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info.regulatory@saiglobal.com

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Legislation Hotline

Editor: Professor Ian Ramsay, Director, Centre for Corporate Law and Securities Regulation

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Detailed Contents

1. Recent Corporate Law and Corporate Governance Developments

1.1 Government to review extension of unfair contract terms to small business

23 October 2018 - The Australian Government has announced it will review the effectiveness of protections for small business against unfair contract terms (UCTs). The UCT protections for small business have been in place since 12 November 2016.

The Treasury Legislation Amendment (Small Business and Unfair Contract Terms) Act 2015 No. 147 (Cth) legislated to:

- extend the consumer UCT protections in the Australian Consumer Law (the ACL) and the Australian Securities and Investments Commission Act 2001 No. 51 (Cth) (the ASIC Act) to small business contracts that meet the prescribed criteria; and
- make provision for exempting certain small business contracts from the operation of the legislation, where those contracts are subject to prescribed laws that are deemed equivalent to the UCT protections in the ACL or the ASIC Act, and which are enforceable.

The UCT protections currently apply to all small business contracts that meet the following criteria:

- the contract is a standard form contract;
- at the time the contract is entered, at least one party to the contract is a business that employs fewer than 20 persons; and
- the upfront price payable under the contract does not exceed $300,000 or $1 million if the contract runs for more than 12 months.

The Government has recently legislated to give the Australian Competition and Consumer Commission (the ACCC) and ASIC stronger powers to protect small businesses from UCTs. Under the Treasury Laws Amendment (Australian Consumer Law Review) Act 2018 No. 132 (Cth) which passed the Parliament on 18 October 2018, the regulators will have investigative powers to assess whether a term in a standard form contract may be unfair.

The review will commence in November 2018 and report to the Government by 1 February 2019. The review will be conducted by the Australian Treasury.

1.2 APRA sets out BEAR expectations

17 October 2018 - The Australian Prudential Regulation Authority (APRA) has released the information paper Implementing the Banking Executive Accountability Regime to assist authorised deposit-taking institutions (ADIs) to meet their obligations under the Banking Executive Accountability Regime (the BEAR).

The BEAR, which establishes heightened standards of accountability among ADIs and their most senior executives and directors, came into force for the largest banks from 1 July 2018. It will apply to all other ADIs from 1 July 2019. The regime was established under legislation and is administered and enforced by APRA.

The information paper, based on APRA's experience in implementing the regime for the largest banks, is aimed at assisting all other ADIs prepare to implement the BEAR, and helping the largest ADIs refine and embed the regime.

It clarifies APRA's expectation of how an ADI can effectively implement the accountability regime on matters including:

- identifying and registering accountable persons;
- creating and submitting an accountability statement for each accountable person, and an accountability map for the ADI;
- establishing a remuneration policy requiring that a portion of accountable persons' variable remuneration be deferred for a minimum of four years, and reduced commensurate with any failure to meet their obligations; and
- notifying APRA of any accountability-related changes or breaches of accountability obligations.

The information paper also includes questions and answers based on some of the issues commonly raised by ADIs during implementation. APRA will address enforcement-related issues, including the disqualification of accountable persons and civil penalties under the BEAR, in a subsequent paper.

1.3 UK financial authorities publish discussion papers on climate change

15 October 2018 - The UK Financial Conduct Authority (the FCA) and the UK Prudential Regulation Authority (the PRA) have published discussion papers on climate change and green finance.

The FCA Discussion Paper: Climate change and green finance sets out how the impacts of climate change are relevant to the FCA's statutory objectives of protecting consumers, protecting market integrity and promoting competition.

The Discussion Paper seeks input on four areas in which the FCA considers a greater regulatory focus is warranted:

- climate change and pensions, ensuring that those making investment decisions take account of risks including climate change;
- enabling competition and market growth for green finance;

- ensuring that disclosures in capital markets appropriately give adequate information to investors of the financial impacts of climate change; and
- the scope for the introduction of a new requirement for financial services firms to report publicly on how they manage climate risks

The PRA Consultation Paper 23/18: Enhancing banks' and insurers' approaches to managing the financial risks from climate change seeks views on a draft supervisory statement (the draft SS) on banks' and insurers' approaches to managing the financial risks from climate change.

The draft SS is intended to complement existing policy material and inform compliance with existing requirements in legislation and PRA rules. The PRA's desired outcome is that firms take a strategic approach to managing the financial risks from climate change, taking into account current risks, those that can plausibly arise in the future, and identifying the actions required to mitigate current and future financial risks.

The draft SS sets out the PRA's proposed expectations concerning how firms:

- embed the consideration of the financial risks from climate change in their governance arrangements;
- incorporate the financial risks from climate change into existing risk management practice;
- use (long-term) scenario analysis to inform strategy setting and risk assessment and identification; and
- develop an approach to disclosure on the financial risks from climate change.

1.4 Consultation on Corporate Collective Investment Vehicle- tranche three

12 October 2018 - The government has released for public consultation Tranche 3 of the *Treasury Laws Amendment (Corporate Collective Investment Vehicle) Bill 2018 (Cth)* (the CCIV) and related explanatory materials.

The CCIV is an investment vehicle with a corporate structure, with the additional consumer protection of a depositary for retail funds which is responsible for the oversight of administrative functions undertaken by the fund. A single CCIV can offer multiple products and investment strategies within the same vehicle.

The government previously released two tranches of the draft Bill for public consultation. Consultation on Tranche 1 was held from 13 June to 18 July 2018. Consultation on Tranche 2 was held from 19 July to 10 August 2018.

Tranche 3 includes:

- the independence requirement for the depositary, whose responsibility it is to safeguard the fund's assets and oversee some of the activities of the fund;
- arrangements and reconstructions, receivership and winding up;
- deregistration of sub-funds and CCIVs;
- takeovers, compulsory acquisitions and buy-outs, and disclosure requirements; and
- other consequential amendments to Chapter 9 of the Corporations Amendment (Asia Region Funds Passport) Act 2018 No. 61 (Cth), the Australian Securities and Investments Commission Act 2001 No. 51 (Cth) and the Personal Property and Securities Act 2009 No. 130 (Cth) to accommodate the new CCIV regime.

1.5 FSB sets out potential financial stability implications from crypto-assets

10 October 2018 - The Financial Stability Board (the FSB) has published the report Crypto-asset markets: Potential channels for future financial stability implications. This report sets out the analysis behind the FSB's assessment of the potential implications of crypto-assets for financial stability. The report follows up on the initial assessment set out in the FSB Chair's March 2018 letter to G20 Finance Ministers and Central Bank Governors, and the summary of the work of the FSB and standard-setting bodies on crypto-assets the FSB published in July 2018.

The report includes an assessment of the primary risks present in crypto-assets and their markets, such as low liquidity, the use of leverage, market risks from volatility, and operational risks. Based on these features, crypto-assets lack the key attributes of sovereign currencies and do not serve as a common means of payment, a stable store of value, or a mainstream unit of account.

Based on the available information, crypto-assets do not pose a material risk to global financial stability at this time. However, vigilant monitoring is needed in light of the speed of market developments. Should the use of crypto-assets continue to evolve, it could have implications for financial stability in the future.

Such implications may include:

- confidence effects and reputational risks to financial institutions and their regulators;
- risks arising from direct or indirect exposures of financial institutions;
- risks arising if crypto-assets became widely used in payments and settlement; and
- risks from market capitalisation and wealth effects.

Crypto-assets also raise several broader policy issues, such as:

- the need for consumer and investor protection;
- strong market integrity protocols;
- anti-money laundering and combating the financing of terrorism (AML/CFT) regulation and supervision, including implementation of international sanctions;
- regulatory measures to prevent tax evasion;
- the need to avoid circumvention of capital controls; and
- concerns relating to the facilitation of illegal securities offerings.

1.6 Legislation to reform regulation of co-ops, mutuals and customer owned banks

4 October 2018 - The government has released draft legislation to provide a definition for a mutual entity in the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) and to clarify the uncertainty around the demutualisation provision of Part 5 Schedule 4 of the Corporations Act.

The legislation forms the first phase of a two-phased approach to the implementation of the recommendations of the inquiry into Reforms for Cooperatives, Mutuals and Member-owned Firms, conducted by Greg Hammond OAM.

The proposed legislation provides a definition of a mutual entity to recognise the sector in the Corporations Act and to determine which mutual entities will be able to raise capital through the issuance of mutual capital instruments, to be implemented in the second phase.

The proposed legislation will also address the uncertainty in Part 5 Schedule 4 of the Corporations Act to enable mutually-owned Australian ADIs to raise capital by providing that the enhanced disclosure requirements are only applicable where an entity no longer meets the definition of a mutual entity.

1.7 World Federation of Exchanges publishes five sustainability principles for member exchanges

4 October 2018 - The World Federation of Exchanges (the WFE), the global industry group for exchanges and central counterparty clearing (CCPs), has published a set of five WFE Sustainability Principles (the Principles) that constitute a formal declaration by the WFE and its membership to take on a leadership role in promoting the sustainable finance agenda.

The five WFE Principles are:

- Exchanges will work to educate participants in the exchange ecosystem about the importance of sustainability issues: This education (capacity building) is designed to build an understanding and appreciation of the impact of ESG issues on the long-term health and performance of financial markets, and the important role that markets can play in enabling a transition to a more just and sustainable world. Capacity building may be done independently or in collaboration with third parties, and may take the form of seminars, courses, case-studies, information sharing among market participants, and the publication of research.;
- Exchanges will promote the enhanced availability of investor relevant, decision-useful ESG information: This could include issuing disclosure guidance to assist issuers, and organising information-sharing/training sessions for issuers around ESG reporting. Exchanges may implement disclosure requirements in phases, beginning with voluntary disclosure, and moving to mandatory/comply or explain disclosure. To ensure the quality of the disclosure, exchanges should encourage disclosure in accordance with widely accepted international standards and against science-based indicators.;
- Exchanges will actively engage with stakeholders to advance the sustainable finance agenda: This could range from engagement with regulators and policymakers to promote the creation of the necessary enabling environment, to contributing to the development of consensus around a sustainability taxonomy, and collaborating with other market participants to develop products that advance the sustainable finance agenda.;
- Exchanges will provide markets and products that support the scaling-up of sustainable finance and reorientation of financial flows: Exchanges can contribute to the mobilisation and reorientation of sustainable finance by, for example, creating frameworks for the listing of green, social and sustainability bonds; developing sustainability indices; and working with third parties to develop sustainability ratings.; and
- Exchanges will establish effective internal governance and operational processes and policies to support their sustainability efforts: Exchanges commit to taking steps to better embed sustainability into their governance, strategy and organisational structures, to support the shift into a more sustainable financial system. This could include: incorporating ESG disclosure into the exchanges' own sustainability reporting; educating staff about sustainability risks and opportunities; and establishing board and senior management oversight of the exchange's own management of ESG risks and opportunities.

1.8 IAASB modernises auditing of accounting estimates in support of audit quality

3 October 2018 - The International Auditing and Assurance Standards Board (the IAASB) has released International Standard on Auditing (ISA) 540 (Revised), its revised standard for the audit of accounting estimates and related disclosures.

This revised standard is the first to be completed as part of the IAASB's broader program *Addressing the Fundamental Elements of an Audit* and is an important part of the IAASB's efforts to improve audit quality globally.

Some of the significant revisions include:

- an enhanced risk assessment that requires auditors to consider complexity, subjectivity and other inherent risk factors in addition to estimation uncertainty which will drive auditors to think more deeply about the risks inherent to accounting estimates;
- a closer link between the enhanced risk assessment and the methods, data and assumptions used in making accounting estimates, including the use of complex models;
- specific material to show how the standard is scalable to all types of accounting estimates and
- emphasis on the importance of applying appropriate professional scepticism when auditing accounting estimates to foster a more independent and challenging sceptical mindset in auditors.

The revised standard becomes effective for financial statement audits for periods beginning on or after 15 December 2019.

