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1. Recent Corporate Law and Corporate Governance Developments

1.1 Professional standards for financial advisers to benefit consumers

17 October 2016 - The federal government has announced it will introduce legislation into the Parliament this year to mandate professional standards for financial advisers.

The reforms will include:

- "[c]ompulsory education requirements for both new and existing financial advisers;
- [s]upervision requirements for new advisers;
- [a] code of ethics for the industry;
- [a]n exam that will represent a common benchmark across the industry; and
- [a]n ongoing professional development component".

The new professional standards regime will commence on 1 January 2019. Existing advisers will have until 1 January 2021 to pass the new exam and until 1 January 2024 to reach degree-equivalent status.

The professional standards legislation will also establish an independent standards body, as a Commonwealth company, to govern the professional standing of the financial advice industry. The independent standards body's chairperson and directors will be appointed by the Minister. The cost of establishing the body will be met exclusively by the large banks and AMP.

Once the standards body is operational, the federal government will take steps to develop an ongoing industry funding model for the body. The federal government will work with stakeholders to ensure the ongoing funding model is developed and implemented as soon as practicable.

The body will be responsible for developing and setting the industry exam, developing the code of ethics, and determining the education and development requirements for both new and existing advisers.

A single, uniform code of ethics will set the ethical principles that advisers will operate under. Professional associations and other independent third party monitoring bodies will develop compliance schemes to monitor and enforce advisers' adherence to the Code. These compliance schemes will be approved by the Australian Securities and Investments Commission (ASIC).

1.2 Open competition in clearing and settlement of shares

12 October 2016 - The Council of Financial Regulators' (CFR) has released policy statements on the regulation of Australian cash equities clearing and settlement

services, a further step in the federal government's opening of competition in clearing of Australian cash equities.

The two CFR policy statements are:

- Regulatory Expectations for Conduct in Operating Cash Equity Clearing and Settlement Services in Australia; and
- Minimum Conditions for Safe and Effective Competition in Cash Equity Clearing in Australia.

The Regulatory Expectations apply to the Australian Securities Exchange Ltd's (ASX) engagement with, and provision of services to, users of its cash equity clearing and settlement services for which it is currently the sole provider. These expectations cover a range of matters relevant to governance, pricing and access.

ASX is expected to publicly commit to act in accordance with the CFR's Regulatory Expectations by releasing an updated *ASX Cash Equities Clearing and Settlement Code of Practice*.

The Minimum Conditions seek to provide potential applicants for clearing facility licences sufficient clarity on the measures that the regulators would consider necessary to support a licence application.

As part of this program of reform, the federal government will develop and consult on legislation to provide the relevant regulators with rule-making and arbitration powers, which would underpin both the Regulatory Expectations and the Minimum Conditions.

Recognising the place of ASX in a more competitive environment, the federal government will also amend ASX ownership restrictions in the Corporations Act 2001 No. 50 (Cth) to make them consistent with other financial sector companies, like banks and insurance companies. This will allow the ASX more flexibility in raising capital.

1.3 SEC announces enforcement results for FY 2016

11 October 2016 - The US Securities and Exchange Commission (SEC) has announced that, in the fiscal year 2016, it filed 868 enforcement actions exposing financial reporting-related misconduct by companies and their executives and misconduct by registrants and gatekeepers, as the agency continued to enhance its use of data to detect illegal conduct and expedite investigations.

The new single year high for SEC enforcement actions for the fiscal year that ended September 30 2016 included the most ever cases involving investment advisers or investment companies (160) and the most ever independent or standalone cases involving investment advisers or investment companies (98). The agency also had its most ever Foreign Corrupt Practices Act-related enforcement actions (21) and money distributed to whistleblowers (US$57 million) in a single year.

The agency also brought a record 548 standalone or independent enforcement actions and obtained judgments and orders totalling more than US$4 billion in disgorgement and penalties.

View Overview of SEC Enforcement in 2016.

1.4 Market manipulation of financial benchmarks

4 October 2016 - The federal government has announced it is strengthening financial regulation to better protect against the possible abuse and manipulation of financial benchmarks by banks.

The strengthened rules regulating the Bank Bill Swap Rate (BBSW), a key financial benchmark that serves as the reference rate for the pricing of a range of financial products, were recommended by the CFR and will ensure that past egregious conduct by the banks in manipulating benchmarks is prevented in the future.

ASIC is already pursuing three of the four major Australian banks over unconscionable conduct and market manipulation in setting the BBSW from 2010 to 2012.

The CFR's advice, which the federal government has released, broadly recommended that:

- administrators of significant (that is, systemically important) benchmarks be required to hold a new 'benchmark administration' licence issued by ASIC unless granted an exemption;
- ASIC be empowered to develop enforceable rules for the administrators of significant benchmarks and for entities that make submissions to such benchmarks (including the power to compel submissions to benchmarks in the case that other calculation mechanisms fail); and
- the manipulation of any financial benchmark (significant or non-significant) or financial product used to determine a financial benchmark used in Australia (such as Negotiable Certificates of Deposit), be made a specific criminal and civil offence. The federal government has accepted the CFR's recommendations and will work to implement these critical reforms over the next 18 months.

View CFR's advice to the Government.

1.5 Emerging market regulators seek to strengthen corporate governance

3 October 2016 - The Growth and Emerging Markets Committee of the International Organization of Securities Commissions (IOSCO) has made available Report on Corporate Governance in Emerging Markets, which seeks to strengthen corporate governance frameworks.

The Report identifies possible measures and regulatory approaches aimed at strengthening corporate governance in emerging market jurisdictions and aligning regulatory frameworks with internationally recognised standards in this area.

The Report focuses on three key areas, specifically:

- board composition and responsibility;
- remuneration and incentive structures; and
- risk management and internal controls.

The Report is based on a comprehensive survey across regulators, exchanges, listed companies, institutional investors and other stakeholders on corporate governance practices in emerging market jurisdictions.

The Report also identifies further initiatives and approaches for raising the bar regarding the implementation of best corporate governance practices, including encouraging greater board diversity and quality reporting of sustainability, social responsibility and cyber risks.

1.6 Guidelines on implicit support for securitisation transactions

3 October 2016 - The European Banking Authority has made available Final Guidelines on implicit support for securitisation transactions. The objective of the Guidelines is to clarify what constitutes arm's length conditions and to specify when a transaction is not structured to provide support for securitisations.

The Capital Requirements Regulation sets out restrictions on the provision of implicit support to securitisations, as this raises supervisory concerns and undermines the achievement of significant risk transfer. If originator or sponsor institutions fail to comply with the relevant requirements, they must, at a minimum, hold own funds against all of the securitised exposures as if such exposures had not been securitised.

The final Guidelines should be read in conjunction with the Guidelines on significant risk transfer.

1.7 Cross border M&A data

October 2016 - The International Institute for the Study of Cross-Border Investment and M & A has made available its quarterly review for the 2016 third quarter (Q3).

Key findings of the review include:

- global M&A volume in Q3 totaled approximately US$800 billion, approximately 10% lower than the second quarter (Q2), and over 10% higher than the first quarter (Q1);
- Q3 saw a number of major deals, including three of the four largest deals in 2016 - the Bayer/Monsanto, Enbridge/Spectra and SoftBank/ARM transactions - all of which were cross-border transactions;
- cross-border M&A activity accounted for 43% of global deal volume in Q3, up substantially from 31% in Q2. Four of the 10 largest deals in Q3 were cross-border transactions;
- European and Chinese M&A activity each accounted for just under 20% of Q3 deal volume, up slightly relative to Q2 and higher than overall levels from 2011-2015. Chinese outbound activity has slowed following unprecedented levels in Q1, as Chinese regulators appear to be increasing scrutiny of outbound investments; and
- deals involving US targets accounted for less than 40% of the quarter's deal volume, below the 50% (or greater) level that has recently prevailed.

1.8 IMF global financial stability report

October 2016 - The International Monetary Fund (IMF) has published its October 2016 Global Financial Stability Report and Executive summary.

The report finds that short-term risks to global financial stability have abated since April 2016, but that medium-term risks continue to build. Financial institutions in advanced economies face a number of cyclical and structural challenges and need to adapt to low growth and low interest rates, as well as to an evolving market and regulatory environment.

Weak profitability could erode banks' buffers over time and undermine their ability to support growth. A cyclical recovery will not resolve the problem of low profitability. More deep-rooted reforms and systemic management are needed, especially for European banks. The solvency of many life insurance companies and pension funds is threatened by a prolonged period of low interest rates. Corporate leverage in emerging market economies remains elevated in some countries, but the current favourable external environment presents an opportunity for overly indebted firms to restructure their balance sheets. The political climate is unsettled in many countries. A lack of income growth and a rise in inequality have opened the door for populist, inward-looking policies. These factors make it even harder to tackle legacy problems and further expose economies and markets to shocks.

A potent and more balanced policy mix is needed to deliver a stronger path for growth and financial stability, and avoid slipping into a state of financial and economic stagnation. The report also examines how the rise of nonbank financing has altered the impact of monetary policy and finds that fears of a decline in the effectiveness of monetary policy are unfounded. It appears that the transmission of monetary policy is, if anything, stronger in economies with larger nonbank financial sectors. Finally, the report examines the link between corporate governance, investor protection, and financial stability in emerging market economies. It finds that the improvements over the past two decades have helped bolster the resilience of their financial systems. These benefits strengthen the case for further reform.

1.9 Global competitiveness report

29 September 2016 - The World Economic Forum has made available its *Global Competitiveness Report 2016* which is an annual assessment of the factors driving productivity and prosperity in 138 countries. The degree to which economies are open to international trade in goods and services is directly linked to both economic growth and a nation's innovative potential. The trend, which is based on perception data from the *Global Competitiveness Index* (GCI)'s *Executive Opinion Survey*, is gradual and attributed mainly to a rise in non-tariff barriers although three other factors are also taken into account; burdensome customs procedures; rules affecting foreign direct investment and foreign ownership. It is most keenly felt in the high and upper middle income economies.

The report also sheds light on why quantitative easing and other monetary policy measures have been insufficient in reigniting long-term growth for the world's advanced economies. The report finds that interventions by economies with comparatively low GCI scores failed to generate the same effect as those performed in economies with high scores, suggesting that strong underlying competitiveness is a key requirement for successful monetary stimulus.

The report offers insight into how priorities may be shifting for nations in earlier stages of development. While basic drivers of competitiveness such as infrastructure, health, education and well-functioning markets will always be important, data in the GCI suggests that a nation's performance in terms of technological readiness, business sophistication and innovation is now as important in driving competitiveness and growth.

For the eighth consecutive year, Switzerland ranks as the most competitive economy in the world, narrowly ahead of Singapore and the United States. Following them is Netherlands and then Germany. The next two countries, Sweden (6) and the United Kingdom (7) both advance three places, with the latter's GCI score being based on pre-Brexit data. The remaining three economies in the top ten; Japan (8), Hong Kong SAR (9) and Finland (10) all move backwards.

View the full report, infographics, videos and more

1.10 ISS announces results of annual benchmark voting policy survey

29 September 2016 - Institutional Shareholder Services (ISS) has released the results of its annual global benchmark voting policy survey.

ISS received 439 total responses to this year's survey, of which 120 were from institutional investors, one-third of who each own or manage assets in excess of US$100 billion. ISS also received responses from 270 members of the corporate community (including companies, consultants/advisors to companies, and other trade organizations representing companies), with the remainder comprised of academics, non-profit organisations, and other governance stakeholders. Key findings from this year's survey include:

- **Multi-Class Structures at initial public offering (IPO) Companies (US):** Respondents were asked whether ISS should consider a policy approach which recommends votes against directors at companies that go public, or emerge from bankruptcy, with a capital structure that includes multiple classes of stock with unequal voting rights. A growing number of companies, especially high-tech firms, have adopted such structures in recent years in an attempt to alleviate short-term market pressures. Critics of these structures cite the potential for abuse and the extreme difficulty of abolishing such schemes once the company goes public given corporate insiders' voting control. Among investor respondents, 57% supported negative recommendations against such post-IPO board members, while 19% opposed them, and 24% opposed negative recommendations when sunset provisions would eliminate the unequal voting rights at some point in the future. Among non-investors, 46% opposed negative recommendations on directors altogether, while a majority either supported such recommendations (24%), or opposed such recommendations as long as the unequal voting rights are subject to sunset (31 %); and

- **Say-on-Pay Frequency (US):** In advance of 2017 say-on-pay frequency votes mandated by the SEC, respondents were asked whether they favored annual, biennial, or triennial votes, or whether the frequency should depend on the specific company. A large majority (66%) of investor respondents favored across-the-board annual say-on-pay votes. Eleven percent and 7% favored biennial and triennial votes, respectively. The remaining 17% of investors believe that the frequency should depend on company-specific factors, of which financial performance and the presence or absence of recent problematic pay practices were flagged by the greatest number of investors.

1.11 APRA releases consultation package on the Net Stable Funding Ratio

29 September 2016 - The Australian Prudential Regulation Authority (APRA) has made available a consultation paper setting out its response to issues raised in submissions on the *Discussion Paper Basel III liquidity - the Net Stable Funding Ratio (NSFR) and the liquid assets requirement for foreign Authorised Deposit-taking Institutions (ADI)* (March 2016 discussion paper). APRA is also releasing a draft revised *Prudential Standard APS 210 Liquidity (APS 210)* and *Prudential Practice Guide APG 210 Liquidity (APG 210)*, which incorporate the net stable funding ratio requirements for ADIs as well as a number of other changes as noted in the response paper.

APRA's current intention is that the NSFR will come into effect from 1 January 2018, in line with the internationally-agreed timetable.

View the Consultation Package.

1.12 EBA harmonises the definition of default across the EU

28 September 2016 - The European Banking Authority (EBA) has published its final report on guidelines specifying the application of the definition of default across the EU and its final draft Regulatory Technical Standards (the final draft RTS) on the materiality threshold of past due credit obligations.

The EBA also released the results of a quantitative and qualitative impact study (QIS) aimed at assessing the impact on the regulatory capital requirements of selected policy options to harmonise the definition of default used by European Union (EU) institutions. Both the guidelines and the final draft RTS will harmonise the definition of default across the EU, thus contributing to improving consistency and comparability of capital requirements.

