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Legislation Hotline

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Detailed Contents

1. Recent Corporate Law and Corporate Governance Developments

1.1 Draft legislation and regulations - enhanced FinTech regulatory sandbox

24 October 2017 - The federal government has released exposure draft legislation and regulations to create an enhanced regulatory sandbox to support innovation in financial services.

As announced in the 2017-18 Budget, the FinTech regulatory sandbox will allow a broad scope of activities to be tested without the need to meet all the existing licensing requirements of the Australian Securities and Investments Commission (ASIC). The enhanced regulatory sandbox will help firms overcome the initial regulatory burden and costs of licensing that may otherwise hinder innovative offerings.

Under the government's proposed legislative framework, firms can test a wider range of new and innovative FinTech products and services, including:

- providing holistic financial advice in relation to superannuation, life insurance and domestic and international securities;
- issuing and facilitating consumer credit;
- issuing non-cash payment products; and
- providing a crowd-funding service.

The 24-month testing timeframe will improve firms' ability to evaluate the commercial viability of new concepts, promoting greater competition and delivering more choice for consumers.

Firms will need to adhere to consumer protections and disclosure requirements including responsible lending obligations, best interests duty, and the need for adequate compensation and dispute resolution arrangements.

The exposure drafts and explanatory material are available on the Treasury website.

1.2 Consultation on Whistleblowers Bill 2017

23 October 2017 - The federal government has released for public consultation exposure draft legislation - the Treasury Laws Amendment (Whistleblowers) Bill 2017.

These reforms will create a single whistleblower protection regime in the Corporations Act 2001 No. 50 (Cth) (the Corporations Act), to cover the corporate, financial and credit sectors, and create a new whistleblower protection regime in the taxation law, to protect those who expose tax misconduct.

The reforms to the Corporations Act include:

- expanding the protections to a broader class of people;
- expanding the types of disclosures that will be protected under the framework;
- allowing disclosures to parliamentarians and the media in certain circumstances, if preconditions are satisfied;
- imposing new stringent obligations to maintain the confidentiality of a whistleblower's identity;
- making it significantly easier for a whistleblower to bring a claim for compensation where he or she has been victimised;
- creating a new civil penalty offence so that law enforcement agencies will be able to take action against companies where the civil standard of proof can be met; and
- requiring all large companies to have a whistleblower policy in place, with penalties for failing to do so.

The new whistleblower protections in the taxation law are broadly consistent with the enhanced protections under the Corporations Act, and will facilitate disclosures about tax misconduct being made directly to the Australian Taxation Office (ATO).

The government's recently formed Expert Advisory Panel will consider the draft legislation as part of the first phase of the Expert Panel's work. The Panel will assess the draft legislation against the recently released report of the Parliamentary Joint Committee on Corporations and Financial Services into Whistleblower Protections in the corporate, public and not-for-profit sectors (PJC Report), and will provide advice to Government on how the draft legislation measures up against the PJC Report's recommendations.

The Government will consider the Expert Panel's advice and the feedback received from the consultation before finalising the legislation for introduction to Parliament in the last sitting week of the year.

The second phase of the Expert Panel's work will involve considering the remaining recommendations in the PJC Report and providing further information and advice to Government, to assist it in formulating its response to the PJC Report.

The draft legislation and supporting explanatory material are available on the Treasury website.

1.3 Strengthening penalties for corporate and financial sector misconduct

23 October 2017 - The Treasury has published the latest consultation paper of the ASIC Enforcement Review Taskforce, *Strengthening Penalties for Corporate and Financial Sector Misconduct*.

ASIC can pursue a range of regulatory and enforcement sanctions and remedies to respond to misconduct that occurs in the corporate, financial market or financial services sectors. However, concerns have emerged in a number of forums that the penalties in the legislation administered by ASIC may not be effective in that they do not reflect community perceptions as to the seriousness of engaging in certain forms of misconduct. The following are the changes proposed by the Taskforce:

- the effect of the key positions put in the paper would be to expand the range of civil penalty provisions and to increase maximum civil penalty amounts in the Corporations Act 2001 No. 50 (Cth) and National Consumer Credit Protection Act 2009 No. 134 (Cth) (Credit Act) to:
  - for individuals, 2,500 penalty units ($525,000); and
  - for corporations, the greater of: 12,500 penalty units ($2.625 million), or three times the benefit gained (or loss avoided) or 10% annual turnover;
- this would mean increases from $200,000 (individuals) and $1 million (corporations) in the Corporations Act and 2,000 penalty units ($420,000) for individuals and 10,000 penalty units ($2.1 million) for corporations in the Credit Act;
- to broadly align with planned changes to the Australian Consumer Law, penalties in the Australian Securities and Investments Commission Act 2001 No. 51 (Cth) would increase from 2,000 penalty units ($420,000) for individuals and 10,000 penalty units ($2.1 million) for corporations to:
  - for individuals, 2,500 penalty units ($525,000); and
  - for corporations, the greater of: 50,000 penalty units ($10.5 million), three times the benefit gained (or loss avoided) or 10% annual turnover;
- in addition to increasing civil penalties ASIC would be able to seek disgorgement remedies (removal of benefits illegally obtained or losses avoided) in civil penalty proceedings brought under the Corporations, Credit and ASIC Acts;
- maximum terms of imprisonment would be increased for a range of offences. The most serious Corporations Act offences, given the nature and/or consequences of the offending (many involving dishonesty) will increase to the highest penalties available under the Act; ten years imprisonment, 4,500 penalty units ($945,000) or three times benefits (individuals) and 45,000 penalty units ($9.45 million) or three times benefits or 10% annual turnover (corporations);
- maximum fine amounts for other criminal offences would also increase, and be standardised by reference to a formula based on length of available prison term:
  - maximum term of imprisonment in months multiplied by ten = penalty units for individuals, multiplied by a further ten for corporations; and
- for strict liability offences, the lowest level fines would increase and ASIC would be able to deal with these offences through the existing penalty notice regime as an alternative to prosecution; and
- ASIC would also be able to deal with a wider range of offences through infringement notice regimes.

The consultation paper is available on the Treasury website.

1.4 Three quarters of companies worldwide yet to acknowledge climate change as a financial risk

13 October 2017 - Almost three quarters (72%) of large and mid-cap companies worldwide do not acknowledge the financial risks of climate change in their annual financial reports, according to the KPMG Survey of Corporate Responsibility Reporting 2017.

Of the minority that do acknowledge climate-related risk, less than one in 20 (4%) provides investors with analysis of the potential business value at risk.

KPMG's survey studied annual financial reports and corporate responsibility reports from the top 100 companies by revenue in each of 49 countries: a total of 4,900 companies.

It found only five countries in the world where a majority of the top 100 companies mention climate-related financial risks in their financial reports: Taiwan (88%), France (76%), South Africa (61%), US (53%) and Canada (52%). In most cases, disclosure of climate-related risk is either mandated or encouraged in these countries by the government, stock exchange or financial regulator.

In terms of industries, companies in the Forestry & Paper (44%), Chemicals (43%), Mining (40%) and Oil & Gas sectors (39%) have the highest rates of acknowledging climate-related risk in their reporting. They are closely followed by the Automotive (38%) and Utilities (38%) sectors. Healthcare (14%), Transport & Leisure (20%) and Retail (23%) are the sectors least likely to acknowledge climate risk.

When looking specifically at the world's 250 largest companies (G250), public acknowledgment of climate-related financial risk is more common but still far from universal. French-based multi-nationals lead with 90% acknowledging climate-related risk, followed by majors headquartered in Germany (61%) and the UK (60%).

Around two thirds of G250 companies in the Retail (67%) and Oil & Gas (65%) industries acknowledge the risk but only around one third (36%) of major Financial Services firms do so. However, the research found only six G250 companies that have informed investors of the potential financial impact of climate risk through quantification or scenario modelling.

1.5 Reserve Bank of Australia Financial Stability Review

13 October 2017 - The Reserve Bank of Australia (RBA) has published the latest Financial Stability Review which provides the Bank's assessment of the current condition of the Australian financial system and potential risks to financial stability. One of the topics discussed in the Review is the Bank's assessment of the global financial environment.

The Review is available here.

1.6 Report on ethnic and cultural diversity of UK boards

12 October 2017 - The Parker Review Committee, led by Sir John Parker, has published its Final Report urging business leaders to improve the ethnic and cultural diversity of UK Boards to better reflect their employee base and the communities they serve.

The report sets out objectives and timescales to encourage greater diversity, and provides tools to support Board members of UK companies to address the issue. The Review's recommendations fall under the following three areas:

- increase the ethnic diversity of UK Boards by proposing each FTSE 100 Board to have at least one director from an ethnic minority background by 2021 and for each FTSE 250 Board to do the same by 2024;
- develop a pipeline of candidates and plan for succession through mentoring and sponsoring; and
- enhance transparency and disclosure to record and track progress against the objectives.

As at the end of July 2017, only 85 of the 1,050 director positions in the FTSE 100 are held by people from ethnic minorities. Only 2% of director positions are held by people from ethnic minorities who are UK citizens, despite this group making up 14% of the total UK population (up from 2% in 1971). 51 companies of the FTSE 100 do not have any ethnic minorities on their Boards.

The Report is available here.

1.7 IOSCO report on credit rating agencies

11 October 2017 - The Board of the International Organization of Securities Commissions (IOSCO) has published a report titled Other CRA Products (OCPs), which provides market participants with a better understanding of certain non-traditional products and services offered by credit rating agencies (CRAs).