1.9 World Federation of Exchanges published report into global SME market

2 October 2018 - The WFE has published its report An Overview of WFE and SME Markets.

The WFE collaborated with the World Bank in 2015 and 2016 to highlight stock exchange activity in this area. This research identified points of commonality and difference in approaches to small and medium enterprise (SME) markets, with the intention of providing policymakers and market operators with insights into key aspects to be considered when designing these types of markets.

This latest report (and the ancillary database *WFESME Markets - Key Datapoints*) builds on this previous research in the following ways:

- it looks at a broader universe of WFE member exchange offerings, rather than focusing on a few markets;
- it uses updated (as at end 2017) data and information to profile the range of SME markets across the WFE membership; and
- it showcases recent innovations in exchange-supported SME finance offerings, beyond traditional equity markets.

This report is based on quantitative and qualitative information of 33 SME markets (three in the Americas,14 in the Asia-Pacific region and 16 in EMEA) at 29 exchanges across the globe.

1.10 Modernising business registers and director identification numbers legislation

1 October 2018 - The government has released for consultation draft legislation aimed at modernising the Australian Business Register (the ABR) and the 31 Australian Securities and Investments Commission (ASIC) business registers.

In the 2018-2019 Budget, the government announced it will modernise the ABR and the 31 ASIC business registers onto a single platform that will be administered by the Australian Business Registrar within the Australian Taxation Office (the ATO).

The current legislative framework that covers ASIC's business registers has not kept up with digital technology and restricts ASIC's ability to interact with clients in their preferred manner. It also does not allow ASIC registry functions to be administered by another agency.

This draft legislation would allow the appointed Registrar (or Registrars) the ongoing flexibility to adapt and respond to changes in technology to improve the user experience and simplify the way clients interact with government business registers.

The draft legislation to modernise the business registers will be consulted on in two parts. The first part includes the core provisions that facilitate a modern government registry regime plus the bulk of the referrals of functions and consequential changes from other Acts. The second part includes the remainder of the referrals of functions and consequential changes.

The amendments proposed by the government will allow ASIC's registry functions to be shifted to the Australian Business Registrar. ASIC will continue to administer all of its regulatory functions under the current ASIC laws.

Also included in the draft legislation is a legal framework for the introduction of Director Identification Numbers (DINs). The draft legislation sets out who will be required to obtain a DIN, the obligations associated with a DIN, the consequences of not meeting those obligations and how DINs will be administered. Details on specific implementation options are currently being considered and will be separately consulted on separately

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1.11 Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry - Interim Report

28 September 2018 - The Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (the Royal Commission) Interim Report, consisting of the volumes listed below, was tabled in Parliament on 28 September 2018:

- Volume 1;
- Volume 2 - Case Studies; and
- Volume 3 - Appendices.

The interim report covers a range of issues identified across the first four rounds of hearings held in Melbourne, Brisbane and Darwin between March and July 2018 and included consumer lending, financial advice, small and medium enterprises, agricultural lending financial issues in remote communities, regulation and regulators, and causes of misconduct.

Additional topics, including superannuation and insurance, considered in hearings held in August and September 2018, will be covered in the final report due by 1 February 2019.

Key issues related to misconduct in the executive summary include:

- "The Commission's work, so far, has shown conduct by financial services entities that has brought public attention and condemnation. Why did it happen? Too often, the answer seems to be greed - the pursuit of short term profit at the expense of basic standards of honesty."
- "When misconduct was revealed, it either went unpunished or the consequences did not meet the seriousness of what had been done. The conduct regulator, ASIC, rarely went to court to seek public denunciation of and punishment for misconduct. The prudential regulator, APRA, never went to court. Much more often than not, when misconduct was revealed, little happened beyond apology from the entity, a drawn out remediation program and protracted negotiation with ASIC of a media release, an infringement notice, or an enforceable undertaking that acknowledged no more than that ASIC had reasonable 'concerns' about the entity's conduct. Infringement notices imposed penalties that were immaterial for the large banks. Enforceable undertakings might require a 'community benefit payment', but the amount was far less than the penalty that ASIC could properly have asked a court to impose."

1.12 Task Force report shows momentum building for climate-related financial disclosures

26 September 2018 - The Task Force on Climate-related Financial Disclosures (the TCFD) established by the FSB has released its 2018 Status Report, providing an overview of the extent to which companies in their 2017 reports included information aligned with the core TCFD recommendations published in June 2017. The report also provides information to support preparers of disclosures in implementing the TCFD recommendations.

The TCFD surveyed disclosures of over 1,700 firms from diverse sectors with broad geographical representation.

It found that:

- the majority of the firms surveyed disclose information aligned with at least one of the TCFD recommended disclosures;
- while many companies describe climate-related risks and opportunities, few disclose the financial impact of climate change on the company;
- a minority of companies disclose forward-looking climate targets or the resilience of their strategies under different climate-related scenarios, including a 2°C or lower scenario, which is a key area of focus for the TCFD;
- disclosures vary widely across industries, for example, more non-financial companies reported their climate-related metrics and targets than did financial companies (however, financial companies were more likely to disclose how they had embedded climate risk into overall risk management); and
- disclosures are often made in sustainability reports or spread across financial filings, annual and sustainability reports.

The TCFD has announced that the number of firms supporting the TCFD recommendations has grown to over 500, with market capitalisations of over USD $7.9 trillion, and including financial firms responsible for assets of nearly USD $100 trillion. This compares with 100 firms when the recommendations were launched in June 2017. The FSB has asked the TCFD to publish a further status report in June 2019 which will allow for analysis of disclosures made in 2018 financial reports.

1.13 Reforms to strengthen penalties for corporate and financial sector misconduct

24 October 2018 - The government has introduced into Parliament the Treasury Laws Amendment (Strengthening Corporate and Financial Sector Penalties) Bill 2018 (Cth).

The Bill seeks to:

- update the penalties for certain criminal offences in ASIC-administered legislation;
- introduce ordinary criminal offences that sit alongside strict and absolute liability offences;
- significantly increase the financial penalties for civil contraventions and give courts discretion to strip contraveners of their ill-gotten gains in civil penalty proceedings;
- modernise and expand the civil penalty regime by making a wider range of offences subject to civil penalties;
- harmonise and expand the infringement notice regime;
- introduce a new test that applies to all dishonesty offences under the Corporations Act 2001 No 50 (Cth); and
- ensure the courts prioritise compensating victims over ordering the payment of financial penalties.

The reforms implement some of the recommendations of the ASIC Enforcement Review Taskforce. The Taskforce was established to review ASIC's enforcement regime. The Taskforce provided its recommendations in a report to the government in December 2017.

1.14 Review of retail payments regulation: Stored-value facilities

24 September 2018 - The Council of Financial Regulators (the CFR) has released an Issues Paper, Review of Retail Payments Regulation: Stored-value Facilities, for public consultation.

The Issues Paper is part of a CFR review of the regulatory framework for stored-value facilities, such as purchased payment facilities. The review will also consider the operation of a number of other aspects of the regulation of retail payments service providers that may have the potential to be improved or clarified.

In broad terms, the review has the following objectives:

- to identify opportunities to simplify the regulatory framework for stored-value facilities;
- to ensure that regulation does not pose an undue obstacle to innovation and competition, while maintaining appropriate levels of consumer protection and system-wide safety;
- to identify any changes necessary to enable regulation to adapt to recent and prospective developments in the payments market, including those associated with advances in technology and new participants;
- to identify opportunities to improve the "competitive neutrality" of regulation; and

- to improve the transparency and clarity of regulation, from the perspective of regulated entities, potential new entrants, and consumers and other users.

1.15 Corporations Amendment (Crowd-sourced Funding for Proprietary Companies) Act

21 September 2018 - The Australian Parliament has passed the Corporations Amendment (Crowd-sourced Funding for Proprietary Companies) Act 2018 No.106 (Cth), which amends the Corporations Act 2001 No. 50 (Cth). The amending Act extends the CSF regime to proprietary companies to allow these companies to access an alternative form of finance with additional obligations.

The amendments extend the CSF regime to proprietary companies by:

- expanding the eligibility for the CSF regime in s. 738H to proprietary companies that meet eligibility requirements;
- providing that proprietary companies with shareholders who acquire shares through a CSF offer are not subject to the takeovers rules;
- adding special investor protection provisions for proprietary companies accessing the CSF regime; and
- removing the temporary corporate governance concessions in the Corporations Amendment (Crowd-sourced Funding) Act 2017 No. 17 (Cth) for proprietary companies that convert to or register as public companies to access the CSF regime.

The special investor protection provisions that will apply to proprietary companies accessing the CSF regime include requirements to:

- maintain a minimum of two directors;
- prepare annual financial and directors' reports in accordance with accounting standards;
- have their financial reports audited once they raise $3 million or more from CSF offers; and
- comply with the existing related party transaction rules that apply to public companies.

1.16 Report outlines keys to sound governance

20 September 2018 - Effective governance is the outcome of a mosaic of organisational policies, processes, and cross-functional interactions, according to a new report from the Institute of Internal Auditors (the IIA) and the International Federation of Accountants (IFAC).

The report, United, Connected and Aligned - How the Distinct Roles of Internal Audit and the Finance Function Drive Good Governance**,** examines the roles both internal audit and the finance function play in maintaining a sound system of corporate governance.

The report identifies several key requirements for effective governance, including:

- an ethical corporate culture that empowers effective leaders throughout the organisation to carry out good governance processes;
- effective communication and collaboration among the various roles; and

- requisite competencies for internal audit and the finance and accounting functions to earn stakeholder support and respect.

1.17 IOSCO issues policy measures to protect investors of OTC leveraged products

19 September 2018 - The Board of the International Organization of Securities Commissions (IOSCO) has issued a final report providing measures for securities regulators to consider when addressing the risks arising from the marketing and sale of over-the-counter (OTC) leveraged products to retail investors.

Simultaneously, the Board issued a public statement on the risks of binary options and the response of regulators for mitigating the risks and harm to retail investors transacting in these products.

The Report on Retail OTC Leveraged Products includes three complementary toolkits containing measures aimed at increasing the protection of retail investors who are offered OTC leveraged products, often on a cross-border basis. The report covers the marketing and sale of rolling-spot Forex contracts, contracts for differences (CFDs) and binary options.

The toolkits set out guidance for regulators on:

- policy measures that can help to address the risks arising from the marketing and sale of OTC leveraged products by intermediaries;
- educating investors about the risks of OTC leveraged products and the firms offering them; and
- enforcement approaches and practices to mitigate the risks posed by unlicensed firms offering the products.

Retail investors typically use these products to speculate on the short-term price movements in a given financial underlying. Typically, the products are offered through online trading platforms - often through aggressive or misleading marketing campaigns. Most retail investors trading in these complex products lose money.

1.18 IOSCO guidance addresses conflicts of interest and conduct risks in equity capital raising

18 September 2018 - IOSCO has published guidance to help its members address conflicts of interest and associated misconduct risks that may arise and undermine the equity capital raising process.

Conflicts of interest and associated conduct risks stemming from the role of intermediaries can harm the integrity and efficiency of the equity capital raising process, damage investor confidence and weaken capital markets as an effective vehicle for issuers to raise funding. To help regulators identify and address these risks, IOSCO has published the final report on Conflicts of interest and associated conduct risks during the equity capital raising process, which sets out guidance for regulators to address conflicts of interests that may occur when intermediaries manage an equity securities offering.

The report details the key stages of equity capital raising where the role of intermediaries might give rise to conflicts of interest that compromise the integrity and efficiency of the process.

The guidance comprises eight measures which address:

- conflicts of interest and pressure on analysts during the formation of their views on an issuer in the pre-offering phase of a capital raising;
- conflicts of interest during the allocation of securities;
- conflicts of interest and conduct risks in the pricing of securities offerings; and
- conflicts of interest and conduct risks stemming from personal transactions by staff employed within firms managing a securities offering.

The guidance sets standards of conduct for market intermediaries in the equity capital raising process.

Implementation of the guidance is expected to materially improve the equity raising process, which includes enhancing:

- the range and quality of timely information that is made available to investors during the process;
- the transparency of allocations; and
- the efficiency and integrity of the overall process, boosting investor confidence and rendering capital markets a more effective channel to raise financing.