In particular, the guidelines clarify all aspects related to the application of the definition of default including the days past due criterion for default identification, indications of unlikeliness to pay, conditions for the return to non-defaulted status, treatment of the definition of default in external data, application of the default definition in a banking group and specific aspects related to retail exposures.

1.13 SEC adopts rules for enhanced regulatory framework for securities clearing agencies

28 September 2016 - The SEC voted to adopt new rules to establish enhanced standards for the operation and governance of securities clearing agencies that are deemed systemically important or that are involved in complex transactions, such as security-based swaps. The SEC also voted to propose to apply the enhanced standards established by the new rules to other categories of securities clearing agencies, including all SEC-registered central counterparties.

The adopted rules apply to SEC-registered securities clearing agencies that have been designated as systemically important by the Financial Stability Oversight Council (FSOC) or that are involved in more complex transactions. Securities clearing agencies covered by the new rules will be subject to new requirements regarding, among other things, their financial risk management, governance, recovery planning, operations, and disclosures to market participants and the public.

View a related Fact Sheet.

1.14 Report on improving the global regulatory environment

28 September 2016 - The International Federation of Accountants and the Institute of Chartered Accountants in England and Wales have jointly made available From Crisis to Confidence: Good Regulation, Governance, and Culture, a report which examines how the global regulatory environment can be enhanced-with an

ultimate goal of improving confidence in the financial and capital markets, business, and government.

Other topics discussed in the report include:

- governance and culture: Why almost ten years after the global financial crisis, rebuilding public trust in financial and capital markets, business, and government remains a vital goal, despite the significant progress achieved from a regulatory perspective;
- regulatory fragmentation: How differences in cultures and expectations concerning regulation, and different legal environments, are leading to an increasingly fragmented international regulatory environment;
- complexity of regulation: Why it is important to achieve the right balance in the regulatory environment and how unnecessary complexity is sometimes created when we seek compliance-based regulatory solutions; and
- the future of regulation: How a holistic view that seeks to create a stronger system for today and tomorrow, rather than addressing past issues, is the right one for the global regulatory environment.

1.15 Financial inclusion: guidance on the regulation and supervision of institutions published by the Basel Committee

27 September 2016 - The Basel Committee on Banking Supervision (the Basel Committee) has issued final Guidance on the application of the Core Principles for Effective Banking Supervision to the regulation and supervision of institutions relevant to financial inclusion. The Basel Committee's Core Principles for Effective Banking Supervision are the de facto minimum standard for sound prudential regulation and supervision of banks and banking systems.

The Guidance identifies 19 of the total 29 Basel Core Principles where additional guidance is needed in the application of the Core Principles to the supervision of financial institutions engaged in serving the financially unserved and underserved. The Guidance also specifies the "Essential Criteria" and "Additional Criteria" associated with the Core Principles that have specific relevance to financial inclusion.

1.16 World Federation of Exchanges publishes cyber resilience principles

23 September 2016 - The World Federation of Exchanges (WFE), which represents more than 200 market infrastructure providers including exchanges and

central counterparties, has made available a set of principles, which relate to cyber resilience and seek to support and complement guidance already provided by global regulators.

The principles have been drafted in consultation with WFE members, following the publication of Committee on Payments and Market Infrastructures (CPMI)-IOSCO's *Guidance on Cyber Resilience for Financial Market Infrastructures* (June 2016). The CPMI-IOSCO's guidance was designed to elaborate further on the main areas of its Principles for Financial Market Infrastructure (FMI) that are relevant for cyber security.

The principles include:

- in developing and implementing local FMI standards and initiatives, existing global cyber security standards should be used as an initial framework, to ensure consistency of approach and operational convention. Any FMI standards should be flexible enough to accommodate differences in regional and national legal and regulatory frameworks; and
- cyber resilience frameworks should be balanced enough to enable continued technology innovation and development of markets and services while still remaining suitably robust to ensure markets are safe.

1.17 Guidance about minute taking

19 September 2016 - The United Kingdom (UK) Governance Institute has issued new guidance about minute taking .

The guidance, highlights the following key points:

- the purpose of minutes is to provide an accurate, impartial and balanced internal record of the business transacted at a meeting;
- there is no 'one-size fits all' approach for minute writing and no 'right way' to draft minutes. Context is always important and each chair and each board will have their own preference for minuting style. It is up to each individual organisation to decide how best its meetings should be recorded;
- the degree of detail recorded will depend to a large extent on the needs of the organisation, the sector in which it operates, the requirements of any regulator and the working practices of the chairman, the board and the company secretary. As a minimum, minutes should include the key points of discussion, decisions made and, where appropriate, the reasons for them and agreed actions, including a record of any delegated authority to act on behalf of the company;
- minutes should be clear, concise and free from any ambiguity as they will serve as a source of contemporaneous evidence in any judicial or regulatory proceedings;

- minutes should facilitate regulatory oversight, but this is not their primary purpose. Nonetheless, those drafting minutes should be mindful of regulatory needs. The well-written minutes of an effective board meeting should convey all the assurance that a regulator needs;
- minutes should not be a verbatim record of the meeting;
- minutes should document the reasons for a decision and include sufficient background information for future reference;
- individual contributions should not normally be attributed by name, but this will be appropriate in some cases;
- draft minutes should be clearly marked as such and amendments to the draft minutes should be thought of as 'enhancements' rather than 'corrections'; and
- the audio recording of board meetings or the publication of board minutes is not, generally, recommended. Any such recording should be deleted once the minutes have been approved.

1.18 Bank for International Settlements market review

18 September 2016 -The latest issue of the Bank for International Settlements (BIS) Quarterly:

- shows that year-on-year growth of US dollar bank loans to borrowers outside the United States turned negative in the first quarter of 2016 for the first time since 2009, the time of the financial crisis;
- explores the UK's role as a hub for international banking. Cross-border borrowing and lending by banks located in the UK, or UK branches of foreign banks, are notably larger-scale than the cross-border business of banks with headquarters in the UK;
- documents the trend of non-financial companies issuing debt in euros rather than US dollars as they take advantage of lower borrowing costs and the European Central Bank's asset purchases. Euro-denominated bonds are accounting for an increasing share of net issuance in international debt securities, including for US and emerging market borrowers.
- discusses the strong growth of over-the-counter markets in derivatives trading, drawing on the recent BIS *Triennial Survey of Foreign Exchange and Derivatives Markets Activity*.

The review also examines developments in currency and bond markets.

1.19 Implications of climate change for investors: report

September 2016 - Blackrock Investment Institute has made available Adapting portfolios to climate change: Implications and strategies for all investors, a report which details how investors can mitigate climate risks and exploit opportunities, and notes that climate-aware investing is possible without compromising on traditional goals of maximising investment returns.

The report examines:

- how climate change presents market risks and opportunities through four channels, specifically:
  - physical: more frequent and severe weather events over the long term;
  - technological: advances in energy storage, electric vehicles or energy efficiency undermining existing business models;
  - regulatory: tightening emissions and energy efficiency standards, and changing subsidies and taxes; and
  - social: changing consumer preferences and pressure groups advocating divestment of fossil fuel assets; and
- how all asset owners can, and should, take advantage of a growing array of climate related investment tools and strategies to manage risk, to seek excess returns or improve their market exposure. The report explains how investors can gradually implement climate considerations into their portfolios.

1.20 Latest Centre for Corporate Law and Securities Regulation research papers

(a) Enforcement of Financial Market Manipulation Laws: An International Comparison of Sanctions (By Leo Bromberg, George Gilligan and Ian Ramsay)

Market manipulation has been a significant focus of regulators, the media and others in many countries, with widespread allegations of market manipulation, not just relating to securities, but in relation to interest rates, foreign exchange and commodities. This working paper presents the results of a detailed comparative empirical study of sanctions imposed for trade-based market manipulation in Australia, Canada (Ontario), Hong Kong, Singapore and the UK. The comparative study is based on a dataset of around 250 sanctions imposed on individuals and companies found or alleged to have contravened market manipulation provisions across the jurisdictions. The study compares the type, magnitude and frequency of sanctions (custodial sentences, banning orders and various pecuniary sanctions) imposed by statutory bodies and the courts for market manipulation in the selected jurisdictions in the ten year period from 1 January 2006 to 31 December 2015. The study also examines pecuniary sanctions imposed relative to illegal profits obtained by the defendants. Key findings include substantial differences between the jurisdictions in the use of sanctions, with much higher use of custodial sentences in Hong Kong, Singapore and Australia, much higher use of banning orders in Ontario and the UK's imposition of the highest median pecuniary sanctions.

(b) Has the Introduction of Civil Penalties Increased the Speed and Success Rate of Directors' Duties Cases? (By Jasper Hedges and Ian Ramsay)

Has the introduction of the civil penalty regime into Australian corporate law increased the speed and success rate of directors' duties cases? This question has been the subject of much commentary but, surprisingly, no empirical research. A number of commentators argue that the civil penalty regime should have increased the speed and success rate of litigation brought by regulators. ASIC disagrees. In this research note, the authors present the results of the first empirical study aimed at answering this question. The civil penalty regime allows ASIC to bring civil proceedings for contraventions of the key directors' duties provisions of the Corporations Act 2001 No. 50 (Cth) based on a standard of proof lower than the criminal standard. The civil penalty regime also allows courts to impose a wider range of sanctions or remedies where a breach of duty is established. These sanctions are a pecuniary penalty, a compensation order or an order disqualifying the defendant from managing companies for a specified period of time. One of the policy considerations underpinning the introduction of the civil penalty regime is that it would reduce the time taken to complete enforcement action in the courts and also increase the success rate of litigation brought by the regulator. These consequences would result from the comparatively liberal civil rules of evidence and procedure. The authors researched all directors' duties cases brought by either ASIC or the Commonwealth Director of Public Prosecutions for the ten year period from 1 January 2005 to 31 December 2014. The research finds that, contrary to a widespread perception that civil proceedings are more successful for the regulator and quicker as a result of more lenient rules of evidence and procedure, there was only a relatively small difference between the success rates and duration of civil and criminal enforcement during the ten year study period.

(c) The Who, Why and What of Enforceable Undertakings Accepted by the Australian Securities and Investments Commission (By Helen Bird, George Gilligan and Ian Ramsay)

This article examines the deployment of enforceable undertakings by ASIC. Enforceable undertakings are formal settlement agreements between a regulator and regulated parties to resolve issues of non-compliance with laws administered by the regulator. This article analyses the circumstances and context under which 414 enforceable undertakings were accepted by ASIC from 1 July 1998 until 31 December 2015 (17.5 years).

The article addresses three fundamental questions:

- who are the regulated parties that gave enforceable undertakings?;

- why did they give them?; and
- what fundamental promises or obligations did their agreements contain?

The study shows that ASIC utilises enforceable undertakings to remove law-breaking individuals from an industry and to promote legal and regulatory compliance on a systemic basis within individual firms and more broadly, especially within the financial planning and wealth management sector.

(d) The Australian Sports Commission's Governance Reform in Sport Discussion Paper and Voting Rules in Corporate Constitutions (By Robert Macdonald and Ian Ramsay)

The Australian Sports Commission's 2015 Governance Reform in Sport Discussion Paper proposes to limit voting by members of a National Sporting Organisation to essentially the minimal set of issues required by the Corporations Act 2001 No. 50 (Cth), and to further mandate the voting rule to be adopted for each issue.

The authors critique the Discussion Paper and argue that three issues require discussion, specifically:

- deciding which voting rules to implement - the efficiency of the proposed voting rules;
- the efficiency of mandatory rules in corporate governance regulation; and
- the balance of power between members and directors.

The authors argue that constitutional voting rules ought to minimise the sum of the decision-making costs and the external costs of the issue to be determined. These two costs of voting depend upon the nature of the issue itself and crucially, upon the identity, the number and the preference heterogeneity of the voting members. There is no *ex ante* reason to assume that a simple majority or any other mandatory voting rule is optimal.

(e) Illegal Phoenix Activity: Quantifying Its Incidence and Cost (By Helen Anderson, Ian Ramsay and Michelle Welsh)

Phoenix activity centres on the idea of a new company arising from the ashes of its failed predecessor. Typically, the individuals in control of the failed company transfer the business to the new company while its debts remain the responsibility of the failed company. The activity becomes illegal where the intention of the company's controllers is to use the company's failure as a device to avoid paying the failed company's creditors (who may include the company's employees and revenue authorities) that which they otherwise would have received had the company's assets been properly dealt with. Illegal phoenix activity has become a matter of increasing concern in recent years. Many parties are interested in understanding the size of the problem, how much it costs the economy, and how well current enforcement mechanisms work. These are important questions because they influence the allocation of government resources and the process of law reform. To answer the quantification questions, the authors gathered all the available data on the incidence and cost of illegal phoenix activity, as well as the enforcement of the various laws that can be utilised to combat it. However, despite the large amounts of information obtained, it was not possible to provide a definitive answer to the quantification questions. Moreover, accurate quantification is highly problematic. This article, which is based on a much longer research report, presents the authors' key findings and explores the difficulties with quantification.

(f) From Enforcement to Prevention: International Cooperation and Financial Benchmark Reform (By Andre Dao, Andrew Godwin and Ian Ramsay)

The London Interbank Offered Rate and Forex scandals have shaken public trust in the global financial system. Despite the global nature of the scandals, the role of international cooperation in preventing financial benchmark manipulation has been surprisingly overlooked. Benchmark reform has tended to focus on structural changes to benchmark administration and regulation, with a particular emphasis on benchmark quality, methodology and governance. Where international cooperation has occurred, it has tended to operate ex post, in facilitating cross-border investigations after crises have already been revealed. Where *ex ante* cooperation has occurred, it has taken the form of high-level standard-setting. It is clear that further cooperation is needed to prevent misconduct rather than to merely punish it. This article addresses the question of international cooperation in the financial benchmark context and concludes that cooperative tools such as *ad hoc* discussions, supervisory colleges, equivalence measures and regulatory networks have the potential to bridge the preventative gap in this regard.

