leave was refused.

(b) Facts

In November 2010, the Court made orders authorising the receivers of certain property of unregistered managed investment schemes, in which the defendants in this proceeding, Letten and Lane, were involved, to establish a Common Fund of pooled assets. The receivers had been appointed as joint and several receivers and managers of the property following the winding up of certain of the schemes.

In June 2014, orders were made authorising the deployment of part of the Common Fund to institute and prosecute the proposed proceeding against the defendants. Letten had been a director and secretary of the proposed plaintiffs, Nicholson Street Pty Ltd, The Glen Centre Hawthorn Pty Ltd and Twinview Nominees Pty Ltd. Lane had also been a director of each company.

The plaintiffs alleged that Letten promoted unregistered managed investment schemes, inviting investors to invest in real estate joint ventures to be carried out through a company managed and controlled by him. The plaintiffs alleged that each such company acted as trustee on behalf of the investors.

LGH Administration Pty Ltd, which is neither a plaintiff nor defendant, is alleged to have operated as the central treasury vehicle for the project trusts. Letten was a director of LGH and alleged to be its controlling mind and will. Lane, who had been a director of the plaintiffs and LGH in later years, was alleged to be intimately involved in the day to day financial affairs of LGH.

Each plaintiff alleged breaches of trust procured by Letten, and that each of the breaches was part of a dishonest and fraudulent design. They alleged that Letten and Lane assisted each plaintiff in its conduct in breach of trust.

(c) Decision

The plaintiffs framed their claims under the second limb of *Barnes v Addy*. Under that limb, a defendant is liable if that defendant assists a trustee or fiduciary with knowledge of a dishonest and fraudulent design on the part of the trustee/fiduciary.

The plaintiffs alleged that were it not for the breaches of trust, the financial position of the trusts would have been vastly improved. They alleged losses suffered by the trusts and an obligation to restore trust losses. The plaintiffs claimed compensation in equity for the amount each plaintiff had assessed as its liability to the trust.

(i) The proper plaintiffs

The plaintiffs' formulation of claims under the second limb exposed a conceptual anomaly. They claimed compensation for an alleged liability to restore lost value to the trust, caused by their own dishonesty and fraud. There was no independent plaintiff, such as a new trustee, or a representative beneficiary, to represent the interests of the beneficiaries in addition to the errant trustee who, it was proposed, would make its own assessment of the extent of its liability to restore the trust.

Judd J considered that the conceptual anomaly would not exist if the receivers had brought the claim. They might have alleged that the defendants procured the trustees to act in breach of their obligations. Alternatively, the receivers might have invoked the second limb of *Barnes v Addy*, or taken a less tortured path by alleging a breach of duty by the defendants as directors. These less complex approaches would not require proof of any dishonest or fraudulent design on the part of the plaintiffs.

Judd J sought to determine whether the plaintiffs' application for leave required them to join a representative beneficiary or beneficiaries. The plaintiffs contended that they were and remained proper plaintiffs in the absence of representative beneficiaries. Placing reliance on *Young v Murphy* and the applied principles, the plaintiffs contended that each had a duty as trustee to make good a loss to a trust fund and that even where a breach by the trustee was dishonest and fraudulent, the trustee will have standing to proceed alone and beneficiaries should only be joined as parties if the trustees will not or cannot themselves proceed.

Judd J considered it necessary to ask whether the plaintiffs sufficiently represented the interests of the beneficiaries. His Honour concluded that here they did not. Judd J held that the plaintiffs' proposition was too narrow and that reliance on *Young v Murphy* was misplaced. The categories of circumstances where a trustee might not sufficiently represent the interest of beneficiaries for the purpose of a proceeding are not closed, nor must there exist exceptional or special circumstances.

His Honour reasoned that provided the plaintiffs maintained their case based on the second limb, the interests of the beneficiaries must be clearly protected. While it is true that the plaintiffs had no independent mind, intention or purpose other than the mind, intention and purpose of at least one of the defendants, the objective observer might reasonably experience some disquiet at the prospect of such an important issue in the proceeding, advanced within an adversarial framework, wholly defined and prosecuted by "dishonest and fraudulent" plaintiffs against defendants who knowingly assisted the plaintiffs in the dishonest and fraudulent design.