This report is the first stage of IOSCO's work to examine conflicts of interest and associated conduct risks in the capital raising process. The second phase will consider conflicts of interest and associated conduct risks during the debt capital raising process.

1.19 Markets Committee analyses changes in fast-paced electronic markets

17 September 2018 - A report by the Markets Committee of the Bank for International Settlements shows trading in foreign exchange and other fast-paced electronic markets is increasingly spread across a range of platforms, with non-bank intermediaries, most notably principal trading firms, gaining a stronger foothold. In addition, access to data and data-centric technologies increasingly defines competitive and market structure changes.

The report, Monitoring of fast-paced electronic markets, analyses major developments in the evolution of market structure and their implications for central banks. Market monitoring is a core part of central bank activities for operational purposes and to help fulfil their financial stability mandates.

The report highlights three key structural trends:

- trading is increasingly fragmented across a range of new venues, while the frequency of activity and speed of information flows have accelerated significantly, especially in foreign exchange markets;
- liquidity provision has become more concentrated among the largest banks, as smaller players resort to an agency model of market-making or exit the business altogether (at the same time, a new set of non-bank intermediaries, most notably principal trading firms, have strengthened their positions); and
- greater electronification has led to the commoditisation of large quantities of high-frequency data.

As many central banks participate actively in fast-paced electronic markets, for example, when implementing monetary policy, they are adapting their approaches to market monitoring. This includes the range of participants with whom they engage, the types of data collected, and the tools and technologies used.

The report points to an overall trend among central banks towards greater usage of high-frequency, transaction-level data. Monitoring market conditions in near time using such data can support monetary policy implementation and foreign exchange reserves management. Over the long term, such monitoring can serve financial stability purposes, for example, by allowing a better understanding of structural trends or aiding the analysis of specific events such as recent "flash crashes".

1.20 Research shows that more companies should treat diversity as part of business strategy

17 September 2018 - The majority of the UK's largest companies have adopted policies on boardroom diversity but their reporting to stakeholders needs to improve. Research entitled Board Diversity Reporting conducted for the Financial Reporting Council (the FRC) by the University of Exeter Business School shows that only 15% of FTSE100 companies fully complied with the UK Corporate Governance Code's provision on diversity reporting by describing their policy on diversity, the process for board appointments, their objectives for implementing the policy, and progress on achieving them.

The FRC's analysis shows that FTSE 350 companies' approaches to diversity are wide ranging. While some do demonstrate a deeper understanding of diversity as an issue of strategic importance, the great majority appear to treat reporting as a compliance exercise, suggesting a lack of commitment.

The revised *UK Corporate Governance Code*, which takes effect from 1 January 2019, requires improved reporting on diversity. It calls on boards to include in their annual reports a description from their nomination committee of how they have applied the company's diversity policy including how this links to progress on achieving company objectives.

The report provides a snap shot of diversity reporting across the FTSE 350 and identifies examples that lead the way in terms of quality and approach.

The key findings of the research include:

- 98% of FTSE 100 and 88% of FTSE 250 companies have a policy on board diversity, a considerable improvement since 2012 when this was first included in the *UK Corporate Governance Code*;
- just 15% of FTSE 100 companies report against all four measures stated within provision B.2.4 of the current *UK Corporate Governance Code*; and
- some companies are embracing the spirit of diversity in their narrative reporting but many need to develop a clearer strategy to drive greater diversity at senior management level.

1.21 Parliamentary Committee review of ASIC annual report

10 September 2018 - The House of Representatives Standing Committee on Economics (the Committee) has published its Review of the Australian Securities and Investments Commission Annual Report 2017.

The matters dealt with in the Committee's report include:

- ASIC's performance and lessons learnt;
- recent measures to strengthen ASIC;
- conflicts of interest in the financial sector;
- mortgage broker commissions;

- consumer redress; and
- surveillance and enforcement.

In the Committee Chair's Foreword, it is stated:

> "ASIC needs to be tougher. Australians expect the big banks and others to fear their regulator. There have been too many examples where ASIC has not adequately penalised those it regulates. The heavy reliance on enforceable undertakings, for example, rather than seeking court-imposed penalties, has not met community expectations.".

1.22 New Centre for Corporate Law research publications

Members of the Centre for Corporate Law and Securities Regulation at Melbourne Law School have recently published the following research publications:

- Depositor Preference and Deposit Insurance Schemes - Challenges for Regulatory Convergence and Regulatory Coordination in Asia (by Angus Chen, Andrew Godwin and Ian Ramsay);
- Social Impact Bonds in Australia (by Ian Ramsay and Corinne Tan);
- Equity Crowdfunding in Australia and New Zealand (by Steve Kourabas and Ian Ramsay);
- Harmful Phoenix Activity and Disqualification from Managing Corporations: An Unenforceable Regime? (by Jasper Hedges, Helen Anderson, Ian Ramsay and Michelle Welsh); and
- Is a Conflict of Interest under the General Law the same as a Material Personal Interest under the Corporations Act? (by Rosemary Langford and Ian Ramsay).

2. Recent ASIC Developments

2.1 ASIC updates guidance as crowd-sourced funding regime extends to proprietary companies

18 October 2018 - ASIC has released updated regulatory guides to coincide with the extension of the CSF framework to eligible proprietary companies. This started on 19 October 2018.

ASIC has amended its guidance to include proprietary companies and updated requirements for public companies after consulting with those parties that made submissions to *Consultation Paper 288 Crowd-sourced funding: Guide for public companies* and *Consultation Paper 289 Crowd-sourced funding: Guide for intermediaries*.

Regulatory Guide 261 Crowd-sourced funding: Guide for companies helps public and eligible proprietary companies to understand and comply with the additional reporting requirements and accountability standards that apply to companies raising funds through the CSF regime. ASIC recognises that this is a new regime for proprietary companies and these companies will not have experience in making public offers of their shares.

Regulatory Guide 262 Crowd-sourced funding: Guide for intermediaries helps intermediaries seeking to provide a crowd-funding service to public and eligible proprietary companies. It explains intermediaries' unique gatekeeper obligations as operators of platforms for CSF offers and investments.

ASIC's MoneySmart website has further information for investors on how to invest through crowd-sourced funding.

2.2 Financial adviser professional standards reforms - ASIC releases new instrument delaying reporting dates and making minor amendments

10 October 2018 - ASIC has released a new legislative instrument relating to the professional standards reforms for financial advisers, as announced on 1 August 2018.

The instrument makes changes to the reporting dates for a number of disclosure obligations in the transition to the new financial adviser professional standards reforms.

It also makes minor technical amendments to address unintended consequences to ensure that the new education and training standards apply in a consistent way to individuals at the intended time.

The reporting changes will simplify licensees' notification obligations and enable ASIC to implement the required systems changes more effectively.

These changes do not affect advisers' and licensees' substantive obligations under the professional standards reforms. Advisers and licensees must still comply with the new substantive professionalism and education requirements and licensees must keep appropriate records for compliance purposes.

View the ASIC Corporations (Professional Standards-Transitional) Instrument 2018/894 and the explanatory statement.

2.3 ASIC provides relief and updates guidance on short selling

8 October 2018 - ASIC has issued a new legislative instrument that provides various relief and modifications to the laws in relation to short selling.

ASIC has also updated its existing guidance in Regulatory Guide 196 Short selling to reflect the legislative instrument.

In addition to providing new relief and modifications, the ASIC Corporations (Short Selling) Instrument 2018/745 (the Short Selling Instrument) continues the effect of other ASIC instruments that were due to expire. It follows a public consultation under *CP 299 Short selling: Naked short selling relief, position reporting amendments and sunsetting class orders*, earlier this year.

The new relief and modifications cover:

- legislative relief for ETF market makers;
- deferred settlement trading;
- initial public offering (IPO) sell downs; and
- an option for global firms to calculate their short positions as at a global end calendar time.

The Short Selling Instrument incorporates the following ASIC instruments that were due to expire:

- *ASIC Class Order [CO 09/774] Naked short selling relief for market makers*;
- *ASIC Class Order [CO 08/764] Exercise of exchange traded options*;
- *ASIC Class Order [09/1051] Short selling relief: Exchange traded options, unobtained financial products and certain bonds*;
- *ASIC Class Order [10/111] Short selling: Limited relief for deferred purchase agreement issuers*;
- *ASIC Class Order [10/288] Covered short sale transaction reporting relief for market makers*;
- *ASIC Class Order [10/135] Relief for small short positions*; and
- *ASIC Class Order [10/29] Short selling reporting regime*.

Most of these have been remade without significant changes.

The Short Selling Instrument took effect from 28 September 2018.

2.4 ASIC consults on "sunsetting" class order regarding share and interest purchase plans

2 October 2018 - ASIC has released a consultation paper proposing to remake its class order on share and interest purchase plans. The class order is due to expire (sunset) on 1 October 2019.

ASIC proposes to remake the class order, as it is operating effectively and efficiently, and it continues 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 ASIC Class Order [CO 09/425] so that the ongoing effect will be preserved without any disruption to the entities that rely on it.

Consultation Paper 304 Remaking ASIC class order on share and interest purchase plans outlines ASIC's rationale for proposing to remake the instrument.

2.5 ASIC corporate plan for 2018/19 to 2021-22

2 October 2018 - ASIC has released its Corporate Plan for 2018-19 to 2021-22 in which small business continues to be an important stakeholder for ASIC, reflected in the plan's action items for 2018-19.

In the financial year ahead, ASIC will focus on poor culture and professionalism in financial services and credit, particularly in the provision of consumer credit and financial advice, the fair treatment of small business, and the use of consumer data by firms (including data governance).

ASIC will continue to review lenders' compliance with small business protections in unfair contract terms legislation and offer broader support to small business by providing information, tools and resources.

In addition to ensuring companies comply with their obligations to small business, ASIC will be focussing on compliance by small business, in particular, illegal phoenix behaviour, non-compliance with financial reporting obligations and director misconduct.

2.6 ASIC releases guidance on code of ethics compliance schemes for financial advisers

28 September 2018 - ASIC has released Regulatory Guidance 269 Approval and oversight of compliance schemes for financial advisers (RG 269).

The financial advice professional standards reforms include obligations for financial advisers to, from 1 January 2020, comply with a code of ethics and be covered by an ASIC-approved compliance scheme under which their compliance with the code of ethics will be monitored and enforced.

RG 269 explains the process and criteria for determining whether to grant approval to a compliance scheme.

It also sets out:

- ASIC's expectations for the governance and administration, monitoring and enforcement processes, and ongoing operation of compliance schemes;
- how ASIC will exercise its powers to revoke the approval of a compliance scheme and to impose or vary conditions on the approval; and
- the notifications that monitoring bodies must make to ASIC.

The code of ethics is being developed by the Financial Adviser Standards and Ethics Authority (FASEA). Consultation on an exposure draft of the code of ethics released by FASEA closed on 1 June 2018. At this time, FASEA has not released the final code. If there are significant changes from the draft code, ASIC may need to revise its guidance when the final code is released.

See also: Report 595 Response to submissions on CP 300 Approval and oversight of compliance schemes for financial advisers.

2.7 ASIC extends employee redundancy funds legislative instrument

25 September 2018 - ASIC has made a new legislative instrument which continues the effect of longstanding ASIC relief set out in ASIC Corporations (Employee redundancy funds relief) Instrument 2015/1150 until 1 October 2021.

An employee redundancy fund pools contributions from employers for employee redundancy payments.

ASIC Corporations (Amendment) Instrument 2018/825 ensures that the existing relief to employee redundancy funds relief from the managed investment and associated provisions in the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) continues.

This relief is from requirements to:

- hold an Australian financial services (AFS) licence with appropriate authorisations;
- register the employee redundancy fund as a managed investment scheme; and
- comply with the managed investment provisions in Chapter 5C of the Corporations Act and other associated provisions, including those relating to Product Disclosure Statements, ongoing disclosure requirements and the anti-hawking provisions.