2. Recent ASIC Developments

2.1 Remake of 'sunsetting' class order on rights issue notifications and repeals 'sunsetting' class order on money market deposits

18 October 2016 - ASIC has made a new legislative instrument to replace *Class Order [CO 02/225] Rights issue notifications*, which was due to expire ('sunset') on 1 April 2017.

The new legislative instrument is ASIC Corporations (Renounceable Rights Issue Notifications) Instrument 2016/993. The instrument has substantially the same effect as *[CO 02/225]*. It provides relief from certain sections of Chapter 6D and Part 7.9 of the Corporations Act 2001 No. 50 (Cth) to facilitate the renunciation and transfer of rights issued under a renounceable rights offer.

ASIC has also repealed *Class Order [CO 00/231] Money market deposits*, which was due to sunset on 1 April 2017.

Class Order [CO 00/231] was repealed as the relief provided by the class order is no longer necessary in light of other provisions of the Corporations Act 2001 No. 50 (Cth) and any residual need for relief is more appropriately given on a case by case basis by application.

ASIC has made available the following related documents:

- ASIC Corporations (Repeal) Instrument 2016/1005;
- ASIC Corporations (Repeal) Instrument 2016/994;
- Consultation Paper 261 (CP 261); and
- Non-confidential submission to CP 261.

2.2 Consultation on four 'sunsetting' class orders on registered managed investment schemes

14 October 2016 - ASIC has made available Consultation Paper 270 Remaking ASIC class orders on registered schemes (CP 270), which proposes to remake four class orders on registered schemes, which are due to expire ('sunset') between 1 October 2017 and April 2018, specifically:

- *Class Order [CO 98/50] Incorporating parts of other compliance plans*;
- *Class Order [CO 98/60] Protecting class rights in a managed investment scheme*;
- *Class Order [CO 98/1806] Related bodies corporate and external members of compliance committee*; and
- *Class Order [CO 98/1808] Allowing constitutions to use Appendix 15A of the ASX Listing Rules*.

CP 270 also outlines ASIC's rationale for proposing to remake the class orders.

ASIC considers that these class orders 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 class orders have not changed.

ASIC proposes to remake the relief under these class orders in a single legislative instrument so that the substantive effect of each class order is continued beyond its expiration date.

The new instrument will continue the relief currently given by the class orders without significant changes, so that the ongoing effect will be preserved without any disruption to the entities that rely on them.

In relation to *Class Order [CO 98/1808]*, it is also proposed that the relief be extended to apply in relation to the listing rules of the Sydney Securities Exchange and may in the future apply in relation to the listing rules of other financial markets that require or allow for the constitution of a registered scheme to contain provisions similar in effect to those in Appendix 15A of the *ASX Listing Rules*.

2.3 Clarification of guidance for forward-looking statements in the mining and resources industry

12 October 2016 - ASIC has re-issued an updated Information Sheet 214 Mining and resources: Forward-looking statements (INFO 214), on statements relating to future matters commonly made in the mining and resources industry.

ASIC's goal is to draw together and better explain the existing rules on the disclosure of statements relating to future matters commonly made in the mining and resources industry, i.e., production targets and forecast financial information based on production targets.

Revised INFO 214 incorporates some minor drafting changes to clarify its guidance. The changes have been made in response to concerns and misunderstandings that arose at the time of INFO 214's original release in April 2016.

ASIC believes the revised guidance now provides companies with sufficient guidance and information to enable them to fully comply with their legal requirements.

The matters clarified in revised INFO 214 comprise:

- forward looking statements have always under law been required to be based on reasonable grounds, and INFO 214 does not change this position;
- production targets and forecast financial information can be published even if secured funding is not in place - but a company still needs to be able to demonstrate 'reasonable grounds' that it could obtain the requisite project finance as and when required;
- production targets and forecast financial information can be published based not only on ore reserves but also on mineral resource estimates - provided they have 'reasonable grounds' for that estimated mineralisation, and each of the *Joint Ore Reserves Committee Code* modifying factors; and
- a company that does not have reasonable grounds for forward-looking statements and therefore cannot make statements of this kind should still disclose reliable and relevant information of a technical nature (for example, from scoping studies) to ensure the market is properly informed of the company's prospects.

2.4 Consultation on 'sunsetting' class order about managed investment scheme buy-backs and updates to related guidance

12 October 2016 - ASIC has made available Consultation Paper 269 Remaking ASIC class order on managed investment scheme buy-backs and updating related guidance (CP 269), which proposes to remake its class order on managed investment scheme buy-backs, currently due to expire ('sunset') on 1 April 2018, and proposed changes to platforms policy.

CP 269 also outlines ASIC's rationale for proposing to remake the instrument and provides details of the updated regulatory guidance.

ASIC proposes to remake the class order with minor changes. In ASIC's view, the class order in general is operating effectively and efficiently and an amended version of the class order would continue to form a necessary and useful part of the legislative framework. The fundamental policy principles that underpin the class order have not changed.

The new instrument would continue the relief currently given by [CO 07/422] On-market buy-backs by ASX-listed schemes without significant changes, so that the ongoing effect will be preserved without any disruption to the entities that rely on it.

However, ASIC is proposing to:

- expand the relief to cover an ASX-listed scheme that has more than one class of interest; and
- simplify requirements where a responsible entity or its nominee exercises a discretion.

ASIC also seeks feedback on its proposed updates to the guidance on managed investment scheme buy-backs.

2.5 Industry review of life insurance claims

12 October 2016 - ASIC has made available Report 498: Life insurance claims review, a review of the life insurance sector's handling of claims. The review found that, while life insurers are paying the considerable majority of claims, there are significant shortcomings in a number of areas of life insurance claims handling, and there is a clear need for public reporting on life insurance claims outcomes - at an industry and individual insurer level.

ASIC's review examined 15 insurers covering more than 90% of the market. The six-month review analysed three years' of data on the four major life insurance policy types - term life cover, total and permanent disablement (TPD), trauma, and income protection. ASIC worked closely with APRA during the review (further information).

ASIC sought to identify whether there were systemic issues across the industry, as well as concerns relating to particular products or firms. The review also assessed whether industry data indicated the need for further, more targeted surveillance work.

ASIC found that approximately 90% of claims are paid in the first instance with around $8.2 billion in net policy payments made in the year ending 30 June 2016.

While not finding evidence of cross-industry misconduct, ASIC's review identified issues of concern in relation to higher claims denial rates and claims handling procedures associated with:

- particular types of policies: The rates of declined claims were highest for total and permanent disability (TPD) cover (average declined claim rate of 16%) and trauma cover (average declined claim rate of 14%);
- a considerable variation in declined claims among insurers, with TPD denial rates being as high as 37% and trauma (up to 25%) for some types of cover; and
- the most common types of life insurance disputes were about the evidence insurers require when assessing claims (including surveillance), and delays in claims handling.

ASIC's review also found that there were higher claims denial rates in relation to insurance policies sold direct to consumers with no financial advice (compared to policies sold through advisers and group insurance policies).

ASIC also made available the following related documents:

- Update on ASIC's investigation into CommInsure;
- Infographic - ASIC's work so far; and
- Infographic - A snapshot of ASIC's review.

2.6 Remake and repeal of 'sunsetting' class orders on markets and securities

5 October 2016 - Following public consultation, ASIC has remade ten legislative instruments and repealed three that are due to expire ('sunset') in 2016 and 2017.

ASIC has remade these instruments before they sunset. The new instruments will continue the substantive effects of the previous instruments with some minor amendments, which include simplifying the drafting to give greater clarity.

The following instruments have been remade:

- *Class Order [CO 01/1519] Disclosure of directors' interests* has been remade into ASIC Corporations (Disclosure of Directors' Interests) Instrument 2016/881;
- *Class Order [CO 02/313] Part 7.11: Transfers of securities under Division 3* has been remade into ASIC Corporations (Transfers of Division 3 Securities) Instrument 2016/893;
- *Class Order [CO 02/608] Warrants: Relief from PDS requirements for secondary sales* and *Class Order [CO 03/957] ASX managed investment warrants: Disclosure and reporting exemptions* have been remade and consolidated into ASIC Corporations (Exchange-Traded Warrants) Instrument 2016/886;
- *Corporations (Low Volume Financial Markets) Exemption Notice 2003* has been remade into ASIC Corporations (Low Volume Financial Markets) Instrument 2016/888;
- *Class Order [CO 03/826] Market related records: Australian financial service licensees dealing on overseas markets* has been remade into ASIC Corporations (Records: Dealings on Foreign Markets) Instrument 2016/889;
- *Class Order [CO 03/911] Licensing relief for self-dealers who provide general product advice about own securities* has been remade into ASIC Corporations (Amendment and Repeal) Instrument 2016/895;
- *Class Order [CO 06/682] Multiple derivative issuers* has been remade into ASIC Corporations (Exchange-Traded Derivatives: Multiple Issuers) Instrument 2016/883;
- *Class Order [CO 07/183] Transfer of Australian securities traded in New Zealand* has been remade into ASIC Corporations (Securities: NZ FASTER System) Instrument 2016/891; and
- *Class Order [CO 02/281] Dematerialised securities traded on Austraclear* has been remade into ASIC Corporations (Dematerialised Securities: Austraclear) Instrument 2016/841.

ASIC has, however, varied the application of the *Corporations (Low Volume Financial Markets) Exemption Notice 2003* by increasing the transaction threshold of low volume financial markets and amending the transaction period to which the transaction threshold applies.

ASIC has also amended the application of *[CO 01/1519]*, such that it no longer imposes certain conditions on the relief.

ASIC has repealed the following class orders, having formed the view that this relief is no longer required:

- *Class Order [CO 02/284] CHESS-approved foreign securities*;

- *Class Order [CO 00/2449] ASX Online-relief from paper lodgement*; and
- *Class Order [CO 02/1296] ASX managed investment warrants-FSR Act transition*.

2.7 Remake of instruments that affect financial reporting

30 September 2016 - Following public consultation, ASIC has remade three legislative instruments that affect financial reporting by companies.

The relief is set out in the following new legislative instruments:

- ASIC Corporations (Audit Relief) Instrument 2016/784 (replaces *Class Order 98/1417*)
- ASIC Corporations (Wholly owned Companies) Instrument 2016/785 (replaces *Class Order 98/1418*)
- ASIC Corporations (Qualified Accountant) Instrument 2016/786 (replaces *Class Order 01/1256*).

ASIC remade these instruments without significant changes before they were due to sunset under the Legislation Act 2003 No. 139 (Cth).

ASIC has released updated versions of the following documents related to audit relief for certain proprietary companies:

- Regulatory Guide 115 Audit relief for proprietary companies; and
- Pro Forma 183 Deed of subordination.

ASIC has also released updated versions of the following documents related to relief for certain wholly owned companies:

- Pro Formas 24 Deed of cross guarantee, PF 25 Notice of disposal, PF 26 Revocation deed, and PF 27 Assumption deed; and
- Information Sheet 24 Deeds of cross-guarantee.

In addition, *Class Orders [CO 98/106] Financial reports of superannuation funds, approved deposit funds and pooled superannuation trusts* and *[CO 99/1225] Financial reporting requirements for benefit fund friendly societies* have been repealed as they are no longer necessary or useful, while *[CO 99/1225]* ceased to be operative more than ten years ago.

2.8 Remake of 'sunsetting' class order about managed discretionary accounts

29 September 2016 - ASIC has made available Regulatory Guide 179 Managed Discretionary Accounts (RG 179), an updated guide on its relief for Managed Discretionary Accounts (MDAs).

ASIC has also made new legislative instrument ASIC Corporations (Managed Discretionary Accounts) Instrument 2016/968 to replace its class order on MDAs that was due to expire ('sunset') on 1 October 2016. This instrument continues the relief from the provisions in the Corporations Act 2001 No. 50 (Cth) that would apply to the provider of a MDA with some changes.

The instrument and RG 179:

- incorporate relief for MDAs operated on a regulated platform and MDAs provided to family members, with some changes from relief under the previous no-action positions;
- implement new requirements to ensure MDA investors are adequately informed when the MDA provider has a discretion to invest in products where recourse is not limited (for example, contracts for difference);
- require specific upfront disclosure about:
    - terminating the MDA contract;□@
    - fees charged within the MDA; and
    - outsourcing arrangements, where the MDA provider outsources significant functions of the MDA; and
- provide greater certainty on the scope and application of the MDA relief and about ASIC's expectations for managing conflicts of interest.

MDA providers currently offering MDAs under ASIC's regulated platform no-action letter must comply with the new regulatory requirements by 1 October 2018 including the new requirement to obtain an MDA specific dealing by issue licence authorisation. Other existing MDA providers must comply with the revised requirements from 1 October 2017.

2.9 Remake of class orders relating to property, strata and management rights schemes

29 September 2016 - Following public consultation, ASIC has continued the relief available to operators, promoters and developers of strata schemes and management rights schemes from certain managed investment, licensing, hawking and disclosure provisions.

ASIC has also continued the relief available to real estate agents who are engaged by investors to let out their strata unit for residential or commercial purposes but not as part of a serviced strata arrangement.

The property, strata and management rights schemes class orders have been remade without significant changes so that their ongoing effect will be preserved without any disruption to those who rely on them.

All seven Class Orders below have been combined into a single instrument, ASIC Corporations (Serviced Strata and Like Schemes) Instrument 2016/869, so that the substantive effect of the relief in each Class Order is continued beyond the expiration date in a new instrument:

- *ASIC Class Order [CO 99/463] Serviced strata schemes valuations*, which is due to sunset on 1 April 2018;
- *ASIC Class Order [CO 02/185] Sale of strata units for $500,000 or more*, which is due to sunset on 1 April 2018;
- *ASIC Class Order [CO 02/245] Closed schemes*, which gives relief to operators of serviced strata schemes that are 'closed schemes' as at 6 October 1998 which is due to sunset on 1 April 2017;
- *ASIC Class Order [CO 02/303] Management rights schemes - amendment*, which is due to sunset on 1 October 2017;
- *ASIC Class Order [CO 02/304] Management rights schemes*, which is due to sunset on 1 October 2016;
- *ASIC Class Order [CO 02/305] Management rights schemes*, which is due to sunset on 1 October 2016; and
- *ASIC Class Order [CO 07/189] Management rights schemes where the strata unit cannot be used as a residence*, which is due to sunset on 1 October 2017.