These non-traditional products may include, for example, private ratings, confidential ratings, expected ratings, indicative ratings, prospective ratings, provisional ratings, preliminary ratings, one-time ratings, regional ratings, national ratings, point-in-time ratings, scoring, credit default swap spreads, bond indexes, portfolio assessment tools, credit assessments, rating assessments, assessments, fund ratings, data feeds, research or other tools.

Although OCPs and services are distinct from commonly identified issuer-paid or subscriber-paid traditional credit ratings, they may be used by market participants to make investment and other credit- related decisions. Issuers and obligors may also use them to make decisions about whether to obtain a traditional credit rating from a particular CRA.

The final report on OCPs describes six groups of OCPs and their current status, as well as business practices and trends within the CRA industry. The report concludes that OCPs should be responsive to the spirit of the four high level objectives set out in the IOSCO Principles Regarding the Activities of Credit Rating Agencies and which relate to the quality and integrity of the rating process; independence and conflicts of Interest; transparency and timeliness of ratings disclosure; and confidential information.

1.8 SEC proposes rules to implement FAST Act mandate to modernise and simplify disclosure

11 October 2017 - The US Securities and Exchange Commission (SEC) has proposed amendments to modernise and simplify disclosure requirements for public companies, investment advisers, and investment companies and to implement a mandate under the *Fixing America's Surface Transportation (FAST) Act*. The proposed amendments would make adjustments to update, streamline or otherwise improve the Commission's disclosure framework.

The proposal reflects changes based on recommendations in the staff's FAST Act Report and amendments developed as part of a broader review of the Commission's disclosure system.

The highlights of the proposed amendments are set out on the SEC website.

1.9 FSB publishes progress report on implementation of IBOR reforms

10 October 2017 - The Financial Stability Board (FSB) has published a progress report on implementation of the FSB's 2014 recommendations to reform major interest rate benchmarks such as key interbank offered rates (IBORs). The 2014 recommendations included measures to strengthen benchmarks and other potential reference rates based on interbank markets, as well as developing alternative nearly risk-free benchmark rates (RFRs). The recommendations were made following examples of attempted market manipulation and false reporting of global reference rates, together with the post-crisis decline in liquidity in interbank unsecured funding markets.

The progress report concludes that IBOR administrators have continued to take important steps to implement the FSB's recommendations, including steps to adjust methodologies used to calculate benchmark rates. However, in the case of some IBORs, such as LIBOR and EURIBOR, underlying reference transactions in some currency-tenor combinations are scarce and submissions therefore necessarily remain based on a mixture of factors including transactions and judgment by submitters. Regulators have taken a number of steps to address these issues, including developing powers to require mandatory contributions to benchmarks, but it remains challenging to ensure the integrity and robustness of benchmarks and it is uncertain whether submitting banks will continue to make submissions over the medium to long-term.

1.10 APRA releases results of stakeholder survey

10 October 2017 - The Australian Prudential Regulation Authority (APRA) has released its *2017 Stakeholder Survey Report*, which found very strong agreement amongst regulated entities that APRA's supervision and enforcement of prudential requirements helped to protect the financial well-being of the Australian community, and benefited their industry in general.

The survey, conducted on APRA's behalf by Orima Research, collated feedback from 320 financial sector companies including banks and credit unions, life, general and private health insurers, superannuation funds and industry associations.

Other strongly positive findings included that:

- APRA's supervision was consistent with its mission;
- APRA's supervision had a positive impact on risk management practices and risk culture; and
- APRA was effective in enforcing its prudential requirements.

In relation to areas for improvement, survey participants encouraged APRA to enhance its analysis of the relative costs and benefits of regulation on industry.

The Report is available here.

1.11 Report on reform of the US capital markets

6 October 2017 - The US Department of the Treasury has released a report detailing how to streamline and reform the US regulatory system for the capital markets.

Over the last 20 years, the United States has seen a nearly 50% decline in the number of publicly traded companies. In the report, Treasury identifies a series of reforms, including:

- streamlining disclosure requirements to reduce costs for companies while providing investors the information they need to make investment decisions;
- tailoring the disclosure and other requirements for companies going public based on their size; and
- re-examining the JOBS Act to identify how its tools can be improved.

Additionally, Treasury found that the federal financial regulatory framework and processes could be improved by:

- evaluating the regulatory overlaps and opportunities for harmonization of SEC and CFTC regulation;
- incorporating more robust economic analysis and public input into the rulemaking process in order to make the rulemaking process more transparent;
- opening up private markets to more investors through proposals to facilitate pooled investments in private or less liquid offerings, and revisit the "accredited investor" definition;
- limiting imposing new regulations through informal guidance, no-action letters or interpretation, instead of through notice and comment rulemaking; and
- reviewing the roles, responsibilities and capabilities of self-regulatory organizations (SROs) and making recommendations for improvements.

Treasury's review of the derivatives market found the need for greater harmonization between the SEC and CFTC, more appropriate capital and margin treatment for derivatives, and resolution of cross-border frictions that fragment global markets.