The extension will allow for consideration of whether employee redundancy funds should continue to technically fall within the managed investment regime of the Corporations Act, particularly in light of proposed law reform to the Fair Work Act 2009 No. 28 (Cth) and Fair Work (Registered Organisations) Act (2009) 1988 No. 86 (Cth) concerning these funds.

2.8 ASIC review finds unacceptable delays by financial institutions in reporting, addressing and remediating significant breaches

25 September 2018 - ASIC has released a report identifying serious, unacceptable delays in the time taken to identify, report and correct significant breaches of the law among Australia's most important financial institutions.

The report REP 594 Review of selected financial services groups' compliance with the breach reporting obligation examined the breach reporting processes of 12 financial services groups, including the big four banks (ANZ, CBA, NAB and Westpac) and AMP.

Key findings from the report include:

- financial institutions are taking too long to identify significant breaches, with the major banks taking an average time of 1,726 days (over 4.5 years);
- there were delays in remediation for consumer loss. It took an average of 226 days from the end of a financial institution's investigation into the breach and first payment to impacted consumers (this is on top of the average across all institutions of 1,517 days before the breach is discovered and the time taken to start and complete an investigation);
- the significant breaches (within the scope of the review) caused financial losses to consumers of approximately $500 million, with millions of dollars of remediation yet to be provided; and
- the process from starting an investigation to lodging a breach report with ASIC also takes too long, with major banks taking an average of 150 days.

Once a financial institution has investigated and determined that a breach has occurred and that it is significant, the law requires that the breach be then reported to ASIC within 10 business days. One in seven significant breaches (110 of 715) were reported later than that 10-business day requirement.

2.9 ASIC extends relief for foreign financial services providers

21 September 2018 - ASIC has extended to 30 September 2019 licensing relief for foreign financial services providers (FFSPs) to allow them to provide financial services to Australian wholesale clients without needing to hold an Australian financial services licence.

The licensing relief that is extended by ASIC is in the following instruments:

- *ASIC Corporations (Repeal and Transitional) Instrument 2016/396* and *ASIC Corporations (CSSF-Regulated Financial Services Providers) Instrument 2016/1109* in which FFSPs relying on this relief can provide specified financial services to Australian wholesale clients if their home regulatory regime has been assessed by ASIC as sufficiently equivalent to the Australian financial services licensing regime; and

- *ASIC Corporations (Foreign Financial Services Providers-Limited Connection) Instrument 2017/18* which provides licensing relief for FFSPs limited to inducing an Australian wholesale client to use the provider's financial services.

These instruments were due to expire in late September 2018.

2.10 ASIC reports on climate risk disclosure by Australia's listed companies

20 September 2018 - An ASIC report on climate risk disclosure by Australia's listed companies has found more can be done to improve consistency in disclosure practices across listed companies, with very limited climate risk disclosure outside of the top-200 companies.

Report 593 Climate risk disclosure by Australia's listed companies sets out ASIC's high-level findings and recommendations for listed companies following an ASIC review of disclosure practices in the market.

The review examined climate risk disclosures:

- by 60 listed companies in the ASX 300;
- in 25 recent initial public offering (IPO) prospectuses; and
- across 15,000 annual reports.

Of the 60 listed companies in ASIC's ASX 300 sample, 17% identified climate risk as a material risk to their business. While most of the reviewed ASX 100 entities had considered climate risk to the company's business to at least some extent, disclosure practices were considerably fragmented, with information provided to the market in differing forms across a wide range of means of disclosure.

In some cases, the review found climate risk disclosures to be far too general, and of limited use to investors. Outside of companies in the ASX 200, there was very limited climate risk disclosure by listed companies.

2.11 ASIC remakes "sunsetting" class order about group purchasing bodies and extends the relief to limited licensees

19 September 2018 - ASIC has remade *ASIC Class Order [CO 08/1]*, which was due to expire on 1 October 2018. The practical effect of this is to continue to exempt certain groups who purchase products to cover other people's risks from needing to hold an AFS licence and other regulatory requirements. For example, a sporting association might arrange cover for its officials and other voluntary workers but does not need to meet the same requirements as an insurance broker or financial adviser. This relieves community groups and other organisations from regulatory burdens due to the low risk of consumer harm.

The new instrument, ASIC Corporations (Group Purchasing Bodies) Instrument 2018/751, continues to provide class relief to eligible group purchasing bodies from the following requirements in the Corporations Act 2001 No 50 (Cth):

- registration of a managed investment scheme under Chapter 5C;
- AFS licensing for certain activities (dealing, providing custodial or depository services and providing certain financial product advice) relating to risk management products; and

- certain other requirements in Chapter 7 relating to disclosure and other conduct.

The only substantive change to the class relief in the new instrument is that the new instrument expressly extends the class relief to holders of "limited licences".

A limited licence is an alternative form of AFS licence that allows the licensee to provide a range of limited financial services relevant to self-managed superannuation funds (SMSFs). It was introduced to facilitate accountants moving into the AFS licensing regime following the removal of the accountants' exemption which previously allowed recognised accountants to provide recommendations about acquiring or disposing of an interest in an SMSF without being covered by an AFS licence. The accountants' exemption was repealed in 2016.

See also: ASIC Corporations (Repeal) Instrument 2018/750.

3. Recent ASX Developments

3.1 Response to consultation - Management of the ASX market

On 28 September 2018 ASX released its response to submissions received on the consultation paper on the management of the ASX Market. The consultation paper was released on 21 March 2018 and was the final of three consultations following the ASX Trade outage in September 2016.

The consultation paper sought feedback on what enhancements could be made to how the ASX Market is managed during technical issues or outages, including feedback on the following topics:

- the application of session states;
- the management of orders during incidents;
- communication with the Market during incidents;
- the current ASX market practice of staggered group openings; and
- action when only a subset of securities are available for trading.

The response summarises the feedback received from the consultation paper and provides ASX's responses to this feedback.

The response to consultation is available on the ASX Website.

3.2 Reports

On 4 October 2018 ASX released the ASX Monthly Activity Report for September 2018.

4. Recent Takeovers Panel Developments

4.1 Bullseye Mining Limited 02 - Declaration of unacceptable circumstances; and orders and undertaking

3 October 2018 - The Takeovers Panel has made a declaration of unacceptable circumstances in relation to an application dated 3 September 2018 by Hongkong Xinhe International Investment Company Limited in relation to the affairs of Bullseye Mining Limited.

Bullseye (an unlisted public company) is the subject of an off-market takeover bid by Opus Resources Pty Ltd, a wholly owned subsidiary of Red 5 Limited (ASX:RED).

On 19 July 2018, Bullseye lodged a third supplementary target's statement disclosing, among other things, that it had entered into two related and inter-conditional transactions:

- the issue of 150 convertible notes (fully underwritten by Mr Desmond Mullan) to raise up to GBP15,000,000; and
- a Gold Prepayment Deed constituting the grant by Bullseye to Mr Mullan (or his associate) of an option to provide AUD100,000,000 funding to Bullseye to be repaid by Bullseye via the delivery of future physical gold ounces (collectively, the Mullan Proposal).

Mr Mullan is the father of Bullseye executive director, Ms Dariena Mullan.

Bullseye issued a Notice of General Meeting dated 20 August 2018 that included resolutions to approve the Mullan Proposal on the basis of the Panel's frustrating action policy.

Prior to the general meeting held on 17 September 2018, in accordance with an undertaking given to the Panel (see TP18/65), Bullseye withdrew the resolutions relating to the Mullan Proposal.

Notwithstanding the withdrawal of the resolutions from the general meeting, the Panel considered the circumstances, taken as a whole, were unacceptable, particularly when considered in the context of the Red 5 offer, the involvement of Ms Mullan in the decision making process and other surrounding circumstances.

The Mullan Proposal effectively allows Mr Mullan, a related party, to determine who will receive notes that, upon conversion, may confer voting power of approximately 28% or more in Bullseye. The terms of the notes also give Mr Mullan significant veto rights with only a holding of more than 20% of the notes.

The Panel also considered certain terms of the notes may deter or block a potential control transaction, inhibit the acquisition of voting shares taking place in an efficient, competitive and informed market and have a coercive effect on shareholders if shareholder approval is required upon conversion of the notes.

The effect on potential control of the terms of the notes and the veto rights, in combination, exceeded what in the Panel's experience would be usual in the circumstances, and there were no measures to disperse that effect.

On 23 October 2018, the Panel made final orders prohibiting Bullseye from issuing certain convertible notes unless it first obtains shareholder approval for the Mullan Proposal.

In light of the Mullan Proposal's significance for potential control of Bullseye and Ms Mullan's involvement in the decision making process in relation to the Mullan Proposal, the Panel requires that shareholder approval is required for the provision of a financial benefit to a related party of Bullseye, in a manner which is similar to that required under Chapter 2E of the Corporations Act 2001 No 50 (Cth), including as to who may vote at the general meeting. Unless Bullseye satisfies ASIC otherwise, Bullseye is required to provide a valuation from an independent expert with the notice of meeting.

The Panel also requires specific disclosure in the explanatory statement for the shareholders meeting in relation to certain terms of the convertible notes which the Panel found may deter or block a potential control transaction, inhibit the acquisition of voting shares taking place in an efficient, competitive and informed market and have a coercive effect on shareholders.

In addition to final orders, the Panel accepted an undertaking from Ms Mullan that she will not vote on future board resolutions relating to the Mullan Proposal.

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

5. Recent Research Papers

5.1 How blockchain could increase the need for an availability of contractual ordering for companies and their investors

This article examines how crypto-assets such as equity tokens might change the nature of how companies and investors structure their relationships. Traditionally, corporate law theorists have argued about whether business organisation law should allow for greater private ordering of relationships between companies and their investors. With the advent of blockchain and new tokenized investment opportunities, an entirely new perspective on contractual ordering has opened. With tokenised interests, not only is private ordering available to an extent never before seen, it is now required because of the absence of default rules governing the relationships between company and investor. This article explores the risks and potential benefits of this new frontier, and includes an overview of the wide range of topics that a private ordering regime will need to consider.

How Blockchain Could Increase the Need for and Availability of Contractual Ordering for Companies and Their Investors

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5.2 Piercing the corporate veil: Historical, theoretical and comparative perspectives

The concept of a company as a separate entity from its shareholders is well known and recognised in many common law and civil law jurisdictions. Generally, it is regarded as a fundamental aspect of corporate law and for this reason courts are loath to depart from it. Nevertheless, the principle of separate personality is not absolute and in both common law and civil law countries the courts have the power to depart from it. Where this occurs, it is often said that the courts "pierce" or "lift" the corporate veil. This will usually, but not inevitably, lead to liability being imposed on another person, perhaps in addition to the corporate vehicle.

This paper aims to compare and critically examine the circumstances under which veil piercing takes place against the objectives of incorporation. The countries examined are England, Singapore and the United States which are common law jurisdictions, as well as the civil law countries of China and Germany. The main purpose of this comparison is to offer a reasonably comprehensive and thorough examination of how the principle of veil piercing, which has been formally adopted either through case law or legislation, is doctrinally applied by the courts in these jurisdictions.

Piercing the Corporate Veil: Historical, Theoretical and Comparative Perspectives

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5.3 Long-term economic consequences of hedge fund activist interventions

The authors examine the long-term effects of interventions by activist hedge funds. Prior papers document positive equal-weighted long-term returns and operating performance improvements following activist interventions, and typically conclude that activism is beneficial. They extend prior literature in two ways. First, they find that equal-weighted long-term returns are driven by the smallest 20% of firms with an average market value of $22 million. The larger 80% of firms experience insignificant negative long-term returns. On a value-weighted basis, which likely best gauges effects on shareholder wealth and the economy, they find that pre- to post-activism long-term returns are insignificantly different from zero. For operating performance, they find that prior results are a manifestation of abnormal trends in pre-activism performance. Using an appropriately matched sample, the authors find no evidence of abnormal post-activism performance improvements. Overall, the results do not strongly support the hypothesis that activist interventions drive long-term benefits for the typical shareholder, nor do the authors find evidence of shareholder harm.