ASIC is currently updating the guidance in *Regulatory Guide 140: Serviced strata schemes* to reflect the new instrument.

ASIC has also continued the relief available to real estate agents who are engaged by investors to let out their strata unit for residential or commercial purposes but not as part of a serviced strata arrangement.

The relief applies as set out in the new legislative instrument ASIC Corporations (Property Rental Schemes) Instrument 2016/870.

The new instrument replaces *Class Order [CO 02/182] Real property rental schemes*. ASIC remade this instrument without significant changes. It continues the relief given to real estate agents where their ordinary business in leasing or managing property does not involve a managed investment scheme where, for example, the owner of the property has the day to day control of the property through being able to give directions to their agent.

2.10 Update of regulatory framework for charitable investment fundraisers

28 September 2016 - ASIC has issued a revised policy and regulatory framework for charities that raise investment funds. The framework removes regulatory barriers to the issue of financial products while strengthening protection for public investors.

The changes follow an ASIC review of the operation of exemptions available to charities from certain managed investment, debenture, fundraising and licensing provisions of the Corporations Act 2001 No. 50 (Cth). The changes are aimed at ensuring the policy is consistent with ASIC's objectives of confident and informed investors and fair and efficient markets.

The review had identified difficulties in liquidity management by fundraisers and the effectiveness of their disclosure.

Following extensive consultation under Consultation Paper 207 Charitable investment fundraisers and further consultation with industry stakeholders, ASIC has made a number of updates, including that:

- from 1 January 2017, charitable investment fundraisers will not be permitted to issue at-call or investments with a term of less than 31 days to retail investors; and
- from 1 January 2018, charitable investment fundraisers that wish to issue investments to retail investors who are not associated with the charity will no longer be exempted from the requirement to hold an Australian financial services (AFS) licence from ASIC.

Further, additional restrictions apply that are designed to avoid the investments being used for transactional facilities.

In addition, ASIC has applied disclosure, lodgment, breach reporting and financial reporting requirements although these requirements are less stringent than the equivalent provisions in the Corporations Act 2001 No. 50 (Cth) that apply to regulated entities.

The changes announced today are effected by repealing existing class order *CO 02/184 Charitable investment schemes- fundraising* and replacing it with ASIC Corporations (Charitable Investment Fundraising) Instrument 2016/813 and issuing a new version of Regulatory Guide 87: Charitable investment fundraising and school enrolment deposits.

The existing class order, *CO 02/151 School enrolment deposits*, has also been repealed and replaced with ASIC Corporations (School Enrolment Deposits) Instrument 2016/812 without substantive amendment. This will continue to permit schools accepting enrolment deposits to do so without the requirement to comply with the relevant provisions of the Corporations Act 2001 No. 50 (Cth).

ASIC has also made available the following related documents:

- Non-confidential submissions to CP 207;
- Report 495: Response to submissions on CP 207 Charitable investment fundraisers;
- ASIC Corporations Repeal instrument 2016/810 in respect of existing *Class Order [CO 02/184]*;
- ASIC Corporations (Charitable Investment Fundraising) Instrument 2016/813 and related *Explanatory Statement*; and
- ASIC Corporations Repeal instrument 2016/819 in respect of existing *Class Order [C0 02/151]*.

2.11 Extension of foreign financial service provider class orders for two years and consults on related class order

28 September 2016 - ASIC has extended, for two years, seven class orders giving relief to foreign financial service providers (FFSPs) providing financial services to wholesale clients. These class orders were due to expire ('sunset') between 1 October 2016 and 1 April 2017.

ASIC has also made available Consultation Paper 268 Licensing relief for foreign financial services providers with limited connection to Australia (CP 268), which outlines a proposal to repeal a related class order for foreign entities with a limited connection to Australia providing services to wholesale clients. This class order is due to sunset on 1 April 2017.

Extension of relief for FFSPs:

- ASIC has extended for two years its relief from the requirement to hold an AFS licence when providing financial services to Australian wholesale clients (see ASIC Corporations (Repeal and Transitional) Instrument 2016/396); and
- ASIC has extended this relief for two years so that ASIC can comprehensively review and consult on the policy settings underlying relief for FFSPs. This extension and review comes as a result of market and regulatory developments since the relief was first granted and a number of ongoing international and domestic reviews. CP 268 outlines further the rationale for this review.

Effect of instrument extending relief:

- *ASIC Corporations (Repeal and Transitional) Instrument 2016/396* continues ASIC's previous relief for FFSPs in the same form with an amended information gathering power. This amendment clarifies that ASIC may request information from an FFSP about the operation of its financial services business. ASIC will consult publicly before 1 October 2018 on its relief in this area; and
- ASIC proposes to repeal [CO 03/824] Licensing relief for financial services providers with limited connection to Australia dealing with wholesale clients ([CO 03/824]). ASIC is seeking feedback on whether the relief provided by the class order is no longer necessary in light of other provisions introduced to the Corporations Act 2001 No. 50 (Cth) since [CO 03/824] was made. If there is any residual need for licensing relief ASIC would consider these on a case by case basis.

3. Recent ASX Developments

3.1 Rule amendments: Expansion of OTC product coverage

ASX has issued a notice, advising that it has made several miscellaneous amendments to the over-the-counter (OTC) Handbook, effective 3 October 2016, including:

- Addition of a new condition for acceptance of OTC Transactions for registration (OTC Handbook 4.5(b)(i); and
- Confirmation that OTC Intraday Margin must be met by an OTC Participant within one hour of ASX making a call or such other period of time as notified by ASX (OTC Handbook 5.6).

3.2 Consultation paper: ASX's replacement of CHESS for equity post-trade services: Business requirements

ASX has made available a consultation paper, which outlines its plans for the replacement of the system that underpins the post-trade processes of Australia's cash equity market, known as the Clearing House Electronic Subregister System (CHESS). The purpose of this consultation is to seek the views of stakeholders on their requirements for the system to replace CHESS.

3.3 Consultation paper: Austraclear - New framework to facilitate compliance with the Common Reporting Standard

ASX has made available a consultation paper, which seeks participant views on the proposed amendments to the Austraclear Regulations in line with the Common Reporting Standard (CRS). The Common Reporting Standard (CRS) is a new global standard for the collection, reporting and exchange of financial account information of foreign tax residents, to combat tax evasion.

3.4 Reports

On 6 October ASX released the ASX Monthly Activity Report for September 2016.

4. Recent Takeovers Panel Developments

4.1 Regal Resources Limited - Declaration of unacceptable circumstances and orders

17 October 2016 - The Takeovers Panel (the Panel) has made a declaration of unacceptable circumstances (Annexure A) and final orders (Annexure B) in relation to an application dated 22 September 2016 by Mr Warwick Sauer in relation to the affairs of Regal Resources Ltd (Regal).

On 30 June 2016, Regal shareholders approved a series of resolutions, including for the purposes of item 7 of s. 611 which (among other things) would increase the voting power of Ndovu Capital VI B.V. (Ndovo) in Regal from 13.23% to between 54.38% and 68.03% through the issue of Regal shares under a placement, conversion of a convertible loan and underwriting of a proposed entitlement offer.

The notice of meeting in respect of the resolutions indicated that Regal shareholders would be provided with the option to subscribe for shortfall shares in excess of their entitlement under the entitlement offer, on the terms and conditions disclosed in the entitlement offer prospectus. Regal's prospectus included statements to the effect that Regal shareholders would have priority under the shortfall offer.

The notice of meeting and prospectus also included statements that the directors reserved a general discretion over the allocation of shortfall shares.

Following closure of the entitlement offer, Regal received applications for 184,166,015 shortfall shares. However, Regal issued only 118,907,986 shares to applicants. The remaining shortfall shares were issued to Ndovu as underwriter.

The Panel considered that Regal's treatment of applications for shortfall shares was inconsistent with its disclosure in the notice of meeting and prospectus, and as a result:

- Regal shareholders were not given sufficient information to assess the transactions the subject of the shareholder resolutions; and
- the acquisition of control over voting shares in Regal has not taken place in an efficient, competitive and informed market.

The Panel considered that the circumstances were unacceptable, having regard to the effect that the Panel is satisfied the circumstances have had on:

- the control, or potential control, of Regal; or
- the acquisition, or proposed acquisition, by Ndovu of a substantial interest in Regal; and / or
- the purposes of Chapter 6 set out in s. 602.

The Panel has made orders requiring Regal to make an offer of new shares to Regal shareholders who were scaled back under the entitlement offer, at an offer price of $0.01 per share (being the entitlement offer price). Those shareholders will be entitled to apply for the number of shortfall shares they applied for but were not issued under the entitlement offer.

The orders also cancel shares held by Ndovu in such number as is equivalent to the number of shares issued to scaled back shareholders pursuant to the new offer.

5. Recent Research Papers

5.1 Shareholder class actions - A critical analysis of the procedure under Part IVA of the Federal Court of Australia Act

Part IVA of the Federal Court of Australia Act 1976 No. 156 (Cth) governs the class action procedure, which has been available in Australia since March 1992. The procedure was not popular amongst shareholders until the late 1990s, and since then, the number of shareholder class actions has steadily increased. Many of these shareholder class actions settled before a final court hearing. This article critically examines the class action procedure and in doing so, highlights the current issues that contribute to a rapid rise in shareholder class actions. The article calls for reform to the class action procedure. It identifies areas for reform in an attempt to improve the position of the group members so that they can receive a better outcome than what they can get under the current class action model.

Shareholder Class Actions - A Critical Analysis of the Procedure Under Part IVA of the Federal Court of Australia Act

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5.2 The regulation of hedge funds

Hedge funds are deliberately structured to sidestep legislative strictures, disclosure and other compliance requirements imposed on institutions raising funds for their activities and as such operate within the cracks of the law. Consequently, there has been much discussion on whether hedge funds should be regulated. Those disfavouring regulation see hedge fund activity as generating efficiency in the marketplace including securities markets by "mitigating price downturns, bearing risks that others will not, making securities more liquid, and ferreting out inefficiencies". Those fearful of financial market failure and its contagion effects, however, argue for varying degrees and forms of regulatory intervention aimed at several different levels: the fund itself (as with the case of a corporate entity); the managers of the fund (in respect of their investment strategies); investors into the fund (investment unit holders as well as creditors); and intermediaries such as broker dealers who facilitate the transactions of the fund. This paper evaluates these claims, as well as exploring the most effective point of regulatory intervention from an investor perspective.

The Regulation of Hedge Funds

5.3 The role of auditing in corporate governance in Australia and New Zealand: A research synthesis

Corporate governance is of growing importance in Australia, New Zealand and all over the world. Corporate governance interacts with auditing and it is useful to understand how corporate governance and auditing affect companies. However, the interaction is not straight forward. To some extent, good auditing will lead to recommendations that will lead to improved governance; while on the other hand, good governance will lead to directors setting high standards including demanding a high standard of auditing. A related issue is whether better governance is a substitute for auditing or a complement. Previous studies of that issue have had mixed results. This review article provides a synthesis of Australian and New Zealand research about corporate governance and auditing that takes stock of what has been found and examines issues that can be explored using multiple studies. We conclude that despite extensive research, there is still considerable uncertainty about the effects of corporate governance mechanisms on auditing and the effects of auditing on corporate governance. The results are intended to be helpful in providing advice about policy in Australia and New Zealand, and in determining directions for new research.

The Role of Auditing in Corporate Governance in Australia and New Zealand: A Research Synthesis

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5.4 Corporate culture: The interview evidence

The authors conduct in-depth interviews of senior executives representing over 20% of the market capitalisation of the US equity market to understand:

- the importance, antecedents and consequences of corporate culture;
- the mechanisms that underlie the creation and effectiveness of corporate culture; and
- the factors that deter a firm from achieving its aspirational culture.

The interviews provide the following insights. First, executives characterise culture as "a beliefs system," "a coordination mechanism," and "an invisible hand." Second, most executives view culture as one of the top three factors that affect their firm's value. Cultural fit in M&A deals is so important that most executives would walk away from a target that is a cultural misalignment. Third, culture is primarily set by the current CEO. Fourth, boards do not directly choose the firm's culture; instead, they influence the choice of culture by picking the CEO and through their influence on specific policies like incentive compensation, hiring, firing, and promotion decisions, and the values the finance function embraces. Fifth, executives emphasise that for a firm's culture to be effective, the firm's espoused values must be backed up by actual behaviour and norms. Sixth, an effective culture improves firm value and profitability by (i) fostering creativity and encouraging productivity; (ii) promoting more risk tolerance; (iii) mitigating myopic behaviour; (iv) creating a climate for suggesting critiques and for allowing ideas to germinate organically; and (v) compensating for mistakes in ways that the firm's assets cannot. In addition to the above, executives suggest several sources of publicly available data to measure corporate culture.

Corporate Culture: The Interview Evidence

6. Recent Corporate Law Decisions

6.1 Taking away the sugar member's powers: oppressive, unfairly prejudicial or unfairly discriminatory

(By Kai Ito, Herbert Smith Freehills)

Mackay Sugar Limited v Wilmar Sugar Australia Limited [2016] FCAFC 133.

Federal Court of Australia, Full Court, Gilmour, Jagot and White JJ, 6 October 2016

(a) Summary

This decision was an appeal from *Wilmar Sugar Australia Limited v Queensland Sugar Limited, in the matter of Queensland Sugar Limited* [2016] FCA 20.

At issue in the appeal was whether a resolution passed in a general meeting of members of Queensland Sugar Ltd (QSL) on 8 December 2015 (General Meeting) to amend QSL's constitution (Constitution) was oppressive to, unfairly prejudicial to, or unfairly discriminatory against a member of QSL, Wilmar Sugar Australia Ltd (Wilmar), within the meaning of s. 232 of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act). Section 232 of the Corporations Act provides, amongst other tests, that if the conduct of a company's affairs or a resolution of members or a class of members does have this effect then the Court may make an order under s. 233, which the trial judge did with the effect of returning the Constitution to its pre-General Meeting form.

By unanimous decision, the Court dismissed the appeal.