Judd J noted that the joinder of an independent representative beneficiary or beneficiaries might be achieved under rl. 16.01 of the Supreme Court (General Civil Procedure) Rules 2005 (Vic). Alternatively, transparency might be achieved if the receivers were to become plaintiffs, alleging their appointment and the basis upon which they represent the interests of the investors/beneficiaries.

(ii) Proposed amendments

The defendants formulated a range of objections to the proposed further amended statement of claim, although the focus of their attention was the adequacy of the pleading of fraud and dishonesty.

His Honour noted that there may be circumstances in which proof that a director deliberately conducted the affairs of a company or companies in a particular way will be sufficient to establish the necessary degree of fraud and dishonesty, for the purpose of the second limb of *Barnes v Addy*.

At the heart of the plaintiffs' case against Lane was knowledge based upon his position and functions. His Honour considered the generality of the plea was unsatisfactory, holding that the plaintiffs must allege, with more precision, the information available to Lane that would indicate to an honest and reasonable person that the conduct of each of the plaintiffs was dishonest and fraudulent.

The unsatisfactory foundation of the case against Lane was compounded by the allegation of assistance, which went little further than alleging that Lane had some involvement in the management of the internal finance management entity. For a plea of knowing assistance, which necessarily involves knowledge of dishonesty and fraud, falling in one of the accepted categories, it is necessary to allege with precision the acts of Lane that made him a knowing participant in the breach of trust.

In order to establish knowing assistance, the plaintiffs must prove that the defendants' conduct made a difference, in the sense that it advanced the primary breach in some way. There must be some causal significance to the conduct.

Leave to file and serve the further amended statement of claim was refused.

6.11 Requirements for a funding agreement between two inter-related companies in liquidation and the role of a special purpose liquidator

(By Alex Pitono, DLA Piper)

In the matter of Octaviar Ltd (in liq) [2015] NSWSC 1621, Supreme Court of New South Wales, Brereton J, 3 November 2015

(a) Summary

This case concerned two applications made by a special purpose liquidator appointed to conduct a proceeding against a third party to recover certain voidable transactions.

Brereton J found that the special purpose liquidator was allowed to retain an unused amount paid under a funding agreement between two related companies in liquidation. His Honour also decided that a successful appeal setting aside earlier

court approval did not make an agreement executed pursuant to that approval invalid. Additionally Brereton J also found that a special purpose liquidator appointed to oversee a certain proceeding may make an application for an extension of his power to carry out further proceedings if appropriate.

The case was also significant as the court provided clarification on what was considered to be "necessary" in relation to a liquidator's power "to do all such things as are necessary for winding up the affairs of the company and to distribute its property" prescribed in s. 477(2)(m) of the Corporations Act 2001 (Cth) (the Act). Such power would be required for a liquidator to enter into an effective funding agreement.

(b) Facts

Octaviar Administration Pty Ltd (OA) and its ultimate holding company Octaviar Ltd (OCV) were each subject to a court winding up order and Mr Fletcher and Ms Barnett (the Liquidators) were appointed as the liquidators of both companies. OCV had previously given guarantees secured against some of its assets and made payments to a third party company - Fortress Credit Corporation (Australia) II Pty Ltd (Fortress). The Liquidators sought to recover these payments on the basis that they were voidable transactions and commenced proceeding against Fortress (the OCV/Fortress Proceeding).

Subsequently, the Liquidators discovered that OA also had a separate claim against Fortress which potentially might have conflicted with OCV's claim. Accordingly, the Liquidators appointed a special purpose liquidator (SPL) in order to pursue the OCV/Fortress Proceeding while the Liquidators separately commenced a proceeding on behalf of OA against Fortress (the OA/Fortress Proceeding).

Upon liquidation of the assets of both companies, it was discovered that OCV did not have sufficient funds to commence the proceeding on its own. Accordingly, the Liquidators and the SPL entered into a funding agreement ('the Funding Deed') for OA to provide funding to OCV. In return, OA would be entitled to 25% of the sum awarded in the event that the judgment was made in favour of OCV. Under the Funding Deed, in order to obtain funding the SPL would be required to issue funding notices to the Liquidators.