Long-Term Economic Consequences of Hedge Fund Activist Interventions

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5.4 Who turned multinational corporations into bearers of human rights? On the creation of corporate 'human' rights in international law

Who turned multinational corporations into bearers of human rights? This contribution analyses the recognition and transformation of the idea of legal persons as rights holders from a rather isolated and restricted phenomenon in some domestic contexts, into a broader and fully-fledged recognition of corporations as human rights bearers in international law. Throughout the last decades, the highly contested and by no means obvious recognition of corporations as independent right holders has become a salient discursive element in two fields of international law; international human rights law and international investment law.

By inquiring into the role of historical contingency, the authors analyse the interplay between events and discursive structures that led to the creation of corporate human rights.

They argue that this development can be traced back to three historical events post 1945:

- first, the inclusion of legal persons in the drafting process of the ECHR and its First Additional Protocol in the late 1940s;
- secondly, the jurisprudence of the European Court of Human Rights, peaking in the 1980s, which effectively promoted and expanded corporate rights; and
- thirdly, the migration of corporate human rights into the realm of investment arbitration in the early 2000s.

Who Turned Multinational Corporations into Bearers of Human Rights? On the Creation of Corporate 'Human' Rights in International Law

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5.5 Managing reputation: Evidence from biographies of corporate directors

The authors examine how directors' reputations are managed through disclosure choices. They focus on disclosures in the director biographies in proxy statements filed with the SEC. They find that a directorship on another board is more likely to be undisclosed when the other firm experienced an adverse event during the director's tenure. Withholding such information is associated with a more favourable stock price reaction to the director's appointment and the loss of fewer subsequent directorships. These findings suggest that the concerns about the reputations of corporate directors lead to strategic disclosure choices that have real consequences in capital and labour markets.

[Managing Reputation: Evidence from Biographies of Corporate Directors]

6. Recent Corporate Law Decisions

6.1 Board's declaration of vacancy of directors' offices following a prolonged period of absence as board meetings upheld

(By Andrew Hay and Shigeki Yamaura, Clayton Utz)

Cao v Apollo Phoenix Resources Pty Ltd [2018] FCA 1445 (20 September 2018) Federal Court of Australia, Markovic J

(a) Summary

Zhong Cao (Mr Cao) was appointed as a director of Apollo Phoenix Resources Pty Ltd (Apollo). Mr Cao resided in China and did not speak English. An arrangement was made between Apollo, Mr Cao and fellow Chinese director, Dehong Yu (Mr Yu) that all correspondences from Apollo for Mr Cao would be provided to Mr Yu who would translate the correspondence into Chinese and convey to it Mr Cao.

Due to the nature of Apollo's business, Apollo's board meetings were often called on short notice. After attending several board meetings by telephone since his appointment as a director, Mr Cao had been absent from subsequent meetings for a prolonged time period, during which Mr Cao's solicitor corresponded with Apollo's solicitors claiming that, among other things, Mr Cao was not given sufficient time to consider items discussed and/or resolved at board meetings.

Following the prolonged period of absence by Mr Cao from board meetings, Apollo's directors other than Mr Cao and Mr Yu resolved to declare the director positions of Mr Cao and Mr Yu to be vacant pursuant to Apollo's constitution.

Mr Cao applied to the court for, amongst other things, an interlocutory order under s. 233 of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) to declare that the vacating of Mr Cao's director position be rescinded or otherwise void or of no effect because Apollo's calling of board meetings on short notice amounted to being oppressive, unfairly prejudicial to or unfairly discriminatory against him.

The court found that the notice given for each of the meetings was reasonable and dismissed Mr Cao's application.

(b) Facts

Mr Cao is a shareholder in Apollo and was appointed as a new director of Apollo in January 2017 along with Mr Yu. When they were appointed as directors, Apollo had 3 other directors. Mr Cao and Mr Yu resided in China.

Before Mr Cao invested into Apollo, the directors of Apollo were made aware that Mr Cao did not speak English and Mr Yu would act as Mr Cao's translator after the investment.

Following the investment and prior to appointment of Mr Cao and Mr Yu's as directors, Apollo and Mr Cao and Mr Yu made an arrangement whereby all board documents, including notices of board meetings and circular resolutions for Mr Cao, would be sent to Mr Yu so that Mr Yu could translate them into Chinese for Mr Cao. Mr Cao did not appoint any other person to act as his translator and did not request Apollo to send board documents to him directly. One of Apollo's directors, Christopher Daws, also told Mr Cao and Mr Yu, in effect, that they will need to execute documents in a timely manner. A copy of Apollo's constitution was sent to Mr Yu.

Board meetings were often called, and relevant documents were given to Mr Yu, on short notice. On occasions when Mr Yu expressed a need for further time to translate documents for Mr Cao, board meetings were at times adjourned to allow that to occur. Since Messrs Cao and Yu's appointment as directors, Mr Cao attended the first four of the board meetings (including two adjourned meetings, meaning there were effectively two meetings) by telephone. His solicitor also contacted Apollo's solicitors expressing Mr Cao's concerns. Mr Cao did not attend the fifth meeting but Mr Yu spoke on his behalf. After Mr Cao attended (through Mr Yu's attendance on Mr Cao's behalf) the board meeting held on 8 September 2017, Mr Cao did not attend any subsequent meetings.

On 22 August 2018, Apollo's three directors based in Australia held a board meeting resolving, among other things, to declare the director positions of Mr Yu and Mr Cao vacant, pursuant to cl. 9 of Apollo's constitution. Clause 9 provided that a director automatically ceases to be a director if:

- the director is absent from meetings of directors for six consecutive months without special leave from the directors; and
- the directors consequently declare his or her office vacant.

On 28 August 2018, Mr Cao lodged an interlocutory application to the court seeking, amongst other things, an order under s. 233 of the Corporations Act declaring that the vacating of Mr Cao's office of director be rescinded or otherwise void or to no effect.

Mr Cao's submissions included that:

- a director of a company was entitled to reasonable notice of a board meeting, which Apollo failed to give;
- failure to give reasonable notice meant that he was not considered to be absent from the board meetings which Mr Cao did not attend; and
- Apollo's conduct in not providing reasonable notice to him and then relying on his non-attendance, or failure to seek leave from, the board meetings as a means of removing him as a director was oppressive and was unfairly prejudicial to or unfairly discriminatory against him as a member in his capacity as a director.

Apollo contended that:

- Mr Cao had failed to establish that the notice provided for each board meeting was not reasonable and, in any event, reasonable notice was given; and
- the directors of Apollo were entitled to rely on cl. 9 of its constitution to make the declaration vacating Mr Cao from his director position.

(c) Decision

Markovic J noted, citing court cases including *Wilson v Manna Hill Mining Company Pty Ltd* [2004] FCA 912, that reasonable notice of directors' meeting is required in the absence of a stipulation of notice period in the constitution. She stated that factors relevant to the court's determination as to whether a reasonable notice has been made include the practice usually adopted by the Apollo board, the nature of Apollo board, and the nature of the Apollo business to be discussed and transacted at particular meetings.

It was noted that, according to the evidence submitted to the court, in this case:

- the arrangement to send notice of board meetings for Mr Cao to Mr Yu for translation became practice and Mr Cao had not sought to change the practice;
- Mr Yu was intimately involved in Mr Cao's dealings with Apollo including providing translation services to Mr Cao, and speaking at board meetings on behalf of Mr Cao;
- the nature of Apollo's business was such that it derives a commercial advantage from making decisions swiftly and from its agility in responding to market conditions;
- leading up to board meetings, directors (including Mr Yu) engaged in discussions between themselves, where Mr Yu said he would relay the content of their discussions to Mr Cao; and
- Apollo accommodated Mr Cao's requests for additional time and rescheduled meetings.

Markovic J proceeded to consider the circumstances of each of the meetings for which Mr Cao did not attend, and determined that, in the absence of any evidence to the contrary, notice given for each of the meetings was not unreasonable.

As for the Apollo board's declaration making Mr Cao's office of director vacant, Markovic J:

- determined that the notice of the board meeting on 22 August 2018 was reasonable and the subject matters of the meeting including the declaration had been made clear to Mr Cao;
- determined that cl. 9 of Apollo's constitution did authorise the directors attending the meeting, which formed the majority of the board, to make the declaration;
- rejected Mr Cao's submission that no declaration had in fact been made at the meeting; and
- determined that it was not unfairly prejudicial to Mr Cao to hold the meeting in the face of his opposition.

Mr Cao's application was dismissed.

6.2 Bell Litigation proceeding transferred to WA Supreme Court

(By Beau Deane Paterson, DLA Piper)

Bell Group NV v Bell Group Finance Pty Ltd, in the matter of Western Interstate Pty Ltd [2018] FCA 1440 (20 September 2018) Federal Court of Australia, McKerracher J

(a) Summary

This decision concerned an application by Bell Group (UK) Holdings Limited (in liquidation) to transfer a Federal Court proceeding to the Supreme Court of Western Australia.

The proceeding was ostensibly part of the broader Bell Litigation and ongoing proceedings concerning the distribution of funds to creditors of the Bell Group. However, it concerned a number of discrete issues.

His Honour, McKerracher J, determined that the application should be approved and the proceeding transferred because the WA Supreme Court represented the "natural home" of the Bell Litigation and the transfer offered substantial case management and costs advantages.

(b) Facts

This decision relates to an application by Bell Group (UK) Holdings Limited (in liquidation) (BGUK) for transfer of a Federal Court proceeding to the Supreme Court of Western Australia (the Application).

As the names of the parties would suggest, the Federal Court proceeding was related to the "notorious" Bell Litigation. The original Bell Litigation proceedings, which were brought by liquidators and various companies in the Bell Group against the Group's former bankers, largely settled in late 2013. As a result of the settlement, approximately $1.3 billion was made available to the first defendant, Bell Group Finance Pty Ltd (BGF), for distribution to creditors.

The distribution of these funds is still subject to a number of proceedings, including this one before the Federal Court. The Federal Court proceeding was to test among other things whether Western Interstate Pty Ltd (in provisional liquidation) was a creditor of BGF and entitled to a proportion of the funds.

(c) Decision

BGUK's application to transfer the Federal Court proceeding to Western Australia was made under s. 1337H of the Corporations Act 2001 No. 50 (Cth). Sections 1337H provides, among other things, that a Federal court civil proceeding may be transferred to the Supreme Court of a state if it appears that, having regard to the interests of justice, it is more appropriate that the proceeding be determined by the Supreme Court.

According to McKerracher J, the question of whether a proceeding should be transferred under s. 1337H involves a weighing of considerations.

These considerations include, among other things:

- the stage of the proceedings;
- the commonality or diversity of issues; and
- the risk of conflicting findings of fact and the potential unnecessary drain on judicial and other public and private resources (see also, his Honour writing in *Yara Pilbara Fertilisers Pty Ltd v Oswal (No 8)* [2015] FCA 49, [24]-[26]).

In the hearing of this application, the pivotal considerations were not that there was any great overlap in the issues in the various proceedings, or that there would be a great risk of inconsistent findings between the Federal Court and the litigation in the Supreme Court, as is typical in such applications. Instead, the focus was on the commercial and case management benefits that would be achieved by transferring the proceeding to the "natural home" of the Bell Litigation in the WA Supreme Court.

Although the key issue in this proceeding (whether Western Interstate is a creditor of BGF) was largely discrete, McKerracher J determined that its resolution would assist in the narrowing of the broader issues between the parties as they were playing out in other proceedings.

His Honour placed emphasis on statements in *Hancock Prospect Pty Ltd v 150 Investment Pty Ltd* (2017) 120 ACSR 495, where Yates J said that:

> ". it makes no sense that an apparently anterior but nevertheless central question in a case raising a broad range of issues for determination in one court should be treated, effectively, as a separate question for resolution in another court . It seems to me that fragmentation of that kind can only lead to manifest inefficiency and certainly greater cost brought about by the inevitable and unnecessary duplication of work."

Maintaining the proceeding in the Federal Court offered no real case management or costs advantages. At the time of this decision, the proceeding was still evolving with potential new cross claims and amendments and substantial interlocutory matters still unresolved.