(b) Facts

(i) Commercial and legal relationships of the parties

At first instance, the plaintiff was Wilmar and the defendant was QSL. The Appellants did not participate in the trial but were granted leave to appeal in the present case. QSL's members comprise of seven sugar mill owners and 23 sugar grower representative members. The Appellants were three of the sugar mill owner members, being:

- Mackay Sugar Limited (Mackay);
- Isis Central Sugar Mill Company Limited (Isis); and
- Bundaberg Sugar Limited (Bundaberg).

The other mill owners are:

- Wilmar (which is the largest producer of raw sugar in Australia);
- MSF Sugar Limited (MSF);
- Tully Sugar Limited (Tully); and
- WH Heck & Sons Pty Ltd (Heck).

QSL operates six bulk sugar terminals in Queensland, in which it stores sugar and exports it to overseas markets. Mill owners acquire raw sugar from growers and then supply that raw sugar to QSL under Raw Sugar Supply Agreements (RSSAs). QSL then markets the majority of this raw sugar to export markets.

Under the RSSAs the mill owners also have an option to identify an amount of raw sugar (calculated using a formula in the RSSAs) as Supplier Economic Interest Sugar (SEIS). When exercised, this option requires QSL to supply the nominated SEIS amount of sugar back to the mill owner, who can then sell the sugar and receive the proceeds itself.

QSL handles about 3.5 million tonnes of raw sugar annually (about 85% of Australia's total raw sugar exports and about $1.7 billion in revenue), and the sugar that Wilmar supplied to QSL under its RSSA was about 54% to 60% of the overall raw sugar received by QSL for export each year. Wilmar also nominated about 700,000-800,000 tonnes of raw sugar as SEIS, which a company in Wilmar's corporate group then marketed and sold internationally. Each of MSF, Tully, Isis and Mackay also elected an SEIS amount under their RSSAs with QSL. As such, for the SEIS amounts, the mill owners competed with QSL in respect of the marketing and exporting of raw sugar.

Wilmar, MSF and Tully all gave notices of termination under their respective RSSAs with QSL, with termination to take effect on 30 June 2017. It was shown at trial that QSL's board of directors were taking various steps to prepare for direct competition with Wilmar, MSF and Tully from this date. QSL's CEO also gave evidence that QSL was concerned that if QSL, MSF or Tully were to have access to QSL's strategies and plans then they may gain a competitive advantage over QSL.

(ii) Amendments to QSL's constitution

QSL's constitution provided for board vacancies to be filled by votes calculated using a formula which depended on the amount of raw sugar each mill owner supplied to QSL. In effect, this meant that Wilmar's preferred nomination would prevail (as Wilmar supplied more than half of the raw sugar to QSL), and Wilmar chose to use this ability to have a board of four independent directors.

In the case of a mill owner who had given notice of termination for their RSSA, the constitution also placed limitations on voting rights on a resolution and precluded such a mill owner from participating in the selection of the Board Selection Committee.

It was in this context that the constitutional amendments at the General Meeting were passed, including with the following effect:

- Wilmar's power to approve nominations of directors was negated;
- each of the Appellants (who had not issued notices of termination under their RSSAs) could now nominate a director and remove or replace the director they had nominated;

- any new director (who fell within the Mill Owner Director class) had to be a person nominated by one of the Appellants; and
- even if Wilmar, MSF or Tully resumed supplying sugar to QSL they could not nominate a Mill Owner Director without the Appellants' approval.

(c) Decision

(i) Meaning of oppressive to, unfairly prejudicial to, or unfairly discriminatory against

In considering whether the changes to QSL's constitution were oppressive to, unfairly prejudicial to, or unfairly discriminatory against a member of QSL within the meaning of s. 232 of the Corporations Act, the Court had regard to Brennan J's decision in *Wayde v New South Wales Rugby League* (1994) 180 CLR 459 at 472-3, where his Honour stated that:

"It is not necessarily unfair for directors in good faith to advance one of the objects of the company to the prejudice of a member where the advancement of the object necessarily entails prejudice to that member or discrimination against him ... The test of unfairness is objective and it is necessary, though difficult, to postulate a standard of reasonable directors possessed of any special skill, knowledge or acumen possessed by the directors. The test assumes ... that reasonable directors weigh the furthering of the corporate object against the disadvantage, disability or burden which their decision will impose, and address their minds to the question whether a proposed decision is unfair".

The decision in *Catalano v Managing Australia Destinations Pty Ltd* [2014] FCAFC 55 was also considered, where Siopis, Rares and Davies JJ stated:

"The question is whether objectively in the eyes of the commercial bystander there has been unfairness, namely conduct that is so unfair that reasonable directors who consider the matter would not have thought the conduct or decision fair".

(ii) The Appellants' contentions

The Appellants did not contend that the trial judge made an error of law or had misunderstood the evidence but rather erred in evaluating the importance of, and the weighting that should be given to, the evidence.

The Appellants contended that the weighting the trial judge gave to Wilmar having a continuing commercial interest in QSL was incorrectly high, and did not consider all the relevant circumstances. Included in the Appellants' submission was the suggestion that "Wilmar had brought the conduct found to be oppressive on itself, by giving notice that it did not wish to extend its RSSA": [56]. However, the Court found that Wilmar still had a continuing commercial interest (that for a number of reasons had not fundamentally changed), and the trial judge's considerations in this respect were appropriate.

The Court rejected the Appellants' argument that the trial judge did not give sufficient weight to the changed competition in the marketing of raw sugar, and it was now in Wilmar's interest for QSL not to succeed, justifying a response from QSL that discriminated against Wilmar. The Court found that "the significance of the changed circumstances of competition should not be overstated", particularly given that Wilmar, MSF, Tully, Isis and Mackay were already in competition with QSL and each other in relation to the marketing of SEIS, and so similar conflicts that had arisen could continue to be managed in the same way.

Finally, the Court rejected the Appellants' argument that the trial judge gave too much weight to the fiduciary and statutory duties QSL directors owed to QSL, even if appointed by Wilmar. The Court stated that there was no evidence that Wilmar exercised any influence over the present independent directors, or intended to depart from its longstanding practice and appoint its own nominees to QSL's board. In addition, the Court held that a commercial observer "would know that the statutory and fiduciary duties of directors are not mere matters of form" and not readily conclude that any hypothetical Wilmar-appointed directors would breach their duties owed to QSL.

Accordingly, the Court dismissed the appeal, with the departing emphasis that "this decision, like that of the trial Judge, concerns the commercial fairness of the position at present and until 30 June 2017. Once Wilmar ceases altogether to supply sugar to QSL pursuant to its RSSA, the balance of the commercial fairness may well change": [85].

6.2 Applying the forfeiture principle to the profit share of partners and members of LLPs

(By Dea Fairbairn, Minter Ellison)

Jeremy Hosking v Marathon Asset Management LLP [2016] EWHC 2418, England and Wales High Court, Chancery Division, Newey J, 5 October 2016

(a) Summary

This English case concerned an appeal of an arbitration award. In issue was whether the principle that a fiduciary acting in breach of a fiduciary duty may lose the right to remuneration also applied to the right to a share in the profit of a partnership. The High Court found that a limited liability partnership (LLP) member's profit share can be forfeited for breach of fiduciary duty, where it can be characterised as a reward for undertaking fiduciary duties (cf. where it reflects an ownership interest in the firm).

(b) Facts

On 2 September 2004, Marathon Asset Management LLP (Marathon) entered into a deed (the LLP Deed) to continue running an investment management business originally set up in 1986 by Mr Jeremy Hosking, Mr Neil Ostrer and two other members (Founding Members). Amongst other things, the LLP Deed set out that the Founding Members were entitled to a share in the profits of the business.

Profits payable to the Founding Members are to be shared equally while each member is employed to work in Marathon's business (Executive Members). Members who are no longer employed by Marathon, or who no longer contribute to the running of the business for reasons of retirement or otherwise (Non-Executive Members), receive 50% of the profits they would have been entitled to if they were still an Executive Member.

On 5 April 2012, Mr Hosking gave notice of his intention to retire and he did so on 11 December 2012, thereafter he became a Non-Executive Member and his profit share was reduced accordingly. Shortly afterwards, Marathon brought arbitration proceedings against Mr Hosking and on 1 October 2014 Mr David Owen QC (the Arbitrator) made a Liability Award that Mr Hosking breached his contractual and fiduciary duties while he was an Executive Member of Marathon. It was established in the arbitration that in July 2012 Mr Hosking had discussed with four significant employees of Marathon, the possibility of starting a new business and had produced a business plan outlining his thoughts.

The Arbitrator determined that, as a result of Mr Hosking's breaches of duty, Marathon had lost the chance of retaining three individuals referred to as the "Global Three". As a result, the Arbitrator concluded Marathon was entitled to equitable compensation in the sum of £1.38 million in respect of the lost chance of retaining the Global Three. It was also concluded that Mr Hosking should forfeit to Marathon £10,389,957.50 (representing 50% of the payment Mr Hosking had received) which had been paid to him during the period of mid-July to mid-December 2012 (the period when he was in breach of his fiduciary duties).

The Arbitrator was of the view that the distinction between Non-Executive Members and Executive Members pertained to the additional obligations imposed on Executive Members. In essence, the additional 50% share of the profits Executive Members received was remuneration for performance of their executive duties (including fiduciary duties). The other 50%, being received by both Executive Members and Non-Executive Members, reflected only an ownership interest in the business.

The Arbitrator's decision was appealed by Mr Hosking to the High Court on the basis that forfeiture could not apply to an LLP member's profit share because it reflects an ownership share in the business rather than remuneration in exchange for performance of fiduciary duties.

(i) The parties' cases

Counsel for Mr Hosking submitted that the forfeiture principle has no application in relation to the share of profits of a partner or member of an LLP. It was said that the obligations of a fiduciary and their incidents depend on the particular context. It was contended that with partnerships and LLPs there is a conceptual difference between profit share and remuneration.

Counsel for Mr Hosking argued that "remuneration" refers to money payable in exchange for services as an expense prior to the division of profits irrespective of the profitability of the firm. In contrast, it was contended that a profit share of a partner or member reflects his status as a partner or member and his ownership interest. It was submitted that a profit share does not lose its character and become remuneration because the partner or member is required to provide his services. The profit share remains payable to the partner or member, and in consequence of his interest in the partnership or LLP, and not as remuneration for his services, even if from a commercial point of view it also compensates the partner or member for his services. Finally, it was argued that there is no provision for forfeiture in the LLP Deed and allowing forfeiture would be inconsistent with and distort the commercial bargain between the parties.

In contrast, Marathon contended the Arbitrator was right to take the view that profit share can be forfeited. It was argued that any payment made to a partner in a partnership or member of an LLP in return for services represents remuneration and is potentially susceptible to forfeiture.

Counsel for Marathon argued that, "as a matter of language profit share payable for undertaking specific duties can appropriately be described as 'remuneration' and that it would make no sense to exclude rewards from the forfeiture principle just because they happened to be conferred by way of profit share". It was suggested that to do so would involve preferring form to substance, which is inconsistent with the basis for the forfeiture principle.

Counsel for Marathon also argued that there is no relevant authority that says either that partners or members of LLPs are to be treated differently from other fiduciaries or that it matters whether a payment for services is made by way of profit share. In Marathon's case, consistent with the principle that, where profit share of a partner or a member of an LLP can be identified as attributable to the provision of services, it should be liable to forfeiture, which is said to chime with the "no profit" rule, (see *Chan v Zacharia* (1984) 154 CLR 178); any potential for unfairness is removed by the requirement that forfeiture should not be disproportionate or inequitable.

Finally, in response to Mr Hosking's argument that there is no provision for forfeiture in the LLP Deed, it was suggested by Marathon that this is unimportant since the forfeiture rule overrides the ordinary operation of contractual entitlements to remuneration.

(c) Decision

In rejecting the appeal, Newey J held that a profit share of a partner or LLP member can potentially be subject to forfeiture.

In reaching his conclusion, Newey J provided a number of reasons. First, it was determined that the Arbitrator was correct to conclude that the forfeiture principle can apply to partners. Newey J acknowledged that while previously the forfeiture principle has mainly been invoked in relation to agents, the rationale for it extends more widely to be applicable to other fiduciaries too. The rationale is based on the need to deter fiduciaries from betraying the trust that is placed in them, which will not necessarily be achieved by requiring the fiduciary to pay damages (see *Management Ltd v Jack* [2009] EWCA Civ 63).

Newey J rejected Mr Hosking's argument pertaining to the distinction between remuneration (which is subject to forfeiture) and profit share (which, on Mr Hosking's argument, could not be subject to forfeiture). Newey J found that while it would often be impossible to characterise the profit share of a partner or LLP member as "remuneration", that was not necessarily always the case. In those unusual cases where a profit share can be identified as a reward for undertaking specific fiduciary duties, there is no good reason for treating it differently from any other form of remuneration. In any event, he considered that the law should be concerned with the substance of the arrangements rather than the form.

Finally, Newey J concluded that the fact there was no contractual provisions or documentation for forfeiture in the LLP Deed cannot necessarily mean that there is no scope for it. It was acknowledged that while the forfeiture principle can be excluded by contract, it has been taken to apply where there is no reference to it in a relevant contract.

6.3 Leave to proceed against company in liquidation refused

(By Katrina Sleiman, Corrs Chambers Westgarth)

QNI Resources Pty Ltd v Park [2016] QSC 222, Supreme Court of Queensland, Bond J, 29 September 2016

(a) Summary

Two joint venturers (QNI Resources Pty Ltd and QNI Metals Pty Ltd (the Joint Venturers)) and the current manager of the joint venture (Queensland Nickel Sales Pty Ltd (QNS)) sought leave to proceed against the former manager of the joint venture and a company in liquidation (Queensland Nickel Pty Ltd (Queensland Nickel)) pursuant to s. 500(2) of the Corporations Act 2001 No. 50 (Cth) (the Act).

The applicants advanced contractual and equitable claims against Queensland Nickel which relied on an unconditioned obligation to return joint venture property. An essential aspect of the applicants' pleaded case was the negation of

Queensland Nickel's entitlement to an indemnity that may confer proprietary or beneficial rights in the joint venture property.