Additional recommendations in the report include:

Improving the oversight of financial market utilities (FMUs), such as by FSOC continuing to study the role FMUs play in the financial system, and regulators considering appropriate risk management for FMUs in order to avoid taxpayer-funded bailouts;

- repealing ss. 1502, 1503, 1504 and 953(b) of the *Dodd-Frank Act*;
- investigating how to reduce costs of securities litigation for issuers;
- increasing the amount that can be raised in a crowdfunding offering from US$1 million to US$5 million;
- examining the impact of Basel III capital standards on secondary market activity in securitized products; and
- advancing US interests and promoting a level playing field in the international financial regulatory structure.

The report is available here.

1.12 Report on corporate culture in the boardroom

4 October 2017 - The US National Association of Corporate Directors (NACD) has released The Report of the NACD Blue Ribbon Commission on Culture as a Corporate Asset, which calls on boards of directors to take a proactive approach to culture oversight as a means to driving sustained success and long-term value creation.

The report contains recommendations and specific action steps board members can take to elevate culture-oversight practices in key areas including CEO selection and evaluation; executive compensation design; discussions with management about strategy, risk, and performance; and assessing culture inside the boardroom.

The report's toolkit includes materials all boards can use to benchmark their current practices and implement improvements, including the following:

- Boardroom discussion guides with specific questions on a range of culture-related topics;
- Guidelines for developing board-level culture metrics and reporting;
- "Red flags" that indicate potential breakdowns in culture;
- Templates for board-member guiding principles and director codes of conduct; and
- Examples of culture survey questions and board disclosures.

1.13 Reforms to stop corporate avoidance of employee entitlements at taxpayers' expense

3 October 2017 - The Employment Minister Michaelia Cash, and Revenue and Financial Services Minister Kelly O'Dwyer MP, have announced that the government will introduce new laws to stop corporate misuse of the Australian Government's Fair Entitlements Guarantee (FEG) scheme.

Some company directors are misusing the FEG scheme to meet liabilities that can and should be paid directly by the employer rather than passed on to Australian taxpayers. The FEG scheme is an avenue of last resort that assists employees when their employer's business fails and the employer has not made adequate provision for employee entitlements.

The proposed changes will provide a significant disincentive for employers to exploit the taxpayer-funded scheme and avoid their responsibilities to their employees. The changes will:

- penalise company directors and other persons who engage in transactions which are directed at preventing, avoiding or reducing, employer liability for employee entitlements;
- ensure recovery of FEG from other entities in a corporate group where it would be just and equitable and where those other entities have utilised the human resources of the insolvent entity on other than arm's length terms; and
- strengthen the ability under the law to sanction directors and company officers with a track record of insolvencies where FEG is repeatedly relied upon.

Costs under the FEG scheme have dramatically increased in recent years with FEG payments totalling more than $1 billion between 2012-13 and 2015-16. There is increasing evidence that some employers are deliberately structuring their corporate affairs to avoid paying employee entitlements when a business becomes insolvent.

1.14 FSB publishes consultation on Unique Product Identifier (UPI) governance

3 October 2017 - The FSB has published a consultation document on proposed Governance arrangements for the unique product identifier (UPI). The consultation sets out proposals for the

governance arrangements for a global UPI, as a key harmonised identifier designed to facilitate effective aggregation of transaction reports about over-the-counter (OTC) derivatives markets.

G20 Leaders agreed at the Pittsburgh Summit in 2009, as part of a package of reforms to the OTC derivatives markets, that all OTC derivatives transaction should be reported to trade repositories (TRs). A lack of transparency in these markets was one of the key problems identified by the financial crisis. Trade reporting, by providing authorities with data on trading activity, is a key part of efforts to identify and address financial stability risks from these markets.

The primary purpose of the UPI is to identify the product that is the subject of OTC derivatives transactions. A UPI would be assigned to each product enabling regulators to aggregate data on OTC transactions by product using either the UPI or individual underlying data elements that make up the UPI. To use the data from trade reporting effectively, it is important for authorities to be able to aggregate reporting not only to consider institution-specific risks but also to consider system-wide risks.

1.15 Central banks propose strategy to improve the security of wholesale payments

28 September 2017 - The Committee on Payments and Market Infrastructures (CPMI), the global standard setter for payment, clearing, settlement and related arrangements, laid out a strategy to improve the security of wholesale payments that involve banks, financial market infrastructures and other financial institutions.

The consultative document, Discussion note - Reducing the risk of wholesale payments fraud related to endpoint security, aims to help focus industry efforts to tackle the increasing threat of wholesale payments fraud. It sets out seven elements designed to address all areas relevant to preventing, detecting, responding to and communicating about wholesale payments fraud.

1.16 Guidance to help boards consider stakeholder interests

26 September 2017 - The UK Governance Institute and the Investment Association have launched guidance to help company boards ensure they understand and weigh up the interests of their stakeholders when making strategic decisions.