6.3 High Court upholds the validity of a deed of company arrangement

(By Thomas Hampel, King & Wood Mallesons)

Mighty River International Limited v Hughes [2018] HCA 38 (12 September 2018) High Court of Australia, Kiefel CJ, Gageler, Nettle, Gordon and Edelman JJ

(a) Summary

This decision considered the validity of a deed of company arrangement (DOCA), with the majority of the High Court of Australia (the Court) rejecting a creditor's claim that a DOCA was either invalid or void under Part 5.3A of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act).

Part 5.3A concerns the administration of the affairs of a company facing insolvency, and provides that a DOCA may be used as a means of maximising the company's chances of survival, or alternatively ensuring creditors receive a better return. Part 5.3A provides various procedures and steps regarding the creation of a DOCA, including the issues it must address and timing. Further, Part 5.3A addresses when a DOCA may be terminated or declared void.

In rejecting both grounds of appeal put before it, the Court upheld the process undertaken by the administrators as being pursuant to a valid deed of company arrangement entered into in accordance with the provisions of Part 5.3A and discussed the application of various relevant provisions in determining whether the DOCA was compliant with Part 5.3A or should be declared void. In short, the investigations conducted by the administrators were deemed to be thorough and sufficient and no grounds to void the DOCA were found.

(b) Facts

In July 2016, Mesa Minerals Ltd (Mesa) was placed into voluntary administration and had two administrators appointed. After preparing reports and holding creditor meetings regarding the future of Mesa, the administrators concluded it was in the creditors' best interests to enter into a "Recapitalisation DOCA". This process aimed to provide the administrators with more time to explore the possibility of a restructure.

The majority of creditors voted in favour of this proposal.

The DOCA was then executed and provided that:

- there was to be a moratorium on all creditor claims;
- the administrators would further investigate and report possible variations to the DOCA over the following six months; and
- no property of Mesa would be made available to creditors.

Mighty River International Ltd (Mighty River) was a creditor of Mesa. It opposed the DOCA and preferred that Mesa be placed into liquidation. It unsuccessfully sought to have the DOCA declared invalid or void in the Supreme Court of Western Australia and on appeal in the Western Australian Court of Appeal. There, Mighty River argued that a "holding DOCA" of the nature entered into, that is expressly created for a moratorium period, should be void.

On appeal to the Court, Mighty River submitted that:

- the DOCA was not a valid deed of company arrangement because it was contrary to the objects of Part 5.3A and so not entered into in accordance with it; and
- even if the DOCA could be considered a deed of company arrangement, the DOCA should be declared void because of breaches of Part 5.3A.

Section 445G(2) gives the Court the power to declare the deed, or a provision of it, void if it is not entered into in accordance with Part 5.3A or if it did not comply with Part 5.3A.

(c) Decision

The Court dismissed Mighty River's appeal by a three-two majority. The majority were Kiefel CJ and Edelman J and Gageler J, whilst Nettle and Gordon JJ dissented.

(i) Was the DOCA valid and consistent with the object of Part 5.3A?

The majority rejected Mighty River's claim that the DOCA was invalid and not a deed of company arrangement because it was not consistent with the objects of Part 5.3A. In particular, Mighty River maintained that the DOCA, by providing for a six month period for the administrators to further investigate options, sought to "sidestep" the requirement under s. 439A(6) of the Corporations Act. Section 439A(6) provides that only a court can extend the convening period for the creditor's meeting to decide the future of a company under administration.

Taking a broad view of the objects of Part 5.3A, the majority held that, notwithstanding s. 439(6), a DOCA may incidentally extend the time for an administrator to investigate, and allow subsequent variations to the DOCA. The majority found that the DOCA created genuine rights and duties, including obliging the administrators to prepare regular reports within the extended time period, meaning the extension was merely incidental.

Further, the majority held the DOCA was not contrary to the objects of Part 5.3A by providing a moratorium on the creditors' claims.

The majority reasoned that:

- the DOCA aimed to ensure Mesa's survival, or otherwise provide a better return to creditors, as supported by the administrators' investigations;
- a moratorium that has the purpose of allowing the administrators more time to investigate is valid, as supported by various precedent; and
- the purposes of the statutory scheme providing only a short convening period before the second creditors' meeting are not undermined by the creditors entering into a longer moratorium period pursuant to the DOCA.

Gageler J (in his separate judgment) further reasoned that Part 5.3A functions to allow creditors themselves to decide on what course of action is in their best interests. There are various provisions that protect any creditors who may disagree with the vote.

(ii) Should the DOCA otherwise be declared void under s. 445G(2)?

The majority also rejected Murray River's claim that the DOCA was otherwise void because of alleged contraventions of Part 5.3A.

The majority found that the DOCA did not contravene the Act. In particular the DOCA did not breach s. 444A(4)(b) in that it did not specify any property to be distributed by the administrator. Section 444A(4)(b) provides for various matters that a deed must specify, but does not impose a positive requirement on administrators to actually distribute property to creditors.

Further, the majority found there were no breaches of:

- s. 438A(b), which obliges the administrators to form an opinion of the creditors' interests; or
- (the since repealed) s. 439A(4), which concerns the timing of these opinions.

In respect of these claims, the majority considered a report submitted by the administrators which provided express and well-reasoned conclusions regarding the creditors' interests. Murray River's claim therefore rested on a conclusion that these expressed opinions were not genuinely held. Although the majority acknowledged there may be circumstances where there is insufficient information to express an opinion, in these circumstances the administrators' confidence regarding the Recapitalisation DOCA was based on substantial research and investigations.

(iii) Minority judgment

Conversely, the minority would have allowed the appeal. In short, the minority found that the DOCA did not provide an alternative arrangement to liquidation, and instead merely granted the administrators further time. The DOCA was therefore not a valid deed of company arrangement for the purposes of Part 5.3A. In reaching this conclusion, the minority focused on the strict core purpose of Part 5.3A (construing these objects more narrowly than the majority), and stressed the important role of court supervision during this process.

6.4 Court grants company leave to bring a derivative action "in the best interests of the company"

(By Maggie Kearney, Ashurst)

Connective Services Pty Ltd v Slea Pty Ltd [2018] VSCA 229 (10 September 2018) Court of Appeal, Supreme Court of Victoria, Fergusson CJ, Whelan JA, McLeish JA

(a) Summary

Connective Services Pty Ltd and Connective Services OSN Pty Ltd (together the Connective companies) appealed the decision of the Victorian Supreme Court, to grant leave to Slea Pty Ltd (Slea) to commence derivative proceedings under s. 237 of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) on behalf of the Connective companies.

Section 237(2) of the Corporations Act sets out five circumstances which, if the court is satisfied exist, require leave to be granted.

Section 237(2) provides that the Court must grant the application if it is satisfied that:

- it is probable that the company will not itself bring the proceedings, or properly take responsibility for them, or for the steps in them;
- the applicant is acting in good faith;
- it is in the best interests of the company that the applicant be granted leave;
- if the applicant is applying for leave to bring proceedings, there is a serious question to be tried; and

- either:
  - at least 14 days before making the application, the applicant gave written notice to the company of the intention to apply for leave and of the reasons for applying; or
  - it is appropriate to grant leave even though the above is not satisfied.

The Connective companies brought the appeal on grounds that the primary judge erred in finding that Slea was acting in good faith, that granting leave was in the Connective Companies' best interests, and that there was a serious question to be tried.

The Victorian Court of Appeal upheld the trial judge's decision to grant leave. The Court found that Slea was acting in good faith in bringing derivative proceedings, adopting the trial judge's application of Palmer J's reasoning in *Swansson v R A Pratt Properties Pty Ltd* (2002) 42 ACSR 313 (*Swansson*). The Court also held Slea was acting in the best interests of the company in bringing the derivative action.

(b) Facts

Slea initially held one third of the shares in the Connective companies. Mr Tsialtis is the sole shareholder and director of Slea. Mr Glenn Lees originally held the remaining shares in the Connective companies, which he transferred to Millsave Pty Ltd (Millsave) in 2006. Mr Tsialtis commenced working for Liberty Financial Pty Ltd (Liberty) in 2008. Liberty's holding company is Minerva Financial Group Pty Ltd (Minerva).

In 2010, Mr Tsialtis, Slea and Minerva entered into the Accommodation Agreement, through which Minerva would consider lending Slea money to enable Slea to buy further shares in the Connective companies if such shares became available. The respective constitutions of the Connective companies contain pre-emptive rights provisions which provide that the Connective companies cannot issue shares unless they were first offered to existing shareholders.

The directors of the Connective companies effected a corporate restructure in early 2013 through which a number of subsidiary companies were established with the Connective companies holding all of the shares in these subsidiaries, known as the Connective Group. Macquarie Bank purchased 25% of the shares in the Connective Group from the Connective companies for $5 million. The proceeds of this sale were distributed as dividends to the shareholders of the Connective companies, including Slea.

In late 2013, Mr Tsialtis became aware of the sale to Macquarie Bank and applied for an injunction. Slea alleged that the corporate restructure and the subsequent sale were in breach of the directors' duties owed to the Connective companies, and Macquarie Bank was an accessory to the breaches. In July 2014, Slea amended its pleading to include a claim for oppressive conduct through the corporate restructure.

The case before the primary judge was an application by Slea for leave pursuant to s. 237 of the Corporations Act to bring a proceeding on behalf of the Connective companies against Mr Lees, Macquarie Bank and others, and to rely on certain documents in that proceeding, should leave be granted.

The issues for determination before the Court of Appeal were:

- whether the primary judge's view as to what constitutes a relevant collateral purpose was too restrictive (the collateral purpose and good faith claim);
- whether the primary judge erred in finding there was no unacceptable delay in Slea bringing the application (the delay claim);
- whether the primary judge failed to focus on the nature and purpose of the proposed proceeding (the companies' best interests claim); and

- whether the primary judge wrongly found that the pre-emptive rights provisions served to ensure the founding members of the Connective companies had the power to control who participated in the business (the serious question to be tried claim).

(c) Decision

The Court of Appeal granted leave to appeal on the grounds of collateral purpose and the companies' best interests, but dismissed the appeal on those grounds.

(i) Collateral purpose and good faith

The Connective companies submitted that Slea's derivative application was brought for the collateral purpose of advancing Liberty's interests pursuant to the Accommodation Agreement with the result that Slea was not acting in good faith as required by s. 237. The Court considered the factors set out by Palmer J in *Swansson* as being indicative of good faith, adopting the approach taken by the primary judge.

In applying these factors the Court held, noting as the primary judge did, that these factors are not exhaustive, that:

- despite Liberty's possible interest in the proceedings, Slea's claims are legitimate claims that it brings in its capacity as a shareholder; and
- the Accommodation Agreement did not support the existence of a lack of good faith in Slea pursuing the action.

The Court held that there was no error in the primary judge's analysis of the good faith requirement.

(ii) Delay

The Connective companies submitted that the primary judge erred in finding that there had not been an unacceptable delay in Slea bringing the derivative proceedings in 2016, despite originally making an application for leave to amend in 2013. The Court noted that a grant of leave is required if the five matters set out in s. 237(2) of the Corporations Act are satisfied, and the presence or otherwise of delay was held not to have affected the existence of any of the five matters in s. 237(2).

(iii) Best interests of the companies

The Connective companies submitted that the primary judge failed to consider that Liberty is a competitor of the Connective companies and the application was brought to further Liberty's interest in gaining control of the Connective companies. They submitted that the primary judge had failed to consider the commercial effect on the Connective companies of the decision to grant leave, particularly in light of the harm that would occur to the Connective companies if the sale to Macquarie Bank was unwound.

The Court held that the question to be satisfied is whether the proceeding itself is in the companies' best interests and found that Slea's claim of a breach of duty is a genuine claim, advanced in good faith. In relation to Liberty's possible interest, the Court found that Liberty could only obtain advantage if Slea succeeded in vindicating its claimed rights, which is a matter for trial.