The Court refused leave as it was not satisfied that the applicants' pleaded case established a serious question to be tried in respect of the claims advanced. The Court considered the acceptance of the claims advanced would be an affront to justice.

(b) Facts

In 1992, a nickel mining and refining project had become owned and operated by two joint venturing companies, whose relationship inter se was governed by a Joint Venture Agreement. That agreement also recorded the appointment of Queensland Nickel as the General Manager of the joint venture and expressed the parties' agreement on a number of matters concerning the role of the General Manager and its relationship with the joint venturers. The General Manager had broad responsibilities for managing the operations, funds and property of the joint venture. The agreement noted that "All Joint Venture Property shall at all times be made available for the purpose and duration of the joint venture and during such duration shall not be used for any other purpose"

Interests in the joint venture changed hands from time to time, but as from 1995 the interests in the project became held by the Joint Venturers. Since at least 2009, the relationship of the Joint Venturers inter se and between them and Queensland Nickel, had not been an arms-length relationship. In about 2009 entities controlled by Clive Palmer acquired a 100% interest in the Joint Venturers. The Joint Venturers in turn owned Queensland Nickel, holding the shares in Queensland Nickel in the same proportions as they owned their interests in the project. Since 2009, Mr Palmer had also been chair of the Joint Venture Oversight Committee, which was the committee which, on behalf of the two Joint Venturers, had the oversight role over the activities of Queensland Nickel as General Manager of the joint venture.

Queensland Nickel was placed into voluntary administration on 18 January 2016 with reported liabilities of $226,390,547. Liquidators were subsequently appointed.

The Joint Venturers and QNS sought leave to proceed against Queensland Nickel. Amongst other things, the applicants claimed the unconditional return of all of the joint venture property held by Queensland Nickel, despite the fact that Queensland Nickel had, apparently, and to the knowledge of the Joint Venturers, properly incurred very significant liabilities and no provision had been made for their discharge.

An essential aspect of the applicants' claims was the negation of the proposition that Queensland Nickel had any beneficial interest in the joint venture property or a right of indemnity out of that property in respect of the liabilities incurred by it.

(c) Decision

(i) Proper approach to an application for leave

Bond J noted that s. 500(2) of the Act has been construed as conferring on the Court a supervisory jurisdiction. The Court is concerned to protect companies in liquidation from being harassed by unnecessary litigation. The Court is also concerned to assist in the orderly administration of companies in liquidation by requiring claimants to adopt the ordinary procedure of lodging a proof of debt unless the claimants can demonstrate that there is some good reason why a departure from that procedure is justified. Bond J noted the following considerations:

- the applicants must show that the case they wish to progress has sufficient merit to warrant the grant of leave, that is, they must demonstrate a serious question to be tried as to their entitlement to the relief they claim. Mere assertion, which is not supported by a solid foundation, will not be sufficient;
- the applicants should lodge a proof of debt and pursue their rights in this way, unless they can show some good reason to the contrary;
- although the relevant considerations cannot be exhaustively stated, some guidance may be obtained from past cases. Some considerations include:
    - the amount and seriousness of the claim, the degree of complexity of the legal and factual issues, and the stage of the proceedings, if commenced;
    - any procedural or substantive prejudice to the creditors resulting from the proceedings;
    - whether the liquidator is likely to reject any proof of debt lodged by the applicant so that an appeal to the court will be necessary;
    - the fact that the applicant has claims against others raising substantially the same issues in which case there is a real question of the inconvenience of the applicant having to follow different procedures in respect of all its claims;
    - whether the existence of pretrial procedures, such as discovery and interrogatories, are likely to be required or beneficial; and
    - where there would be multiple proceedings were leave not granted, this would be a powerful factor favouring the grant of leave, thus, where one of a number of claims is permissible, leave may be granted for a weaker, associated claim; and
- the Court may grant leave on terms. For example, the grant of leave is subject to a condition that the applicant would not seek to enforce any judgment it obtained without first obtaining the leave of the Court.

(ii) Failure to demonstrate a case of sufficient merit to warrant the grant of leave

On the material before Bond J, the applicants' case involved the Court accepting the following propositions:

- the Joint Venturers could place a General Manager in charge of the management, operation and administration of their joint venture and of the management and control of the joint venture property, which they had agreed to make available to the General Manager for the purpose and duration of the joint venture (and solely for that purpose);
- the Joint Venturers could knowingly allow their General Manager to incur tens of millions of dollars of liability in relation to joint venture expenses for matters as apparently proper and fundamental to the conduct of the joint venture business by the General Manager as its employees, its freight handler and its ore supplier;
- the Joint Venturers could knowingly allow their General Manager not to follow the formal mechanisms for financial reporting and budgeting set out in the Joint Venture Agreement as the means by which they could be required to provide funds to the General Manager, expecting that the General Manager would be able to generate sufficient funds to meet the joint venture expenses by the use of joint venture property to conduct the joint venture business; and
- by the simple expedient of terminating the relationship and appointing a new General Manager, the Joint Venturers could, without making any provision for the discharge of the former General Manager's liabilities for joint venture expenses properly incurred, establish an entitlement to compel the former General Manager to transfer all the joint venture property to the new General Manager, but to keep all of the liability.

His Honour held that acceptance of such a case would be a startling affront to justice. His Honour relied on "a number of well-recognised legal principles, the application of which would enable the law to avoid such an affront". Based on those principles, it could be concluded that the General Manager had a right of indemnity which would be regarded as secured by a lien over the joint venture property.

His Honour held that absent a solid foundation for the pleaded negations, there can be no solid foundation to (and no point in the Court embarking on a consideration of) the applicants' claims for relief against Queensland Nickel. His Honour dismissed the application.

6.4 Pay the bill: The pitfalls of indemnifying a director's misdeeds as a third party funder

(By Samuel J. Hickey, LLB Candidate, University of Queensland)

Iron Mountain Mining Ltd v K & L Gates [2016] WASCA 166, Supreme Court of Western Australia, Court of Appeal, Martin CJ, Murphy and Mitchell JJA, 27 September 2016

(a) Summary

In *Iron Mountain Mining Ltd v K & L Gates*, the Court stayed an appeal against the Supreme Court of Western Australia's decision to deny an application for an assessment of legal costs. The stay was issued on the basis that proceedings had been instituted contrary to s. 58(3)(b) of the Bankruptcy Act 1966 No. 33 (Cth) (the BA).

The Court's judgment contained important holdings in relation to the construction of indemnities covering the costs of criminal proceedings, and the ability of companies to recover excessive legal fees when they have funded litigation as a third party, but have no contractual relationship with the legal practice.

The judgment signifies that merely paying another's legal expenses does not warrant an entitlement to a costs assessment, or the reimbursement of excessive legal fees.

(b) Facts

Iron Mountain Mining Ltd (IMM) had agreed to indemnify their officers against liability in criminal proceedings. Mr Zohar relied on this indemnity in defending proceedings brought against him pursuant to s. 1309(2) of the Corporations Act 2001 No. 50 (Cth) (the CA) for supplying the Australian Securities Exchange with false and misleading information. Mr Zohar's representatives in these proceedings were K & L Gates (KLG). There was no contractual relationship between IMM and KLG.

Mr Zohar eventually pleaded guilty to three of the six offences with which he had been charged, and the other three were discontinued. He was subsequently declared bankrupt.

Section 199A of the CA prohibits companies from indemnifying persons for proceedings in which they had been found guilty. Section 199C provides that an agreement is void to the extent that it contravenes s. 199A.

IMM applied for an assessment of the costs it had incurred in defending Mr Zohar under the Legal Profession Act 2008 No. 21 (WA) (the LPA). Section 295 of the LPA provides that a third party payer can apply to a taxing officer for an assessment of a bill for legal costs. The term "third party payer" is defined in s. 253(1)(a) to mean a person who had been under an obligation to pay legal costs.

The Supreme Court of Western Australia found that IMM was not a third party payer, and thus not entitled to a costs assessment. The master reasoned that, in order for a party to have "owed an obligation", that obligation had to have been in existence at the time when the application for a costs assessment had been made. As the indemnities owed to Mr Zohar had been rendered void *ab initio* by virtue of s. 199C of the CA, IMM had not been under an obligation to pay Mr Zohar's legal fees.

IMM appealed this decision, arguing that they in fact were a third party payer, and that the indemnities should have been construed in such a way as to avoid being rendered void. Notably, IMM's purpose in seeking an assessment was not to recover an amount from Mr Zohar. Rather, it contended that KLG was subject to an implied obligation under the LPA to repay the difference (if any) between the legal services IMM had paid for and the amount as certified by a costs assessment.

(c) Decision

(i) Construction of the indemnities

IMM's primary argument was that the master had erred in finding that the CA had rendered the indemnities void ab initio. IMM contended that the indemnities should have been subject to an implied condition that, in the event Mr Zohar was found guilty, he would repay all legal costs to IMM. In *Note Printing Australia Ltd v Leckenby* [2015] VSCA 105, the Victorian Court of Appeal confirmed that an agreement containing a condition to this effect would not contravene s. 199A, and would therefore not be rendered void by s. 199C.

Both sides accepted that the indemnities should be construed in line with the decision in Leckenby. It was not necessary for the Court to consider this issue further, although it did indicate that it was not at odds with the construction proposed by the parties.

As the Court did not resolve this issue, it would be unwise to assume that indemnities will be interpreted in line with Leckenby. Indemnity clauses that could extend to covering the cost of criminal proceedings should therefore clarify that payments will only be made up until, and unless, a guilty verdict is reached, and that the indemnified is obliged to repay their legal fees if found guilty.

(ii) IMM's eligibility for a cost assessment

The key question of law in this case concerned the construction of the requirement under s. 253 of the LPA that a party seeking a costs assessment had to be under an obligation to pay another person's legal fees. IMM contended that it was enough for that obligation to have existed at the time when payment had been provided. KLG's riposte was that the relevant obligation had to have existed at the time when the application for an assessment had been made.

Ultimately, the Court adopted KLG's construction of s. 253. This holding was justified by the fact that there would be no point in an assessment determining an amount payable pursuant to an obligation that did not exist at the time of assessment.

The Court's decision reflects a substantial change from the LPA as it was in 2003. Under the 2003 legislation, any "party charged" could apply for a taxation of costs. The Court's finding reflects the narrow approach favoured by the 2008 legislation, which now prevents gratuitous payors from seeking a costs assessment.

Notwithstanding the Court's acceptance that the indemnities had not been invalidated by s. 199C, it still found that IMM was not a third party payer. The Court reasoned that, because Mr Zohar had been found guilty at the time IMM had made their application, IMM had not been under any obligation to pay Mr Zohar's legal fees.

The Court went on to comment that IMM's motivations in seeking the assessment were misconceived. It clarified that the effect of undertaking a costs assessment under the LPA would only determine the amount that IMM should have paid for defending Mr Zohar. In situations where legal costs had already been paid, such as the present, a costs assessment could only quantify whatever refund might be payable to IMM by Mr Zohar, in the event that excessive legal fees had been charged. As IMM had no agreement with KLG, a costs assessment would not be binding on KLG, nor give rise to any obligation to KLG.

If IMM were granted a costs assessment, Mr Zohar would have to repay to IMM any amount that was in excess of the amount as taxed under the assessment. As a non-associated third party payer, IMM could have no recourse against KLG for excessive legal costs. It is possible that this problem could have been avoided if KLG had been brought into the contractual relationship between IMM and Mr Zohar.

The Court also dismissed IMM's contention that there was an implied obligation on KLG to reimburse the difference between the costs paid and costs as taxed under an assessment.

The impact of the Court's construction is that companies providing indemnities in Western Australia must be mindful of the fact that, if the person they are indemnifying becomes insolvent, it may be fruitless to seek a costs assessment for the value of legal expenses. If a company has funded litigation under a scheme which fails to create a contractual relationship between the company and the legal practice, then the company could be left in the precarious position of being bound to pay legal fees without being able to seek a costs assessment.

(iii) The staying of the appeal

The Court acknowledged that IMM may still have an obligation to pay Mr Zohar's legal fees in respect of the discontinued charges. If IMM applied for an assessment of legal fees in relation to those charges, Mr Zohar could be liable to reimburse IMM for excessive legal costs. The Court considered it appropriate that Mr Zohar and his trustee in bankruptcy be joined to the proceedings before they continued. The Court stated that it could not yet conclude that the appeal be wholly dismissed.

Finally, the Court determined that any future proceedings should be brought before a court with federal jurisdiction. It was found that monies for legal fees owed by a bankrupt client to a third party provider of legal costs constituted a provable debt, as defined under s. 58(3) of the BA, and as such only a court with bankruptcy jurisdiction could hear the matter.

6.5 Liquidator's application for extension of time under s. 588FF(3)(b) to bring voidable transaction proceedings

(By Katrina Sleiman, Corrs Chambers Westgarth)

In the matter of Walton Construction (Qld) Pty Ltd (In Liq) [2016] FCA 1152, Federal Court of Australia, Edelman J, 23 September 2016

(a) Summary

The liquidators of Walton Construction (Qld) Pty Ltd and Walton Construction Pty Ltd (the Companies) applied to extend the time within which to bring voidable transaction proceedings under s. 588FF(1) of the Corporations Act 2001 No. 50 (Cth) (the Act). Section 588FF(3) of the Act provides that unless the Court allows a longer period, any voidable transaction application must be made by the later of three years after the relation-back day or 12 months after the first appointment of a liquidator in relation to winding up.

The liquidators sought general, or "shelf", orders extending the time without specifying any particular potential respondent or transaction in the orders.

After consideration of the matters relevant to its discretion, the Court made orders for a general extension of time for six months to bring any application by the Companies under s. 588FF(1).

(b) Facts

In October 2013, administrators were appointed to the Companies, and subsequently, were appointed as liquidators. Proceedings were brought for the removal of the liquidators due to a conflict of interest and they were replaced in July 2014. The new liquidators lost significant time for reasons outside of their control (the termination of the first liquidators and difficulty in recovering and reviewing the Companies' books and records). The liquidators claimed to have identified four potential voidable transactions, totalling around $4 million and expected to uncover further voidable transactions in the course of undertaking further investigations.