Pursuant to s. 477(2B) of the Act, court approval was required as the funding agreement was expected to last beyond three months. This was issued on 30 March 2012 by the New South Wales Supreme Court. Subsequently, the Funding Deed was executed in May 2012.

However, Fortress successfully appealed to the New South Wales Court of Appeal on 8 April 2015 in relation to the approval. The Court of Appeal remitted the application for approval back for fresh consideration.

Consequently, on the back of the Court of Appeal's decision the Liquidators decided that they should not comply with the additional funding notices issued by the SPL requesting further funds. However, since the OCV/Fortress Proceeding was imminent, the Liquidators decided to advance a sum of $1.5 million to the SPL. The SPL regarded this as inadequate to cover the risks associated with the proceeding and decided to settle instead.

Subsequently, the Liquidators also settled the OA/Fortress Proceeding. The settlement resulted in Fortress agreeing to assign OA the debt due to Fortress

from OCV alongside the securities held by Fortress in relation to that debt.

In addition, previously in April 2011, the receivers and managers of OCV lodged a proof of debt in relation to the winding up of OA which was rejected by the Liquidators. The receivers and managers appealed the decision although it was discontinued as part of the OA/Fortress' settlement with the provision that it may be renewed should OCV wish to do so. However, if this course of action was taken this might put the Liquidators in conflict as they may have to act for both OCV and OA simultaneously.

The SPL proceeded to make two applications to the court. The first one requested directions from the court pursuant to s. 479(3) of the Act in relation to the following matters:

- How should the SPL distribute the funds that remained in his control;
- Whether the SPL was justified in terminating the Funding Deed (or whether it had been terminated) on the basis of material breach or repudiation;
- Whether the SPL would be justified in making application to extend his power to represent OCV in possible future action against OA in relation to the proof of debt.

The second application was concerned with the remitted hearing for the approval of the funding deed pursuant to s. 477(2B).

(c) Decision

(i) The $1.5 million provided by the general purpose liquidators

As a result of the OA/Fortress' settlement, Brereton J raised the possibility that the Liquidators may be considered as officers of a "secured party" of OCV. Under s. 532(2)(c)(ii) or Act, such person would be disqualified from acting as a liquidator of a company.

Brereton J did not think it was necessary to resolve whether the Liquidators would be disqualified by s. 532(2)(c)(ii). However, his Honour proceeded to weigh the two alternatives. If the Liquidators were in fact disqualified by s. 532(2)(c)(ii) while having the $1.5 million returned to them, the Liquidators would have to account for it to their replacement. However, in this case since the Liquidators did not oppose the SPL retaining the payment and there appeared to be no identifiable risks or detriments in the SPL retaining the funds for the time being, the SPL was justified in retaining the $1.5 million.

(ii) The settlement proceeds

Brereton J considered the impact of the Liquidators' refusal to comply with the funding notices issued by the SPL. The matter was complicated by the impact of Fortress' successful appeal to the New South Wales Court of Appeal.

It was submitted by the SPL that the successful appeal by Fortress should result in the termination of the Funding Deed by frustration or for failure of a condition. Alternatively, the SPL argued that should the Funding Deed still remain on foot, the Liquidators' conduct amounted to repudiation. As such the SPL would be entitled to terminate the Funding Deed if it had not already done so by conduct.

Despite the successful appeal by Fortress to the New South Wales Court of Appeal, ultimately his Honour found that the Funding Deed remained valid and

effective. His Honour stated that although the lack of requisite approval from the court meant the liquidator's act was not binding between the liquidator and the company, this should not affect the right of a third party to obtain performance from the liquidator.

Additionally, as court approval had been obtained at the time the Funding Deed was executed, the Funding Deed remained on foot even if subsequently the order was set aside on appeal. The benefits of such a finding are that OCV would avoid the obligation to pay 25% of the settlement proceeds to OA, and a potential claim for damages for breach of the Funding Deed.

(iii) Expansion of SPL's powers

The Court stated that the SPL was a strong candidate to conduct a fresh appeal against the Liquidators' decision to reject the proof of debt. This was a point that was also agreed to by the Liquidators. Accordingly, the SPL was justified in making an application to extend his powers.

Brereton J also held that it would be appropriate for the SPL to represent the interests of OCV in the contemplated negotiations.