The guidance identifies ten principles to guide the way boards approach these issues. They cover: identifying key stakeholders; the composition of the board and development of directors; the way in which boards receive and process information; designing appropriate engagement mechanisms; and reporting and feedback to shareholders and stakeholders.

The ten principles are:

- boards should identify, and keep under regular review, who they consider their key stakeholders to be and why;
- boards should determine which stakeholders they need to engage with directly, as opposed to relying solely on information from management;
- when evaluating their composition and effectiveness, boards should identify what stakeholder expertise is needed in the boardroom and decide whether they have, or would benefit from, directors with directly relevant experience or understanding;

- when recruiting any director, the nomination committee should take the stakeholder perspective into account when deciding on the recruitment process and the selection criteria;
- the chairman - supported by the company secretary - should keep under review the adequacy of the training received by all directors on stakeholder-related matters, and the induction received by new directors, particularly those without previous board experience;
- the chairman - supported by the board, management and the company secretary - should determine how best to ensure that the board's decision-making processes give sufficient consideration to key stakeholders;
- boards should ensure that appropriate engagement with key stakeholders is taking place and that this is kept under regular review;
- in designing engagement mechanisms, companies should consider what would be most effective and convenient for the stakeholders, not just the company;
- the board should report to its shareholders on how it has taken the impact on key stakeholders into account when making decisions;
- the board should provide feedback to those stakeholders with whom it has engaged, which should be tailored to the different stakeholder groups.

The guidance is available here.

2. Recent ASIC Developments

2.1 Release of update to evidence metrics for performance reporting

20 October 2017 - ASIC has released updated evidence metrics to report against six common key performance indicators (KPIs) in the federal government's *Regulator Performance Framework* (Framework).

Following ASIC's first self-assessment against the Framework in 2015-16, ASIC identified some ways to improve ASIC's metrics as it had become apparent that some of ASIC's metrics had become outdated as business processes changed over time.

These changes include:

- grouping related KPIs together, to tell a coherent performance story;
- making sure the metric is only listed once and placed under the most relevant KPI; and
- changing some metrics that were excessively specific, so they remain relevant as ASIC's processes change.

The updated metrics follow consultation with industry in June 2017.

Download

- Revised Regulator Performance Framework metrics; and
- Report 548 Response to submissions on amendments to ASIC's evidence metrics under the Regulator Performance Framework including non-confidential submissions to our stakeholder consultation.

2.2 Appointment of the Australian Securities and Investments Commission Chair

On 17 October 2017, Revenue and Financial Services Minister Kelly O'Dwyer, announced that the government intends to recommend to the Governor-General in Council that Mr James Shipton be appointed as the full-time Chair of ASIC for a five-year period from 1 February 2018.

Mr Shipton is currently the Executive Director of the Program on International Financial Systems at Harvard Law School. From 2013 to 2016 he was the Executive Director, Intermediaries Supervision and Licensing Division at the Hong Kong Securities and Futures Commission. Prior to that he spent nine years at Goldman Sachs - five years as Head of Hedge Fund Consultancy and four years as Head of Government and Regulatory Affairs in the Asia Pacific. Before joining Goldman Sachs, Mr Shipton was a Director of Eurekahedge Advisers and Managing Director of Compliance Asia, based in Singapore, and Vice President at Dresdner Kleinwort Wasserstein in both Hong Kong and London. He commenced his career as a lawyer at Linklaters and Blake Dawson Waldron.

2.3 Consultation on improving the financial capabilities of Australians

16 October 2017 - The *National Financial Literacy Strategy* sets out a plan to strengthen the financial capabilities of all Australians with the aim of improving financial outcomes.

A key feature of the National Strategy is collaboration across different sectors, including government agencies, community organisations, the education sector and financial services firms. ASIC is leading a public consultation process to shape the National Strategy from 2018 and is seeking feedback on a number of issues including:

- updating the language of the National Strategy from "financial literacy" to "financial capability" to reflect a growing focus on behaviours that support better financial outcomes;
- expanding the priority audiences identified under the National Strategy, for example to include people with disability (and their families or carers) who are navigating choices and options under the National Disability Insurance Scheme, or people in newly arrived communities who are attempting to understand and access financial services;
- broadening stakeholder reach and engagement with the National Strategy, including through the use of new technologies; and
- improving research, measurement and evaluation.

Download

- Consultation paper

2.4 Update on interest-only home loans

11 October 2017 - ASIC has provided an update on its targeted review of interest only home loans. Announced in April 2017, the review was a targeted industry surveillance examining whether lenders and mortgage brokers are inappropriately recommending more expensive interest-only loans.

With many lenders, including major lenders, charging higher interest rates for interest-only loans compared with principal-and-interest loans, lenders and brokers must ensure that consumers are not provided with unsuitable interest-only home loans.¡¡

ASIC has concluded the first stage of its targeted review, which involved data collection from 16 home loan providers (including large banks, mid-tier and smaller banks, and non-bank lenders). ASIC found that Australia's major banks have cut back their interest-only lending by $4.5 billion over the past year. However, other lenders have partially offset this decline by increasing their share of interest-only lending.