The liquidators made an application to extend the time within which to commence the identified voidable transaction proceedings. The application was opposed by the prospective defendants to the foreshadowed litigation, Mawson Restructures and Workouts Pty Ltd (Mawson) and QHT Investments Pty Ltd (QHT).

Mawson pointed to delays by the current liquidators and the merits of its potential defence. QHT argued that the transaction in relation to it had been investigated, a claim had already been brought in relation to it, and there was no basis to infer that any new matter might be identified in relation to it.

(c) Decision

(i) Legal principles concerning an application for an extension of time

In *Fortress Credit Corporation (Australia) II Pty Ltd v Fletcher* (2015) 254 CLR 489 (Fortress), the High Court held that s. 588FF(3) entitled the Court to make "shelf orders" extending the limitation period in which to commence voidable transaction proceedings not yet identified. As s. 588FF(3)(b) does not prescribe any criteria for the exercise of the discretion, Edelman J considered recent authorities.

In *Walker v CBA Corporate Services (NSW) Pty Ltd* [2012] FCA 328, the Court considered three matters which will usually be considered:

- the explanation for the delay in commencing the proposed proceedings within the period provided for by the statute;
- any prejudice likely to be suffered in the event the extension is granted; and
- a preliminary view of the merits of the proposed proceeding, except where the liquidator's purpose in seeking the extension is to undertake further work to decide whether or not to bring proceedings.

In relation to "shelf orders", the High Court in Fortress identified the following considerations relevant to the exercise of the Court's discretion:

- disadvantage to potential defendants not identified in a shelf order;
- the encouragement to liquidators not to identify potential defendants, thereby reducing the prospect of opposition at initial application;
- the risk of a multiplicity of litigation by successive defendants applying to reagitate extension applications of which they had not been given initial notice;
- the risk of inconsistent outcomes on applications to set aside extension orders by respective defendants;
- no finality, as claims by defendants that they were identifiable, but not identified, might cause ongoing challenges to any extension granted;
- want of certainty for liquidators and prospective defendants who might seek to have leave revoked after it had been granted and after proceedings had commenced;
- the potential for wasted costs to be incurred contrary to the interests of creditors; and
- the determination of applications by reference only to evidence that the liquidator elected to put before the court.

(ii) Consideration of relevant factors

Edelman J held that there should not be an extension of time in relation to QHT. In relation to Mawson and in considering Mawson's objections, Edelman J had regard to the following factors:

- the limited time the current liquidators have had to investigate claims following the termination of the initial liquidators;
- difficulties in accessing the Companies' books and records;
- the substantial work that the current liquidators have been able to perform, with limited funding;
- Mawson's concession that it would not suffer any prejudice beyond the general prejudice of delay which is suffered by any other party against whom a claim might be brought following an extension of time;
- the merits of a claim will weigh more heavily as a factor where the extension is sought to bring a claim which has been identified as one which will be brought, rather than where the reason for the extension is to investigate, consider and to obtain the advice of counsel as to whether to bring a claim; and
- in an application of this nature it will be rare for the Court to be in a position to reach conclusions about the merits of any prospective claims or defences.

After weighing up the relevant factors, Edelman J was satisfied that the liquidators should be granted a general shelf order extension of six months to investigate, consider, and bring any further claim based on s. 588FF(1) of the Act. The liquidators were also granted an extension of the limitation period of six months with respect to three out of the four identified claims on the basis that the liquidators were resolving matters relating to funding. The liquidators obtained an extension of the limitation period for eight weeks with respect to an identified claim against the Australian Taxation Office.

6.6 Electronic signatures, ostensible authority, ratification and estoppel

(By Robert Marsh, King & Wood Mallesons)

Williams Group Australia Pty Ltd v Crocker [2016] NSWCA 265, Supreme Court of New South Wales, Court of Appeal, Ward, Simpson and Payne JJA, 22 September 2016

(a) Summary

In this case before the New South Wales Court of Appeal the appellant argued that despite the respondent (Mr Crocker) not placing his electronic signature on a credit application and an associated all-moneys guarantee personally, nor specifically authorising anyone else to place his signature on the documents, the appellant was able to enforce the documents against Mr Crocker.

The appellant's arguments in the appeal fell into three main categories:

- ostensible authority;
- ratification; and
- estoppel.

Ward J held, with Simpson and Payne JJA agreeing, that on the facts of the case, Mr Crocker hadn't made any representation to the appellant that he had authorised any other person to affix his electronic signature to the documents and as such could not be personally bound under the principles of ostensible authority. The absence of any relevant representation also defeated the appellant's claims based on estoppel. Finally, the court dismissed the appellant's arguments in relation to ratification as there was no evidence that Mr Crocker had actual knowledge of the guarantee, nor that he had "shut his eyes to the obvious" in relation to the presence of the guarantee.

(b) Facts

Mr Crocker was one of three directors of IDH Modular Pty Ltd (IDH), a special purpose company set up to supply building modules for a building project. Mr Crocker and his co-directors were also directors of a related entity, Image Designer Homes Pty Ltd (Image). In 2010, Williams Group Australia Pty Ltd (Williams) approved a credit application by Image, supported by an all-moneys guarantee signed be each of Image's directors (Image Credit Agreement). Pursuant to the Image Credit Agreement, Williams supplied certain building materials to Image on credit. In 2012, Williams approved a similar credit application by IDH (IDH Credit Agreement). The IDH Credit Agreement was also supported by an all-moneys guarantee (the IDH Guarantee).

The IDH Guarantee, as was the case with the guarantee under the Image Credit Agreement, was provided to Williams via fax and bore the electronically affixed signatures of each of the directors of IDH, purportedly witnessed by IDH's administration manager. The case at first instance, and on appeal, involved an ultimately unsuccessful attempt by Williams to enforce the IDH Guarantee against Mr Crocker.

On the evidence presented at trial and generally accepted by the Court of Appeal, it was held that an unknown person had affixed Mr Crocker's signature both to the IDH Credit Agreement and IDH Guarantee unbeknownst to Mr Crocker.

(c) Decision

(i) Ostensible authority and estoppel

The Court of Appeal, in reference to the High Court's judgment in *Pacific Carriers Ltd v BNP Paribas* (2004) 218 CLR, at paragraph 65 - 66 stated:

"That passage makes it clear that, for there to be a finding of ostensible authority in the present case, it would be necessary for the putative principal (Mr Crocker) in some fashion to have held out to Williams that whoever placed his electronic signature on the relevant documents (and forwarded them to Williams) was authorised by him to do so. The representation need not have been communicated by Mr Crocker to Williams directly (and there is force in the submission that a direct communication would have established actual authority). It could, in an appropriate case, arise out of some omission on his part. However, there needs to have been a representation of authority by Mr Crocker (not the agent who applied the electronic signature), on which Williams relied when supplying goods to IDH on credit, for Mr Crocker to be bound by the guarantee. Once the need for such a representation (in order to found a claim based on ostensible authority) is appreciated, the difficulties in Williams' argument become apparent".

The Court then went on to indicate that there were not sufficient factual grounds to support a finding that Mr Crocker held out to Williams in any relevant way that whomever affixed his electronic signature to the IDH Guarantee was authorised to do so. Williams' arguments in relation to estoppel were dismissed on the same basis.

(ii) Ratification

In relation to the ratification arguments put forward by Williams, the Court of Appeal noted that the primary Judge had correctly articulated the test for knowledge of the principal necessary to ratify the conduct of the agent as "full knowledge of all the material circumstances". Again, on the specific facts of the case, the Court of Appeal held that Mr Crocker did not have the relevant degree of knowledge to have ratified his unknown agent's actions.

(iii) Forgery

The court spent some time addressing submissions by both parties as to whether the affixed signature was in fact a forgery. However, ultimately, the court decided it was unnecessary to reach any conclusion on this point having regard to its findings on ostensible authority and ratification.

6.7 Consideration of fiduciary duties for directors who are on the boards of two competing companies

(By Austin Chen, King & Wood Mallesons)

Edenham Pty Ltd v Meares [2016] WASC 301, Supreme Court of Western Australia, Le Miere J, 22 September 2016

(a) Summary

This case involved an application for summary judgment. In essence, the plaintiff company alleged that the defendants breached their fiduciary duties to the plaintiff company by carrying on business in competition with the company during their time as directors of the company.

Le Miere J considered the facts of the case and dismissed the application for summary judgment on the basis that he did not have a sufficiently high degree of certainty about the outcome of the proceeding. No findings were made as to whether the defendants breached their fiduciary duties owed to the plaintiff company.

(b) Facts

The plaintiff company, Edenham Pty Ltd, is the trustee of the Osprey Unit Trust which was established in 1989. At that time, the plaintiff company as trustee of the trust carried on business as a surveyor and the first and secondment defendants, Alex and Kerry, were the only directors of the plaintiff company. The third defendant company, Premier Holdings was at that time, and has always been, controlled by Alex and Kerry. Premier Holdings has always carried on business as property developers, property investors and project managers.

A number of additional directors were appointed to the board of the plaintiff company from 1994, and after 2012 neither Alex nor Kerry were directors of the plaintiff company. It is common ground that the plaintiff company carried on project management work from 1998 onwards.

In the present case, the plaintiff company argued that Premier Holdings, controlled by Alex and Kerry, carried on business as a project manager of property developments and did so in competition with the plaintiff company. As Alex and Kerry were directors of the plaintiff company at the relevant time, they breached fiduciary duties owed to the plaintiff company and duties under ss. 181, 182 and 191 of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) by acting as directors of Premier Holdings. In addition, Premier Holdings was an accessory and knowingly assisted Alex and Kerry in committing their breaches.

The defendants denied the plaintiff's claims and argued that, among other things:

- there was no conflict of duties because there was no competition between the plaintiff company and Premier Holdings; and
- if there was a conflict, the plaintiff company had consented to that conflict because at the establishment of the business, Alex and Kerry were the only directors and they had given the relevant consents.

(c) Decision

As this cases involved an application for summary judgment, no findings were made as to whether the defendants breached their fiduciary duties.

The test to be applied in a summary judgment application was stated by the *High court in Agar v Hyde* (2000) 201 CLR 522. A summary judgment will only be allowed if there is "a high degree of certainty about the ultimate outcome of the proceeding if it were allowed to go to trial in the ordinary way".

The Court examined the legal principles in relation to director duties discussed below and the relevant evidence provided by both the plaintiff and the defendants and concluded that there is a serious question to be tried. Therefore, the summary judgment application was dismissed.

(i) Director's duties

Le Miere J considered that the plaintiff company's claims concern breaches of fiduciary duty, whether the claims are made under the common law or the Corporations Act. The plaintiffs argued that the defendants breached their fiduciary duties by contravening the conflict rule and the profit rule. The conflict rule states that directors cannot have material personal interests in matters falling within the scope of their service without the company's fully informed consent. The profit rule states that directors cannot use their position for their own possible advantage without the company's fully informed consent.

For the conflict rule, the scope of a director's fiduciary duties will depend on the circumstances. Le Miere J noted that the extent to which the potential of any conflict must be apparent has been subject to different formulations but in essence, a director must not be in a position where there is a real or substantial possibility of a conflict.

For the profit rule, there is no absolute duty on a director to abstain from engaging for his or her own benefit in the same kind of business carried on by the company. However, directors are accountable to the company if they divert business opportunities away from the company and into their own business. The court considered the principles concerning the diversion of business opportunities in *Streeter v Western Areas Exploration Pty Ltd* [No 2] [2011] WASCA 17 and stated that:

- whether a business opportunity is a relevant opportunity for the company depends on the scope of the company's business;
- whether the directors are in a position of conflict depends on whether the directors have a positive duty to acquire or seek to acquire particular business opportunities for the company; and
- whether a director has a duty to acquire a business opportunity for the company may depend on the capacity in which the opportunity came to the director.

Le Miere J examined evidence provided by both the plaintiff company and the defendants and was satisfied that there is evidence to suggest that Premier Holdings carried on business as project managers, where the activities fall within the scope of the business carried on by the plaintiff company. However, as the application was for a summary judgment, Le Miere J did not have a sufficiently high degree of certainty about the outcome of the proceeding to enter judgment for the plaintiff company.

(ii) Defence of consent

In the alternative, the defendants argued that even if they breached their fiduciary duties owed to the plaintiff company, implied consents were given by the plaintiff company due to the fact that the defendants were the only directors of the plaintiff company when the Osprey Unit Trust was established.

The principles for consenting to conflict are:

- a fiduciary will not be liable to account for profits or gains acquired by virtue of their fiduciary position if it can be shown that the principal consented and the consent was given on the basis of a full and frank disclosure of all the material facts;
- the onus of proving fully informed consent is on the fiduciary; and
- consent need not be given expressly.

Le Miere J considered that the principal difficulty confronting the defendants is that the defendants ceased to be the only directors of the plaintiff company in 1994. Le Miere J further quoted the sixth edition of *Equity and Trust in Australia*, Dal Pont, which stated that "shareholder consent cannot be used as a blanket indemnification or exemption on a prospective basis, only for specific absolution for properly disclosed conflicts or profits".

While Le Miere J concluded that the defendants will face difficulties in advancing an argument of informed consent, this defence would not be hopeless at trial.

As a result, the summary judgment application was dismissed.

6.8 Stay of s. 596A examination summons to liquidator following no finding of benefit, a special position held by the liquidator, and abuse of process

(By Alex Moores, DLA Piper)

In the matter of Kimberley Diamond Company Pty Ltd (in liq) [2016] FCA 1016, Federal Court of Australia, General Division, Gleeson J, 16 September 2016

(a) Summary

Kimberley Diamonds Limited (KDL) arranged for the issue of an examination summons under s. 596A of the Corporations Act 2001 No. 50 (Cth) (the Act) to the liquidator of Kimberley Diamond Company Pty Ltd (in liquidation) (KDC). The examination summons was issued in order to investigate the sales and marketing process undertaken in the liquidation. KDL was dissatisfied with the way the liquidator had handled this component of the liquidation specifically and, while not contesting certain components of the overall liquidation, objected to the timing of the process and information provided to the potential bidders.

The Federal Court of Australia (the Court) examined the purpose of the public examinations as well as the extent of the judiciary's power to vary or stay an issued summons. The liquidator argued that the summons was an abuse of process, and that there was insufficient basis or reason given for the summons that did not create a benefit to the public or the liquidation. The Court ultimately found the liquidator's argument to be compelling and stayed the summons, awarding costs to the liquidator.