(iv) Approval of the Fortress Funding Deed

Brereton J subsequently considered whether approval should be granted for the Liquidators and the SPL to enter into the Funding Deed. In doing so, his Honour focused on the ground on which the primary judge's approval was overturned - a requirement that the primary judge be satisfied that the Liquidators had an underlying power to enter into the Funding Deed.

The relevant underlying power was the Liquidators' power under s. 477(2)(m) which provides that a liquidator may "do all such things as are necessary for winding up the affairs of the company and distributing its property". His Honour examined whether the outcome of the OVA/Fortress Proceeding would be beneficial to OA so as to necessitate its funding. Brereton J ultimately concluded that there were no clear relevant benefits to OA on the following basis:

- It was not appropriate to evaluate whether the benefits accrued to the group of companies as a whole. The OVA/Fortress Proceeding mainly benefited OVA;
- It was not apparent how the "increased options in terms of allocation of costs" argued by the Liquidators provided any actual or potential benefit to OA;
- The benefit to OA of not having to seek new freezing orders was merely a fraction of funding the costs of the OCV/Fortress Proceeding;
- The subsequent benefit in the OA/Fortress Proceeding should not be taken into account. The important issue was how the OCV/Fortress Proceeding would benefit OA;
- The Liquidators' argument hinged on whether OA would propose to accept an assignment of the charge from Fortress. This was unlikely and in the alternative the success of OCV in a proceeding would reduce the quantum of OA's potential recovery under its own proceeding.

Based on the above basis, Brereton J held that entering the funding agreement was not within the scope of the Liquidators' power to do what was "necessary" to wind up the company. His Honour, however, did mention that there is an arguable case that the Liquidators had the requisite power when they entered into the deed,

which approval was beyond recall once they did so, and it may be prudent for the Liquidators to obtain judicial advice or declaratory relief to that effect.

6.12 Court reduces creditor's statutory demand based on debt created under Building and Construction Industry Security of Payment Act 1999

(By Gary King, MinterEllison)

Re J Group Constructions Pty Ltd [2015] NSWSC 1607, Supreme Court of New South Wales, Robb J, 30 October 2015

(a) Summary

The plaintiff, J Group Constructions Pty Ltd, applied under ss. 459G and 459H of the Corporations Act 2001 (Cth) (the Corporations Act) to set aside a statutory demand for $174,009.96 served by the defendant, PGA Rendering Group Pty Ltd. The demand related to a non-payment under a contract for the supply and application of paint and an acrylic render to the exposed walls of a building being constructed by the plaintiff (the works). The plaintiff refused to pay a portion of the contract price, alleging the works had been completed poorly and with the incorrect products. An adjudicator heard the dispute pursuant to the Building and Construction Industry Security of Payment Act 1999 (NSW) (the Security of Payment Act) and held in favour of the defendant. The defendant filed the adjudication certificate in the District Court and issued a statutory demand for the debt. The plaintiff applied to the Supreme Court to set aside the demand. Robb J of the New South Wales Supreme Court held that the plaintiff had raised a genuine offsetting claim that the products used for the works were not fit for purpose and reduced the statutory demand from $174,009.96 to $8,542.90.

(b) Facts

The plaintiff and defendant entered into an agreement for the works in April 2014. The defendant quoted $290,000 plus GST for the works. The defendant's quote indicated that a number of Dulux products would be used for the works. Before sending an executed copy of the quote to the plaintiff, the defendant made handwritten amendments to the quote that changed the references to using Dulux products for the works to instead using a Rockcote product. Rockcote is a paint product that is similar to the Dulux products initially quoted.

The plaintiff made partial payments towards the contract price, but refused to pay $166,531.58 of the price, alleging that the defendant had not used the products required by the contract and that, in any event, the works were completed to an inadequate standard.

The plaintiff engaged an expert who concluded that the total area needed to be repaired or repainted and listed "poor opacity, application marks, uneven appearance, uneven paint finish and clearly noticeable patched repair areas" as the cause of the unacceptable results for the works. The plaintiff obtained a quote from a third party to repaint the building for $165,218.90.

The defendant also engaged an expert who concluded that there was only minor aesthetic variation in the works due to the natural characteristics of the building's walls. The defendant's expert concluded that the works had been completed in a

satisfactory manner.