ASIC's interest-only lending review has also found:

- Borrowers who used brokers were more likely to obtain an interest-only loan compared to those who went directly to a lender; and
- Borrowers approaching retirement age continue to be provided with a significant number of interest-only owner-occupier loans.

ASIC has moved into the second stage of its review, and will be reviewing individual loan files from both lenders and mortgage brokers. These lenders and mortgage brokers have been selected based on a number of criteria, including their relative share of interest-only home lending.

2.5 Finalisation of client money reporting rules

10 October 2017 - ASIC has released the finalised ASIC Client Money Reporting Rules 2017 (client money rules) which, from 4 April 2018, will impose record-keeping, reconciliation and reporting obligations on Australian financial services (AFS) licensees that hold "derivative retail client money" within the meaning of the Corporations Act, unless the client money relates to a derivative that is traded on a fully licensed domestic market, such as ASX 24.

The final client money rules incorporate some changes in response to industry consultation and feedback on Consultation Paper 291 *Reporting rules: Derivative retail client money* (CP 291), issued in July 2017 (refer: 17-231MR).

ASIC's response to the submissions it received during the consultation is detailed in Report 546 *Response to submissions on CP 291 Reporting rules: Derivative retail client money* (REP 546).

ASIC has also released Information Sheet 226 *Complying with the ASIC Client Money Reporting Rules 2017* (INFO 226) *to assist AFS licensees comply with their obligations under the client money rules.*

The release of the client money rules follows the passage of Treasury Laws Amendment (2016 Measures No. 1) Act 2017 No. 25 (Cth) and the Corporations Amendment (Client Money) Regulations 2017. These reforms will prevent AFS licensees from withdrawing client money provided by retail derivative clients, and using it for the wide range of purposes currently permitted under the Corporations Act, including as the AFS licensee's own working capital.

The client money rules will commence on 4 April 2018, at the same time the other client money reforms take effect. This gives AFS licensees a six month transition period to ensure they have the necessary systems, policies and procedures for complying with the client money rules.

The release of the client money rules and guidance follows public consultation in July 2017 (see 17-231MR).

Download

- ASIC Client Money Reporting Rules 2017;
- Information Sheet 226 Complying with the ASIC Client Money Reporting Rules 2017;
- Treasury Laws Amendment (2016 Measures No. 1) Act 2017;
- Corporations Amendment (Client Money) Regulations 2017; and
- Report 546 Response to submissions on CP 291 Reporting rules: Derivative retail client money.

2.6 Remake of "sunsetting" class order about mortgage schemes

4 October 2017 - ASIC has remade Class Order [CO 02/238] *Mortgage schemes - Chapter 5C and disclosure relief*, which was due to expire on 1 October 2017. The new instrument, ASIC Corporations (Mortgage Investment Schemes) Instrument 2017/857, continues to provide:

- scheme registration, licensing, disclosure, and hawking relief for certain small-scale schemes with no more than 20 members;
- scheme registration relief in relation to individual mortgages in a scheme; and
- withdrawal-related relief for individual mortgages in a scheme.

ASIC has temporarily extended the relief given under [CO 02/238] for small, industry-supervised schemes. The Legal Profession Uniform Law as it applies to the promotion and operation of managed investment schemes by law practices is due to come into force on 1 July 2018. ASIC will review the extension within 12 months of issue and assess whether it should be remade and, if so, whether it is operating effectively and efficiently.

ASIC has not continued the transitional "run-out" relief provided by [CO 02/238] as it was no longer necessary.

Consultation Process

The relief was remade following public consultation in Consultation Paper 287 *Remaking ASIC class order on mortgage schemes and proposed relief for multiple withdrawal periods* (CP 287), issued in June 2017.

All respondents were supportive of the proposals in CP 287. ASIC has included material in the explanatory statement for the new instrument to provide clarity regarding:

- the status of the temporarily extended, industry-supervised scheme relief if s. 258 of the Legal Profession Uniform Law comes into effect; and
- the scope of the withdrawal-related relief for individual mortgages in a scheme.

Download

- ASIC Corporations (Mortgage Investment Schemes) Instrument 2017/857;
- ASIC Corporations (Repeal) Instrument 2017/858;
- CP 287.

2.7 Remake of "sunsetting" class order providing licensing relief for trustees of wholesale equity schemes

29 September 2017 - ASIC has remade Class Order [CO 07/74] *Wholesale equity schemes: Licensing relief for trustees*, which provides relief, in specified circumstances, to trustees of wholesale equity schemes from the requirement to obtain an Australian financial services (AFS) licence. The Class Order was due to expire (sunset) on 1 October 2017.