(b) Facts

KDL is an ASX-listed diamond mining and exploration company which conducts mining and exploration operations. KDC was a subsidiary of KDL until it was placed into voluntary administration. The liquidators, in their then capacity as administrators, formed the view that selling the KDC entity would be the best option for creditors. Several months later, the liquidators reported that despite over twenty expressions of interest in the business, all offers were deemed less beneficial to creditors than if the plant and equipment was sold separately. In addition, the liquidators reported that they had issued a Notice of Disclaimer of Onerous Property in relation to the mining lease for the Ellendale mine site. A statement of position annexed to the report at this time recorded a total deficiency to creditors of approximately $65-$66 million.

Following this report, KDL provided several pieces of evidence to the liquidators in support of their position that had a more effective sale and marketing process been undertaken there would not have been a deficiency as reported, and there may have been a dividend to KDL as a shareholder in KDC. Some of this evidence included a statement from the West Australian Department of Mines and Petroleum (WADMP) that the Ellendale site was a viable resources project, and also statements from a participant in the sale process. The latter included comments that the liquidator allegedly did not provide any technical information or assistance interpreting documents in the dataroom, did not allow site visits, required a bid without allowing negotiation, and imposed a period of "only a couple of weeks" for the assessment period.

KDL applied to ASIC to be granted eligible applicant status in relation to the matter, which was successful given KDL's status as a contributory of KDC. This allowed KDL to issue the summons, as s. 596A of the Act provides that the court is to summon the person in relation to examinable affairs if an "eligible applicant" applies and the person to be summonsed is or was an officer or provisional liquidator of the corporation. KDL argued that on this definition, the summons was valid. The liquidator did not challenge the granting of eligible applicant status and KDL did not challenge the Notice of Disclaimer under s. 568B of the Act. In being granted the eligible applicant status, KDL outlined that its narrow scope of inquiry would relate to two specific areas:

- the inadequacy of the sale process in that the duration was insufficient given unique and international appeal of the site; and
- the conduct of the sale process relating to the defective way information was communicated to potential bidders and the effect of issues raised by the participant in the sales process.

(c) Decision

The Court examined the history of the application of s. 596A of the Act, and that the judicial treatment of the section has shifted from identifying two clear objectives - those being allowing liquidators to gather information and enabling evidence to be obtained that supports criminal charges in a winding up - to a broader approach reading s. 596A in context with other examination powers such as s. 596B. While the application of the section may be appropriate generally, the Court found that it still has power to stay the summons if there is an improper purpose.

(i) The special position of liquidators

The Court premised analysis of arguments in relation to the alleged failing of the liquidator with the principle that the role of liquidator is a highly trusted position, acting as an agent or officer of the corporation and, in some instances, the courts. Liquidators are not subject to a duty to achieve the best possible price for assets in their control. They owe duties of care, diligence and good faith but, provided they act in this nature and in accordance with other duties, they cannot be held liable for obtaining a price for creditors that is later found to have not been the highest available.

A liquidator is not immune from litigation if it is found to have failed to be reasonable and this causes a loss, but there are special provisions relating to liquidators because there is a desire to prevent harassment of the individual and interference with the role. Leave from the court and a prima facie case is at least required to bring action against liquidators for this reason. The Court held that the liquidator will ultimately be a better judge of many commercial decisions than the courts and, even when the decisions take on a legal element, it is not usual that the courts will step in and revise the contemporaneous decisions of liquidators managing holistic and multi-faceted company administrations or liquidations.

(ii) Mandatory examination requiring justification

In analysing the case law in relation to liquidators, the Court held that the mandatory examination of the liquidator should not be permitted to proceed unless there is reason to believe that the examination may fulfil the purpose of s. 596A being to benefit the company, its creditors, members or the public generally. This conclusion is based on the role of the Court in protecting the integrity of the winding up, and in ensuring that the winding up is conducted in a timely and efficient manner. As such, the justification for the examination becomes relevant.

While KDL argued that a s. 596A summons could be issued for exploratory reasons, the Court stated that there is no evidence that there has been fraud, dishonestly, misconduct, conflict of interest, misunderstanding of liquidator's function, flaw of commercial judgment or that any particular difference in the way the liquidation was run would have delivered a more favourable outcome. The statements by WADMP and the participating potential bidder were given little weight in proving the liquidator made incorrect commercial decisions, and they do not give rise to justification for exploratory examination. Generally, there was no *prima facie* case giving the Court concern with the conduct of the liquidators.

(iii) Examining abuse of process

Again studying the historical approach, the Court found that application of the principle is broad, with abuse of process circumstances being "very varied" and needing only to have a result which would be "manifestly unfair to a party" or would "otherwise bring the administration of justice into disrepute among right-thinking people". Notwithstanding the broad application, the court in *Rogers v The Queen* (1994) 181 CLR 251 determined at paragraph 286 that there are generally three categories of abuse of process:

- invoking of a court's processes for an illegitimate or collateral purpose;
- where using the court's procedures would be unjustifiably oppressive to a party; or
- where using the court's procedures would bring the administration of justice into disrepute.

The Court held that, due to the fact that there was no realistic prospect that the examination would have any practical utility, that there is a substantial intrusion into the liquidation by examining the liquidator in the course of his conduct, and that there is no reason to believe that the mandatory examination of the liquidator may provide a benefit to the company, its creditors, its members or the public generally, the summons was held to be an abuse of process and stayed by the Court.

6.9 ASIC investigation not enough to find criminal prosecution 'on the cards' for company director

(By Will Foxcroft, Clayton Utz)

Citation Resources Ltd v Landau [2016] FCA 1114, Federal Court of Australia, McKerracher J, 13 September 2016

(a) Summary

McKerracher J decided two applications filed in a proceeding against Mr Landau (Landau) by Citation Resources Ltd (Citation) alleging breach of director's duties for the misappropriation of company funds from an account he opened for Citation. Landau had also been under investigation by ASIC for suspected contraventions of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) and the Criminal Code Act Compilation Act 1913 No. 28 (WA).

Landau applied for a stay of proceedings on the grounds that his right of silence would be infringed and that his financial resources would not enable him to defend criminal and civil proceedings at the same time. The application for a stay was dismissed as McKerracher J determined that criminal prosecution was not "on the cards". Citation sought a discovery order for documents relating to the account and misappropriated funds. The discovery application was dismissed as disclosure of such documents would place Landau at increased risk of prosecution.

(b) Facts

Citation has commenced proceedings in the Federal Court against Landau, a former director. Citation alleges that on 1 April 2015, Landau caused a Westpac bank account to be opened in the name of the company with two employees having authority to make transactions. Landau was listed as an approver for the account. Citation alleges breach of director's duties by Landau through misappropriation of approximately $2.14 million of company funds from the account between June 2015 and February 2016. It alleges that the payments were unauthorised and to third parties who had no entitlement to payment from the company. Citation seeks a s. 1317E declaration of contravention, a civil penalty provision of the the Corporations Act, for breach of his director's duties.

The present proceeding concerned an application for limited discovery by Citation and an application for a stay of proceedings by Landau.

(c) Decision

Both applications were dismissed.

(d) Reasoning

(i) Discovery

The application for discovery was made pursuant to rl 20.14 of the Federal Court Rules 2011 No. 134 (Cth). Rule 20.14 provides that if the court gives an order for discovery, documents that are directly relevant, that the party is aware of after a reasonable search and are, or have been in the party's control must be given.

Citation sought documents relating to the opening and operation of the Westpac account.

At [28], McKerracher J cited the formulation of Ashley JA in *Gemmell v Le Roi Homestyle Cookies Pty Ltd (in liq)* (2014) 46 VR 583 at 112:

"the appellants may successfully invoke the privilege against potential self-incrimination if there is a real and appreciable risk that a pleading or the giving of discovery might expose them to increased jeopardy of criminal prosecution"

At [30], his Honour notes that in the present circumstances, even an affidavit disclosing whether documents exist could increase Landau's "jeopardy" if, for example, the document related to the authority required for the payments. If no such document existed, it would imply that proper authority had not been obtained.

McKerracher J held that the increase in jeopardy to Landau was "relatively obvious" and the application for limited discovery was dismissed.

(ii) Stay of proceedings

Landau's application for a stay of proceedings was brought on the basis that there is a real prospect of a criminal prosecution against him, arising from the same facts subject of the civil proceeding.

At [37], his Honour quotes Wootten J in *McMahon v Gould* (1982) 7 ACLR 202 at 206 (McMahon), describing the various factors for consideration in an application for a stay of civil proceedings where there is a risk of criminal prosecution. His Honour goes on to state that subsequent to McMahon, a majority of the High Court in *Reid v Howard (No 2)* (1995) 184 CLR 1 emphasised the importance of the privilege against self-incrimination, describing it at [11] as a "bulwark of liberty" and a "basic and substantive common law right".

McKerracher J stated that the real point of dispute between the parties is whether criminal prosecution is "on the cards", an expression coined in *Australian Securities and Investments Commission v HLP Financial Planning (Aust) Pty Ltd* (2007) 164 FCR 487 at [59]. The phrase has been interpreted to mean "reasonably possible" or a "reasonable possibility": *Websyte Corporation Pty Ltd v Lee (No 2)* [2012] FCA 562 at [117]. The expression does not require that a decision to prosecute has been made or a decision to send a brief to a prosecuting authority has been made.

The factors in favour of a criminal prosecution being 'on the cards' were:

- ASIC had obtained a freezing order over Landau's assets;
- Landau was subject to a travel restraint obtained by ASIC;
- ASIC had investigated and examined Landau in respect of the same subject matter as the civil proceeding;
- the allegations are serious; and

- an ASIC officer had sworn to the fact that Landau may face criminal charges.

Two further factors in favour of a stay were that Landau will not have sufficient financial assets to defend both civil and criminal proceedings, and that Citation would be unlikely to suffer prejudice if proceedings were stayed.

Despite the factors listed above, McKerracher J declined to stay proceedings in light of the following:

- the circumstances giving rise to the risk of criminal prosecution also involved two other companies;
- Citation's application for discovery was refused with no positive defence pleaded by Landau;
- it is unlikely Landau would be subject to significant costs prior to trial given his defence; and
- Citation's entitlement to bring its case to court was significant.

There was no order as to costs as McKerracher J considered that the applications had taken a similar amount of time.

(e) Conclusion

This case serves as a reminder of the court's reluctance to stay civil proceedings against company directors and that criminal prosecution being "on the cards" is not an easy threshold to meet.

6.10 Provisional liquidators appointed in light of numerous suspected contraventions of the Corporations Act

(By Andrew Robertson, Ashurst)

Australian Securities and Investments Commission v Uglii Corporation Limited [2016] FCA 1099, Federal Court of Australia, Davies J, 8 September 2016

(a) Summary

The Federal Court found in favour of ASIC's application for the appointment of provisional liquidators to the defendant companies under s. 472(2) of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act). Findings, which had emerged from two separate investigations, of six suspected contraventions of the Corporations Act by the companies, including trading while insolvent, had led ASIC to file a winding up order against the companies. In making the present order under s. 472(2), Davies J held that there was a reasonable prospect that the winding up order would be granted, on grounds of insolvency and the just and equitable ground.

(b) Facts

Since March 2015, ASIC had undertaken two investigations into the defendant companies. The first was in regards to suspected Corporations Act contraventions by Uglii Corporation, one of its former directors, and a current director of each of the companies. The second focused on contraventions of ss. 319(1), 320(1), 558G, 727, 1041E and 1041G by the companies.

The two investigations revealed numerous suspected contraventions of the Corporations Act by the companies, including the breach:

- of ss. 319 and 320 for failure to lodge end of year financial reports and half year financial reports with ASIC;
- of s. 1041H for making false or misleading statements in relation to sale of shares;
- of ss. 727 and/or 734 for failing to provide a disclosure document when offering securities in ads for sale and advertising that offer;
- of s. 201A(2) for only having two directors registered for a public company, rather than the prescribed minimum of three; and
- of s. 588G for trading while insolvent.

In response to these investigations, ASIC applied to wind up each of the companies under ss. 459B and 464 for insolvency, and alternatively, under s. 461(1)(k) on the just and equitable ground.

ASIC have subsequently applied for the appointment of a provisional liquidator under s. 472(2), which provides that the Court may appoint an official liquidator provisionally at any time after the filing of a winding up application and before the making of a winding up order or, if there is an appeal against a winding up order, before a decision in the appeal is made.

Relying on the suspected contraventions, ASIC submitted there is evidence that first, each of the companies is insolvent, and second, there is a lack of confidence in the controllers of the companies and the manner in which they have managed the entities and raised funds from investors.

(c) Decision

Davies J accepted both grounds upon which ASIC had relied. In regards to insolvency, Davies J concluded that the evidence strongly suggests that the companies were not solvent, and did not accept that the defendant's patents had substantial value that could impact cash flow projections. The defendants were unable to refute the "cogent evidence" of insolvency.

Davies J also held that there was a reasonable prospect that the winding up order would ultimately be made on the just and equitable ground. The defendants had not contested their failure to lodge financial reports, to provide disclosure documents to investors and to have at least the minimum number of directors. The four newsletters issued by the defendants were also found to strongly indicate misleading and deceptive conduct in contravention of s. 1041H.

The defence submitted that each individual infraction would independently justify a winding up order and that the existing auditors would be as well placed to address insolvency and complete the audits of the accounts. However, Davies J concluded that there was no reason to have confidence that the directors will do what is required to enable the auditors to complete their task.

Generally, a provisional liquidator should not be appointed if any less intrusive measure will satisfactorily address the circumstances: Australian Securities and Investments Commission v Tax Returns Australia Dot Com Pty Ltd [2010] FCA 715 and [86]. Davies J held that there was no alternative measure in this case. The suspected contraventions were described as "not just procedural lapses" and Davies J rejected the submission that the contraventions were not sufficiently serious to warrant the appointment of a provisional liquidator.

7. Contributions

If you would like to contribute an article or news item to the Bulletin, please email it to: law-cclsr@unimelb.edu.au.

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