The dispute proceeded to adjudication under the Security of Payment Act. The adjudicator found in favour of the defendant and held that plaintiff was liable to pay the defendant the balance of the contract price, interest and the total of the adjudication fees. The defendant filed the adjudication certificate in the New South Wales District Court and issued a statutory demand against the plaintiff for a total of $174,009.96, comprising $173,761.80 for the judgment debt, plus interest of $76.16 and filing fees of $172.

The plaintiff commenced proceedings against the defendant in the New South Wales District Court alleging the defendant had breached the contract by using Rockcote instead of Dulux products and that, regardless of the product used, the defendant had breached the contract by failing to complete the works adequately. The plaintiff claimed $350,000 in damages for the rectification costs of the allegedly defective work and the consequential losses allegedly suffered due to the delay in constructing the building.

The plaintiff also applied to New South Wales Supreme Court under ss. 459G and 459H of the Corporations Act to set aside the defendant's statutory demand.

(c) Decision

Section 459H(1) of the Corporations Act allows a company to apply for an order setting aside a statutory demand served on the company under s. 459G of the Corporations Act if the Court is satisfied of either or both of the following:

a. that there is a genuine dispute between the company and the respondent about the existence or amount of a debt to which the demand relates;
b. that the company has an offsetting claim.

Section 459H(2) requires the Court to calculate the substantiated amount of the demand by subtracting the "offsetting total" from the "admitted total".

Robb J acknowledged (at [88]) the "relatively low" threshold for establishing a genuine dispute or offsetting claim under s. 459H of the Corporations Act. His Honour also extensively considered the requirements for setting aside a statutory demand under the Corporations Act based on a debt created by the Security of Payment Act.

His Honour accepted (at [103]) that "so long as a statutory debt created by the Security of Payment Act exists, or a judgment issued under that Act remains in force, a company which is so indebted cannot genuinely dispute the existence of the debt for the purposes of s. 459H(1)(a) of the Corporations Act." Consequently, his Honour held (at [145]) that the Court should reject any of the plaintiff's arguments raised under s. 459H(1)(a) claiming there was a genuine dispute about the existence of the debt but held that the Court could recognise any offsetting claims for the purposes of s. 459H(1)(b) of the Corporations Act.

(i) Use of Rockcote in place of Dulux products

Robb J rejected the plaintiff's argument that the debt should be set aside because Rockcote was used in place of Dulux products. His Honour held that the plaintiff's argument on this point sought to dispute the existence of the underlying debt pursuant to s. 459H(1)(a) of the Corporations Act, which was not permissible.

His Honour (at [35]) also rejected the plaintiff's argument that the handwritten amendments to the quotation, which replaced the references to Dulux products with references to Rockcote, were an invalid attempt to vary the terms of the agreement. Instead, his Honour accepted the adjudicator's finding that the handwritten amendments were incorporated into the original agreement.

(ii) Quality of the works

Robb J held that the Court was not bound to uphold the adjudicator's original decision rejecting the offsetting claims made by the plaintiff. His Honour instead held (at [169]) that the plaintiff had a genuine offsetting claim against the defendant that "even if the contract specified the use of Rockcote for application to the walls of the Building, and even if that product was applied in accordance with specification, it was not fit for purpose because it was a high-gloss product applied to a substrate that would most likely lead to an unsightly and uneven finish."

His Honour then considered the application of s. 459H(2) of the Corporations Act to calculate the difference between the admitted total of the debt and the offsetting amount. For the purposes of assessing the offsetting total, his Honour accepted the plaintiff's expert opinion that the building would need to be repainted and used the replacement quote of $165,218.90 as the figure for the offsetting total. The District Court judgment debt amount of $173,761.80 was used as the admitted total under s. 459H(2) of the Corporations Act, leaving a difference between the two figures of $8,542.90.

Robb J ordered that the defendant's statutory demand be varied so that the amount of the demand was $8,542.90.

6.13 Applications against company in liquidation rejected

(By Lachlan Salt, Ashurst)

Lal v Singh [2015] NSWSC 1608, Supreme Court of New South Wales, Black J, 30 October 2015

(a) Summary

The Plaintiff brought an application to continue proceedings against a company in liquidation and an application for a stay on the winding up of that company. Both applications were unsuccessful.