The new instrument, ASIC Corporations (Wholesale Equity Scheme Trustees) Instrument 2017/849 has been updated to take into account a strengthening, in 2013, of financial and custody requirements as outlined in Class Order [CO 13/760] *Financial requirements for responsible entities and operators of investor directed portfolio services*, Class Order [CO 13/761] *Financial requirements for custodial and depository services* and Class Order [CO 13/1410] *Holding assets: Standards for providers of custodial and depository services*. The financial and custody requirements were not reflected in [CO 07/74].

ASIC has also issued ASIC Corporations (Amendment and Repeal) Instrument 2017/848, which repeals [CO 07/74] and amends [CO 13/760] and [CO 13/761] as they apply to managers of wholesale equity schemes so that they are consistent with the requirements in the new instrument.

Consultation process

The relief was remade following public consultation in Consultation Paper 280 *ASIC class order on wholesale equity schemes: Licensing relief for trustees - [CO 07/74]* (CP 280), issued in March 2017.

All of the respondents expressed the view that the relief in [CO 07/74] continues to form a useful regulatory purpose and were broadly supportive of the changes proposed in CP 280.

Report 545 *Response to submissions on CP 280 ASIC class order on wholesale equity schemes* (REP 545) highlights the key issues that arose out of the submissions received on CP 280 and ASIC's responses to those issues.

Download

- Report 545;
- Non-confidential submissions to CP 280;
- ASIC Corporations (Wholesale Equity Scheme Trustees) Instrument 2017/849;
- ASIC Corporations (Amendment and Repeal) Instrument 2017/848;
- Consultation Paper 280.

2.8 Provision of guidance for initial coin offerings

28 September 2017 - ASIC as released guidance to help issuers of initial coin offerings (ICOs) consider their legal obligations when offering coins or tokens.

ASIC and the Australian Competition and Consumer Commission (ACCC) also jointly warned people of the potential risks of investing in ICOs.

Information sheet 225 provides guidance about the potential application of the *Corporations Act 2001* to businesses that are considering raising funds through an initial coin offering.

ASIC's MoneySmart website has also published guidance for investors on the risks of investing in initial coin offerings.

2.9 Repeal of "sunsetting" class orders relating to prime broking and holding client assets

28 September 2017 - ASIC has repealed three class orders relating to prime broking and the holding of client assets, which were due to expire (sunset) on 1 October 2017. These were:

- ASIC Class Order [CO 03/1110] *Prime brokerage: Relief from holding client property on trust*
- ASIC Class Order [CO 03/1111] *Prime brokerage: Relief from holding scheme property separately*
- ASIC Class Order [CO 03/1112] *Relief from obligation to hold client money on trust*

To permit adequate time for potentially affected stakeholders to consider making alternative arrangements, ASIC has extended the operation of Class Orders [CO 03/1110] and [CO 03/1112] by 12 months to 30 September 2018.

ASIC has also amended ASIC Class Orders [CO 13/1409] *Holding assets: Standards for responsible entities* and [CO 13/1410] *Holding assets: Standards for providers of custodial and depository services* because they contained references to the repealed Class Orders.

The relevant instrument is the ASIC (Amendment, Repeal and Transitional) Instrument 2017/839.

ASIC decided to repeal the Class Orders following public consultation through Consultation Paper 273 *Repealing ASIC class orders on holding client assets* (CP 273), issued in November 2016.

CP 273 sought feedback on ASIC's proposal to discontinue the relief in [CO 03/1110], [CO 03/1111] and [CO 03/1112].

2.10 Remake of relief for financial counselling agencies providing advice or credit assistance

27 September 2017 - ASIC has made two new instruments relating to financial counselling agencies to continue the relief provided by class orders that were due to expire (sunset).

ASIC has remade:

- Class Order [CO 03/1063] *Licensing relief for financial counselling agencies in* ASIC Corporations (Financial Counselling Agencies) Instrument 2017/792; and
- Class Order [CO 11/926] *Credit licensing exemptions for NGOs (non-government organisations) providing credit assistance to consumers* and ASIC Credit (Financial Counselling Agencies) Instrument 2015/992, in ASIC Credit (Financial Counselling agencies) Instrument 2017/793.

The new corporations instrument continues relief for financial counselling agencies from the Australian financial services (AFS) licensing, conduct and disclosure obligations in Chapter 7 of the Corporations Act 2001 No. 50 (Cth), when providing particular financial product advice.

The new credit instrument continues relief for rural financial counselling service providers from the requirement to have an Australian credit licence when providing credit assistance. It also continues amendments made to the National Consumer Credit Regulations 2010 No. 44 (Cth) for financial counselling agencies.

The relief was made without substantive changes following public consultation through Consultation Paper 282 *Remaking ASIC class orders on financial counselling licensing relief* (CP 282).

Download

- ASIC Corporations (Financial Counselling Agencies) Instrument 2017/792;
- ASIC Credit (Financial Counselling agencies) Instrument 2017/793; and
- Non-confidential submissions received to CP 282.