(iv) Serious issue to be tried

The Connective companies submitted that the directors were not bound to activate the pre-emptive rights provisions, rather the provisions gave the Connective companies the power to issue shares and to sell the business. In undertaking the restructure, the Connective companies submitted that the directors employed their power in a way that did not enliven the pre-emptive rights provisions and the directors were obliged to take that course if it was in the Connective companies' best interests. The question turned on whether the power was exercised for a proper purpose as the parties agreed what was done was within the directors' powers.

The Court held that there was a serious issue to be tried, but the question as to whether the conduct was for an improper purpose was a matter for trial. The Court held that determining that the Connective companies' had the power to do what they did, did not conclude the inquiry as to whether that power was exercised for a proper purpose.

6.5 Proposed demerger of Coles Group Ltd from Wesfarmers Ltd

(By Nick Walker, King & Wood Mallesons)

Re Wesfarmers Ltd; ex parte Wesfarmers Ltd [2018] WASC 308 (8 October 2018) Supreme Court of Western Australia in Chambers, Vaughan J

(a) Summary

Wesfarmers Ltd (Wesfarmers) plans to, via a scheme of arrangement, demerge Coles Group Ltd (Coles) into a separately listed company. As part of the scheme process, Vaughan J made orders pursuant to s. 411(1) of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) to convene a meeting of Wesfarmers' members to consider and vote on the proposed scheme.

(b) Facts

On 16 March 2018, Wesfarmers announced to the ASX the proposal to demerge Coles via a demerger scheme of arrangement. On 19 September 2018, Wesfarmers sought orders under s. 411 of the Corporations Act in relation to the proposal.

The proposed demerger would see a capital reduction, most Wesfarmers shareholders receiving one Coles share for each Wesfarmers share (with Wesfarmers retaining a 15% interest in Coles and 50% interest in Flybuys), and Coles becoming a separately listed company on the ASX official list.

This application was the first step in the proposed scheme of arrangement process.

(c) Decision

Vaughan J made orders pursuant to s. 411(1) of the Corporations Act to convene a meeting of Wesfarmers' members to consider and vote on the proposed scheme. Vaughan J also made ancillary orders as to the convening and conduct of the meeting under s. 1319 of the Corporations Act and approved for distribution to the members a scheme booklet containing the explanatory statement required by s. 412(1)(a) of the Corporations Act.

(i) Legal framework

Section 411 of the Corporations Act permits the use of a scheme of arrangement to re-organise a company. Vaughan J summarised the legal framework for a scheme of arrangement and the stages required under s. 411:

- stage 1: Application to the court to approve the convening of a scheme meeting and the distribution of the draft explanatory statement to members;

- stage 2: Members vote on the scheme. Provided the scheme obtains the necessary majority when voted on by members (75% by value and ordinarily 50% by number) the scheme will be binding on dissenting minority members; and
- stage 3: Application to the court to approve the scheme. It is at this stage that the court will make its final determination on whether to approve the scheme.

The decision of Vaughan J pertains to the first stage of the proposed scheme of arrangement.

(ii) Approval of the scheme meeting

Before Vaughan J was able to make the order to convene a scheme meeting, it was necessary that his Honour was satisfied of the following:

- there must be an "arrangement" between a Part 5.1 body and its members, as a company, Wesfarmers falls within the Part 5.1 body definition (additionally, citing *Re Foster's Group* [2011] VSC 93, the court found that the proposed scheme was an "arrangement");
- ASIC must be given 14 days' notice of the hearing (or a shorter permitted time) and have had a reasonable opportunity to examine the proposed arrangement and make submissions in relation to those matters, the court found, from the evidence, that these requirements had been met;
- the draft explanatory statement must provide adequate disclosure and contain the information prescribed by the Corporations Act, the court's assessment of the explanatory statement is discussed below; and
- it was also necessary to comply with certain procedural requirements in the Supreme Court (Corporations) (WA) Rules 2004 (WA), Vaughan J found that these requirements had been complied with.

Vaughan J explained that, in addition to the applicant satisfying the statutory and procedural requirements, in order to convene the scheme meeting, the court ought to be satisfied that the scheme is "bona fide and properly proposed" (citing numerous cases including *Re NRMA Ltd [No 1]* [2000] NSWSC 82 [22] - [24]) and that there is no apparent reason why the scheme would not in due course (subsequent to receiving the necessary majority votes) be approved by the court.

Vaughan J considered the propriety and legality, fairness and reasonableness, performance risk, and drafting of the proposed demerger scheme and determined the proposed demerger was fit for consideration by Wesfarmers' members.

(iii) Explanatory statement

The explanatory statement must provide the disclosure required by s. 411(3) and s. 412 of the Corporations Act. Citing a number of cases, Vaughan J stated that the standard of disclosure requires that:

- members are properly informed in their consideration of the proposed scheme;
- all of the main facts are stated to enable shareholders to exercise their judgement on the scheme;
- a fair and balanced picture is presented, and that the "[c]ards must be placed on the table"; and
- nothing is misleading or deceptive in any material sense.

Vaughan J noted "the tension that exists between providing fulsome, yet comprehensible, disclosure" and that much of the booklet is "replete with dense financial information'. Noting the effective use of well-constructed summaries that, where appropriate, directed to more detailed discussions and the other evidence presented, Vaughan J was satisfied that the appropriate balance was struck in the preparation of the explanatory statement and that there was prima facie evidence that the document would provide proper disclosure to members.

(iv) Capital reduction

The Wesfarmers proposal includes a proposed equal capital reduction. While noting that the court is not required to approve the capital reduction, Vaughan J stated that "the proposed capital reduction will not be an impediment to the effectuation of the proposed demerger".

(v) Conclusion

Vaughan J found that Wesfarmers' application was "thoroughly prepared and carefully presented" and that his Honour was "left in no doubt that the substantive and procedural requirements under s. 411(1) had been satisfied". Vaughan J went on to state that the proposed scheme was fit for consideration by the members of Wesfarmers and that the scheme was one that sensible business people might consider would benefit Wesfarmers' members.

6.6 Attempt to replace responsible entity of registered managed investment scheme declared invalid

(By Ruby Ramachandran, MinterEllison)

Sandalwood Properties Ltd (Subject to a Deed of Company Arrangement) v Huntley Management Ltd [2018] FCA 1502 (8 October 2018) Federal Court of Australia, Colvin J

(a) Summary

At a meeting of the members of a registered management investment scheme, resolutions were passed to remove the then responsible entity and to appoint a new responsible entity and manager. The existing responsible entity challenged the resolutions and conduct of the meeting, and in doing so raised questions as the proposed responsible entity's Australian financial services licence (AFSL). The Federal Court upheld the challenge, finding that the proposed responsible entity was not authorised to manage the scheme and that the interim chair had presided over the determination of the vote on the resolution to appoint him as chair.

(b) Facts

Sandalwood Properties Ltd (subject to a deed of company arrangement) (receivers and managers appointed) (SPL) was the responsible entity and manager of the registered management investment scheme TFS Sandalwood Project 2003 (the Project). At a meeting of the members of the scheme on 23 July 2018, resolutions were purported to have been passed which appointed Graeme Scott as chair of the meeting and removed SPL as the responsible entity conditional upon the appointment of Huntly Management Ltd (Huntley) as the new responsible entity and appointment of Sandalwood Growers Co-Op Ltd as the new manager.

At the time that the resolutions were passed, Huntley held an AFSL which stated that Huntly was authorised "to operate the following kinds of registered managed investment scheme (including the holding of any incidental property) in its capacity as a responsible entity". After these opening words, the licence then listed 13 specific managed investment schemes, but did not provide a description of a class or group or category of managed investment schemes. One of the specific schemes listed was the TFS Sandalwood Project 2002.

At the meeting, the members elected Mr Scott as chair. Mr Scott and Teague Czislowski sat at the front of the meeting. Notes of the meeting recorded Mr Scott as stating that he was taking the role of temporary chair and inviting Mr Czislowski to declare each poll on the resolution for appointment of the chair. Mr Scott also declared as carried the motion appointing himself as chair.

Mr Scott and Mr Czislowski also excluded the votes of SPL for each resolution including the resolution appointing Mr Scott as chairperson. They argued that SPL could not vote on the appointment of the chair because it could not vote on other resolutions. SPL said this ruling was a substantive irregularity.

(c) Decision

Colvin J found that Huntley's AFSL did not authorise it to operate the Project. The AFSL did not describe the characteristics of a class or group of managed schemes that it could operate nor did it state that Huntly was to be authorised to operate schemes similar to the 13 listed schemes. Construing the licence as extending to similar schemes as those listed would introduce considerable uncertainty. Given that ASIC was required by s. 914A(6) to ensure that AFSLs specified the particular financial service or class of financial services authorised, AFSL licences should not be uncertain as to their scope. It was unlikely that ASIC intended to grant licences the scope of which required a person to compare the characteristics of different schemes.

The evidence also indicated that Huntley had been taking steps to amend its AFSL to include specific reference to the Project and that there was no evidence indicating that Huntley had applied for a licence for a class of schemes rather than a named scheme.

Section 601FK states that a company "cannot be chosen or appointed as the responsible entity or temporary responsible entity of a registered scheme unless it meets the requirements of s. 601FA". Section 601FA provides that the "responsible entity of a registered scheme must be a public company that holds an Australian financial services licence authorising it to operate a managed investment scheme". Therefore, Huntley could not be chosen or appointed, because at the time that it was chosen it did not meet the requirements of s. 601FA. It was not sufficient if, by the time Huntley was included on the record of the scheme's registration, its AFSL covered the Project. The resolution choosing Huntley was therefore invalid and had no legal effect.

In relation to the choice of chair, Colvin J found that Mr Scott was the interim chair and that this rendered the members meeting invalid as Mr Scott had presided over the determination of the vote on the resolution to appoint him as chair, following *National Australia Bank Ltd v Market Holdings Pty Ltd* [2001] NSWSC 253, (2001) 161 FLR 1 at [100].

As to SPL's entitlement to vote, Colvin J noted that s. 253E provides that a "responsible entity of a registered scheme and its associates are not entitled to vote their interest on a resolution at a meeting of the scheme's members if they have an interest in the resolution or matter other than as a member". Colvin J noted that this did not mean that the responsible entity could not vote at a meeting as a whole but rather that the eligibility to vote is determined in respect of each resolution considered at a meeting. On the resolutions as to the appointment of the chair or the adjournment resolution, SPL had no interest other than its interest as a member. There were therefore substantive consequences to Mr Scott presiding over the determination of the vote on the resolution to appoint him as chair. However, Colvin J did not decide the question of whether a ruling by a chair to disallow the votes of SPL on the resolution to appoint the chair could be challenged.

As a result, Colvin J declared that each of the resolutions passed at the meeting was invalid and of no effect.

6.7 Ownership of company following dispute between business partners

(By Katrina Sleiman, Corrs Chambers Westgarth)

In the matter of NL Mercantile Group Pty Ltd [2018] NSWSC 1337 (31 August 2018) Supreme Court of New South Wales, Gleeson J

(a) Summary

The proceeding concerned a dispute between two former business partners as to the ownership of the company and the summary dismissal of one of the partners on the basis that he had breached various fiduciary and statutory duties owed to the company.

(b) Facts

Up until December 2014 the plaintiff, Mr Rofe, was the sole shareholder, director and secretary of the first defendant, NL Mercantile Group Pty Ltd (Mercantile). In late 2014, Mr Rofe and Mr Payne agreed to carry on a debt collecting business together. On 3 December 2014, Mr Rofe resigned as a director and secretary of Mercantile, appointed Mr Payne as director and secretary in his place and transferred the one issued share in Mercantile to Mr Payne (Mercantile Share).

Mr Rofe contended that he entered into an agreement with Mr Payne in about December 2014 that Mr Payne would hold 50% of the Mercantile Share on trust for Mr Rofe. Mr Rofe further contended that Mr Payne signed a document styled "Undisclosed Shareholders' Agreement" dated 4 November 2015 recording the terms of the trust between Mr Payne and himself.