(b) Facts

This judgment considered applications by the Plaintiff (Lal) for an order granting leave to proceed against the Second Defendant company, Eagle Investment Services Pty Ltd (the Company) under s. 417B of the Corporations Act 2001 (Cth) (the Act) and an order that the voluntary winding up of the Company be stayed under s. 472 of the Act.

The Company was incorporated on 18 February 2014 with the First Defendant (Singh) as its sole director and member. The parties agree that Lal was to be a silent partner and had some form of half interest in the Company.

Lal argued that in September 2014 an agreement was reached that Singh would resign from his position as director of the Company and transfer his shares in the Company to Lal's mother. Lal also said that under the September 2014 agreement Singh would appoint Lal's mother as the Company's sole director and that Lal would pay Singh $30,000. Lal contended that he paid two amounts totalling $10,000 to Singh in part performance of the September 2014 agreement - although the payment of these amounts predated the September 2014 agreement by almost two months.

On 2 February 2015 Singh and the Company gave an undertaking to the Court that, subject to the Court's further order, they would not sell or dispose of two Parramatta properties which the Company owned without giving Lal 21 days prior notice and further that they would continue to make payments on a hire purchase agreement which the Company had taken out on a Range Rover motor vehicle.

On 11 February 2015, the Company purported to agree to sell the office space. Lal successfully sought an injunction in respect of the sale. The agreement was later rescinded by Singh, the Company and the third party purchaser on terms that the Company pay $3,000 to cover the third party purchaser's losses and costs.

The Company was placed in voluntary liquidation by Singh on 29 May 2015.

Lal contended that various of the steps taken by Singh or the Company involved breaches of the orders by the Court. Lal also contended that various amounts would not have been payable to creditors if the September 2014 had been complied with. Singh disputed these positions.

(c) Decision

In respect of Lal's application under s. 417B of the Act for leave to continue proceedings against the Company, the parties agreed that the relevant order would in fact need to be made under s. 500(2) of the Act so far as the Company is in voluntary winding up. Section 500(2) provides that, except by leave of the Court and subject to its terms, no civil proceeding may be proceeded with or commenced against a company which has resolved to voluntarily wind up. Singh opposed the grant of leave for Lal to continue the proceedings against the Company.

Black J noted that Lal pleaded only a straightforward money claim against the Company; being that it together with Singh gave undertakings in the proceedings on 2 February 2015, that Singh and the Company breached those undertakings on or about 11 February 2015, and that Lal had suffered loss and damage.

Black J concluded that a breach of an undertaking given to the Court may be treated as a breach of contract which gives rise to a claim for damages, and further noted that it was a matter which could readily be proved in a liquidation and that there was no reason to think the liquidator could not properly determine a claim put on that basis. Black J also noted the right of Lal to bring, as well as the comparative simplicity and cost-effectiveness of bringing, an appeal against any decision of the liquidator under s. 1321 of the Act.

On the basis of the above, Black J determined that Lal should proceed by way of proof of debt and therefore refused to grant Lal's request for leave to continue to pursue the litigation against the Company.

In respect of Lal's application for a stay of the winding up of the Company, Black J noted and assumed, without deciding, Lal's contention that he had standing to bring the application because he (Lal) was a creditor of the Company.

However, Black J did not accept Lal's submission that Singh's placing of the Company into voluntary liquidation constituted a breach of the Court's orders made against Singh and the Company, on the basis that the appointment of the liquidator does not bring about any disposition of the Company's property. Further, Black J accepted the submission of counsel for Singh that any question raised by Lal about Singh's improper motive for putting the Company in liquidation would have done little to answer the fact of the Company's actual insolvency insofar as an application for a stay of the winding up was concerned.

Noting that the liquidator was on notice of the injunction preventing the Company from disposing of properties, the Company's actual state of insolvency, the lack of support for the stay application from other creditors, and the liquidator's actual opposition to the stay application, Black J rejected Lal's application to stay the winding up of the Company.