On 15 March 2016, Mr Payne resigned as a director and secretary of Mercantile at the request of Mr Rofe and transferred the Mercantile Share to the second defendant, Emerald Superannuation and Insurance Pty Ltd (Emerald) pursuant to a Share Sale Deed dated 15 March 2016. Mr Rofe was appointed a director of Mercantile on that date and was the managing director and had full and unfettered control of the business.

Mr Rofe contended that Emerald received the Mercantile Share with notice of the trust on which Mr Payne held that share and that he entered into an oral agreement with Emerald in March 2016 that Emerald would cause Mercantile to issue Mr Rofe with shares to enable him to hold a 50 % interest in Mercantile. Emerald and Mercantile disputed the claims and contended that any agreement involved a disposition of an equitable interest in personalty and is unenforceable for want of writing. Mr Rofe relied on part performance to overcome the absence of writing.

On 21 October 2016, Mr Rofe was summarily dismissed by Mercantile and resigned as a director of Mercantile. Mr Rofe claimed he is the beneficial owner as to 50% of the Mercantile Share now held by Emerald and claimed damages for alleged wrongful dismissal.

By its cross-claim, Mercantile claimed (among other things) damages or equitable compensation against Mr Rofe for alleged breach of his fiduciary and analogous statutory duties as a director or officer of Mercantile.

(c) Decision

The following issues required determination.

(i) Did Mr Payne hold the Mercantile Share on trust?

Mr Payne denied any discussion about a trust arrangement with Mr Rofe. The register of members of Mercantile recorded the entry of Mr Payne on 3 December 2004 as the holder of one share non-beneficially and on 4 December 2014 Mr Payne signed a Form 484 (Change to company details), which was lodged with ASIC, recording that the share was held non-beneficially. As a book kept by a body corporate under a requirement of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) is admissible in evidence in any proceeding and is prima facie evidence of any matter stated or recorded in the book (s. 1305(1) of the Corporations Act), the prima facie position was that Mr Payne held the Mercantile Share non-beneficially.

Her Honour considered that Mr Payne and Mr Rofe each intended that Mercantile would develop as a successful business and it is most unlikely that Mr Rofe would give up entirely his ownership interest in Mercantile when agreeing to go into business with Mr Payne, as Mr Payne suggested. The better explanation for the transfer of the Mercantile Share is that they both wanted to avoid publicly identifying Mr Rofe's involvement in the management of the business given his past criminal record. Her Honour also considered that the terms of the shareholders' agreement dated 4 November 2015 signed by Mr Payne and Mr Rofe are consistent with there being a trust arrangement between them in relation to the Mercantile Share. Accordingly, her Honour held that Mr Payne held the Mercantile Share as to 50% on trust for Mr Rofe.

(ii) Did Emerald receive the Mercantile Share with notice of the trust?

The priority dispute between Mr Rofe and Emerald involved competition between the holders of an equitable interest and a later legal estate in the Mercantile Share. This involved consideration of whether Emerald was a bona fide purchaser for value without notice. While the parties approached the matter on the basis that Mr Rofe bore the onus of proof that Emerald had notice of the trust, her Honour considered the better view is that the onus of proof lies on the holder of the legal estate.

Her Honour preferred the evidence of Mr Rofe over the evidence of Mr Bardella, director of Emerald, finding that Emerald had actual knowledge that Mr Rofe was a beneficial owner as to 50 % of the Mercantile Share. Therefore, Emerald received the Mercantile Share with notice of the trust on which Mr Payne held that share as to 50% for Mr Rofe.

Based on the findings under headings (i) and (ii) above, her Honour declared that Emerald holds 50% of the Mercantile Share on trust for Mr Rofe and ordered that Emerald pass a members' resolution splitting the Mercantile Share into two shares in accordance with s. 254H of the Corporations Act and that upon the resolution being passed, Mercantile is to record in its register that Mr Rofe holds one of the two issued shares.

(iii) Did Emerald agree with Mr Rofe to issue shares in Mercantile to give him a 50% interest?

Again, her Honour preferred the evidence of Mr Rofe over the evidence of Mr Bardella, finding that Mr Bardella agreed with Mr Rofe that once Emerald obtained the shares in Mercantile it would transfer 50% of the shares to Mr Rofe.

Emerald contended that any oral agreement with Mr Rofe is unenforceable as it was required to be in writing by s. 23C(1)(c) of the Conveyancing Act 1919 No. 6 (NSW). Subject to the issue of part performance, her Honour accepted that contention. With respect to part performance, her Honour concluded that the evidence was insufficient to establish that Mr Rofe's acceptance of the appointment as a director of Mercantile on 15 March 2016 was unequivocally and in its nature referable to some assurance that Emerald would recognise his 50% interest in Mercantile and issue him shares reflecting that interest once it had obtained control of the company from Mr Payne.

(iv) Was the summary dismissal of Mr Rofe justified?

Mercantile claimed the summary dismissal was warranted by reason of Mr Rofe's breach of fiduciary and statutory duties to Mercantile due to Mr Rofe:

- claiming and receiving payments from Mercantile for remuneration to which he was not entitled;
- causing Mercantile to make payments totalling $50,000 to a company in which he had a 50% beneficial interest and in respect of which Mercantile received no benefit;
- causing Mercantile to make payments to a third party of $31,715 for services other than for the benefit of Mercantile;
- causing Mercantile to enter into a lease of residential premises for Mr Rofe's personal benefit; and
- using a fuel card and credit card provided by Mercantile to pay for personal expenses totalling $15,023.22.

The question for determination was whether the conduct complained of showed that Mr Rofe disregarded the essential conditions of the contract of employment. With respect to the first allegation, her Honour found that Mercantile established that Mr Rofe's conduct in rendering invoices and causing payment to be made to himself in excess of his contractual entitlement was a breach of s. 182(1) of the Corporations Act. Counsel for Mr Rofe accepted that if Mr Rofe was not entitled to remuneration of $200,000 gross per annum then his claim for summary dismissal must fail. Nonetheless, for completeness, her Honour considered the other grounds relied upon by Mercantile.

With respect to the second allegation, her Honour found that Mr Rofe breached s. 181(1) of the Corporations Act. Her Honour rejected the third allegation based on evidence that Mercantile received services from the third party. Regarding the fourth allegation, her Honour found that while it represented a breach of Mr Rofe's employment contract, given the relatively small amount ($5,950) it did not amount to a repudiation entitling summary dismissal. As to the last allegation, her Honour did not find that the conduct amounted to a repudiation.

Based on the above findings, her Honour held that Mercantile is entitled to recover $179,063.34 as damages or compensation under s. 1317H of the Corporations Act.

6.8 Compulsory acquisitions of shares under Part 6A.2

(By Yael Boneh, Herbert Smith Freehills)

Ijack Pty Ltd v Cobb, in the matter of Vealls Limited [2018] FCA 1321 (29 August 2018) Federal Court of Australia, Moshinsky J

(a) Summary

Ijack Pty Ltd (Ijack) sought the court's approval of a compulsory acquisition of income shares in Vealls Limited (Vealls). The acquisition was opposed on the grounds that Ijack did not hold full beneficial interests in at least 90% of the securities in Vealls and that the offered price did not give fair value.

Moshinsky J found, in accordance with s. 664A(2) of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act), that:

- Ijack was a 90% holder in relation to the income shares;
- that the relevant compulsory acquisition notice was lodged within the six month period prescribed by s. 664AA(b);

- that the standing and procedural requirements for approval of the compulsory acquisition of outstanding income shares were satisfied; and
- that the terms of the compulsory acquisition gave fair value for the income shares.

(b) Facts

(i) Background

Vealls Limited (Vealls) was incorporated in April 1951 in Victoria, and had been majority owned and controlled by the Veall family since incorporation. Vealls had three classes of shares on issue, being capital shares, income shares and preference shares.

In late 2017, Vealls undertook an on-market buy-back of its capital and income shares at the following prices:

- capital shares - $14.56 per share; and
- income shares - $0.52 per share.

The buy-back announcement advised that if the Veall family was able to undertake compulsory acquisition of the Veall shares after the completion of the buy-back then it proposed to do so.

(ii) Compulsory acquisition

On 29 November 2017, Vealls announced that the Veall family had advised it that the family met the compulsory acquisition thresholds in s. 664A(2) of the Corporations Act and intended to commence the process of compulsorily acquiring all the Vealls shares not held or controlled by the family.

On 26 February 2018, the plaintiff, Ijack, issued notices of compulsory acquisition for Vealls' capital, income and preference shares. In relation to the income shares, the consideration offered was $0.57 per share.

Compulsory acquisition of the preference shares and capital shares was not contentious.

(iii) Applicable principles

The provisions dealing with the compulsory acquisition of securities by a 90% holder are set out in Division 1 of Part 6A.2 of the Corporations Act, and in particular s. 664A (threshold for general compulsory acquisition power), s. 664F (the court's power to approve acquisition), and s. 667C (valuation of securities).

(iv) Objections to the compulsory acquisition

Ijack applied to the Court for the following declaration and order:

- a declaration that the terms of the compulsory acquisition of the income shares give a fair value for the shares; and
- an order that the Court approve the acquisition of the income shares by Ijack, pursuant to s. 664F of the Corporations Act.

Shareholders who held at least 10% of the income shares covered by the compulsory acquisition notices objected to the acquisition.

These shareholders opposed Ijack's application on the following grounds:

- Ijack had not discharged its onus of proof that it and its related bodies corporate held full beneficial interests in at least 90% by value of the securities in Vealls; and
- Ijack's offered price of $0.57 per income share did not give fair value for the income shares.

(c) Decision

Moshinsky J found that the standing requirements and procedural requirements for the compulsory acquisition of the income shares were satisfied. Further, he found that the terms of the compulsory acquisition gave a fair value for the income shares.

Accordingly, the court approved the acquisition of the income shares by Ijack.

Referring to previous case law on the provisions of Part 6A.2, Moshinsky J noted that there are essentially three principal matters that an applicant under s. 664F must address:

- standing (is the applicant a 90% holder?);
- compliance with procedural requirements (has the 90% holder complied with the requirements of Part 6A.2?); and
- fair value (do the terms of the compulsory acquisition offer a fair value for the outstanding securities?).

(i) Standing - 90% holder

Ijack contended that it was a 90% holder in relation to the income shares under s. 664A(2) when it issued the compulsory acquisition notices.

The three requirements of s. 664A(2) applicable to the present case were:

- the securities were shares or convertible into shares;
- Ijack's voting power in Vealls was at least 90%; and
- Ijack held, either alone or with a related body corporate, full beneficial interests in at least 90% by value of all the securities of Vealls that were shares or convertible into shares.

The first requirement was not in issue, and the third requirement of full beneficial holding was accepted on evidence.

With regard to the second requirement, Moshinsky J accepted Ijack's reliance on s. 610 of the Corporations Act, which describe a person's "voting power" as a "person's and associates" votes being the total number of votes attached to all the voting shares in the designated body (if any) that the person or an associate has a relevant interest in. Ijack pointed to three other companies who held shares in Vealls, and who had the same ultimate holding company as Ijack. Accordingly, Ijack, together with those three companies, its associates, was a 90% holder in relation to the income shares within the meaning of s. 664A(2).

(ii) Compliance with procedural requirements

The court accepted that Ijack and its associates had complied with the relevant timing requirements for lodging a notice of compulsory acquisition, and that Ijack had complied with the procedural requirements of ss. 664B, 664C, 664E and 664F(2).

(iii) Fair value

The court had evidence from two valuation experts, Deloitte for Ijack (Deloitte Report) and Grant Thornton for the respondents.

Deloitte proposed that the fair value of Vealls shares be calculated using the ordinary realisation value of Vealls as a whole allocated across the three classes of shares in accordance with their winding up entitlements.

Grant Thornton proposed that the fair value of the income shares (with no regard to the value of the other classes of shares) be calculated using a capitalisation of future maintainable dividend valuation, applying the Gordon Dividend Growth Model.

Moshinsky J accepted the valuation method adopted in the Deloitte Report, which allocated the value of Vealls as a whole across the classes of shares, taking into account the financial risk, and voting and distribution rights, of the classes (as required by s. 667C(1)(b)).

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.