6.14 Confirmation that a director's entitlement to indemnification under a director's deed of indemnity can arise before proceedings actually commence

(By Rebecca Searle, King & Wood Mallesons)

Jeffries v Indigenous Land Corporation [2015] NSWSC 1616, Supreme Court of New South Wales, Rein J, 28 October 2015

(a) Summary

The NSW Supreme Court has affirmed that a director of a company can be entitled to indemnification under a deed of indemnity provided by the company in circumstances where an allegation has been made that the director has breached their duties, notwithstanding that actual proceedings have not been commenced against the director and the director may ultimately be liable to the Company if proceedings are commenced.

(b) Facts

The plaintiffs, William Jeffries and David Baffsky, were former directors of the defendant, Indigenous Land Corporation (ILC). In 2012, both the plaintiffs had entered into Deeds of Access, Indemnity and Insurance (the Deeds) with ILC under which ILC had agreed to indemnify the plaintiffs for certain costs incurred in their capacity as directors of ILC.

Relevantly, the Deeds provided that:

> ILC indemnifies the director. against any liability for legal costs incurred by the director. in defending an action for a liability incurred as a director of ILC, provided that the costs are not incurred in defending or resisting proceedings in which the director is found to have a liability to ILC for which he could not be indemnified under the deed.

On 27 February 2015, the plaintiffs received letters (the 27 February Letters) from ILC asserting that they had breached certain statutory and common law directors' duties of care and diligence owed to ILC, that ILC had suffered loss as a result of those breaches, and that the plaintiffs were liable for that loss (the Allegations). The plaintiffs claimed that they were each entitled to be indemnified by ILC under the Deeds for legal costs incurred in obtaining advice in respect of the Allegations.

Despite the Allegations, at the time of judgment ILC had neither commenced proceedings against the plaintiffs, nor notified the plaintiffs that it intended to commence proceedings. As such, ILC asserted that the plaintiffs were not entitled to benefit from the indemnity under the Deeds as the entitlement to be indemnified did not arise until:

i. such time as a Court adjudicated ICL's claims against the plaintiffs in favour of the plaintiffs; or
ii. the commencement of proceedings in respect of the Allegations.

(c) Decision

Rein J held that the plaintiffs were entitled to be indemnified by ICL under the Deeds for any legal costs incurred in defending the Allegations.

(i) Entitlement to be indemnified before a finding in favour of the directors in relation to the Allegations

Rein J held that the relevant clause in the Deeds did not operate only after there had been a hearing in relation to the Allegations in which the plaintiffs obtained a positive ruling. Rather, the plaintiffs were entitled to the indemnity until there was a finding against them in relation to the Allegations.

In reaching his decision, Rein J considered the application of s. 27M of the Commonwealth Authorities and Companies Act 1997 (Cth) (the CAC Act). That section provides that ICL must not indemnify a director against legal costs incurred by the director in defending proceedings brought by ICL, if there is a finding in those proceedings that the director is liable to ICL. The prohibition in s. 27M of the CAC Act is analogous with the prohibition in s. 199A of the Corporations Act 2001 (Cth).

In determining that the payment of funds by ICL to the plaintiffs prior to a finding in the plaintiffs favour in respect of the Allegations did not involve a breach of s. 27M of the CAC Act, Rein J had regard to the decisions in *Rickus v Motor Trades Association of Australia Superannuation Fund Pty Ltd* [2010] FCAFC 16 and *Note Printing Australia Ltd v Leckenby* [2015] VSCA 105. In particular, Rein J noted that for the prohibition in s. 27M of the CAC Act to "bite", there must be a finding against the plaintiffs in the very proceedings in respect of which legal costs are being claimed.

Rein J also rejected ICL's submission that allowing the plaintiffs to benefit from the indemnity in the circumstances would be uncommercial.

(ii) Entitlement to be indemnified prior to the commencement of proceedings in relation to the Allegations

Rein J then considered whether the plaintiffs had taken steps which led them to incur liability for legal costs in defending an action.

Rein J noted that, in his view, steps can be taken to defend a proposed action before it is commenced and that it must have been envisaged that a director who received the 27 February Letters would be likely to seek legal advice concerning a prospective defence to the proceedings that were foreshadowed. Rein J observed that once the 27 February Letters were received by the plaintiffs, he could see no good reason to limit the indemnity to legal costs incurred after foreshadowed proceedings had commenced.

7. Contributions

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