3. Recent ASX Developments

3.1 Amendments to ASX Listing Rules to regulate reverse takeovers

Effective 1 December 2017, ASX has amended the ASX Listing Rules to require shareholder approval for reverse takeovers. ASX has also made amendments to the voting exclusions in Listing Rule 14.11, and to Listing Rules 1.2 and 1.3 to clarify the accounts that an applicant for listing must provide to ASX with its listing application.

The final Listing Rule Amendments are available here.

3.2 ASIC and RBA welcome the publication of ASX BBSW Trade and Trade Reporting guidelines

On 10 October 2017 ASIC and the RBA welcomed the publication of the ASX BBSW Trade and Trade Reporting Guidelines (ASX BBSW Guidelines).

The bank bill swap rate (BBSW) is the major interest rate benchmark for the Australian dollar and is widely referenced in financial contracts. A major concern over recent years has been the low trading volumes during the rate set window, the time of day that BBSW is measured. In response, the BBSW methodology is being strengthened to enable the benchmark to be calculated directly from a wider set of market transactions. ASX, the Administrator of BBSW, has been consulting market participants on this new methodology with the strong support of ASIC and the RBA.

The ASX BBSW Guidelines are an important part of the new BBSW methodology, as they provide guidance on the trading of bank bills during the rate set window. The ASX BBSW Guidelines also set out how these trades should be reported to the ASX to support the timely calculation and publication of BBSW.

3.3 Monthly activity report

On 5 October 2017 ASX released the ASX Monthly Activity Report for September 2017.

4. Recent Takeovers Panel Developments

4.1 RNY Property Trust - Panel declines to conduct proceedings

4 October 2017 - The Takeovers Panel has declined to conduct proceedings on an application dated 27 September 2017 from Aurora Funds Management Limited (Aurora) as responsible entity of the Aurora Property Buy-Write Income Trust in relation to the affairs of RNY Property Trust (RNY).

RNY is the subject of an off-market takeover bid for all the units in RNY not owned by Aurora. The application concerned, among other things, whether the implementation by RNY of its cash distribution strategy would constitute an unacceptable frustrating action and whether disclosure in the target's statement was adequate (see TP17/49).

The Panel considered that it was unlikely to find that taking steps in implementing RNY's cash distribution strategy would be a frustrating action giving rise to unacceptable circumstances since details of the strategy had been announced prior to the announcement of Aurora's bid.

The Panel was concerned that the risk that RNY unitholders may not receive any cash distribution, following implementation of RNY's cash distribution strategy, was not given sufficient prominence in RNY's target statement. However in the exceptional circumstances of this case, the Panel decided not to conduct proceedings on this issue. The Panel noted that if RNY fails to address the issue in a supplementary target's statement, Aurora could highlight this deficiency in a supplementary bidder's statement.

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

4.2 Asia Pacific Data Centre Group - Panel Declines to Conduct Proceedings

16 October 2017 - The Takeovers Panel has declined to conduct proceedings on an application dated 9 October 2017 from NEXTDC Limited in relation to the affairs of Asia Pacific Data Centre Group.

Asia Pacific Data Centre Group is the subject of an off-market takeover bid by 360 Capital FM Limited (in its capacity as trustee for the 360 Capital Diversified Property Fund) for all stapled securities in Asia Pacific Data Centre Group that it does not own. The application concerned, amongst other things, whether disclosure in the bidder's statement and the target's statement was adequate in respect of a proposed capital distribution which may be implemented after the end of the offer period (see TP17/52).

The Panel noted that the bidder's statement discloses that the implementation of the proposed capital distribution is subject to the decision and legal obligations of Asia Pacific Data Centre, and that 360 Capital will only make a decision to proceed following legal and financial advice on those requirements.

The Panel considered that further disclosure would require speculation on various matters, including the circumstances at the time the proposed capital distribution is implemented, and the Panel considered it unlikely that such speculation would contribute to an informed market. The Panel noted that NEXTDC has already highlighted its concerns in its announcement to the market on 26 September 2017, and 360 Capital responded to the announcement on 27 September 2017.

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

5. Recent Research Papers

5.1 Compensation consultants and the level, composition and complexity of CEO pay

Firms that use consultants have higher-paid CEOs. This paper shows that this positive and robust association is not only driven by consultant conflicts of interest but also (and even to a larger degree) by the composition and complexity of pay: firms using consultants compensate their CEOs with a higher percentage of incentive pay and more complex incentive plans, which in turn, are associated with higher levels of pay. The paper also shows that, among firms that do not retain consultants, firms that pay more to their CEOs and use more complex incentive plans, are more likely to hire compensation consultants the following year. Finally, the paper shows that shareholders "Say-on-Pay" votes are more favourable for companies using compensation consultants, but this association is also explained by the composition and complexity of CEO pay.

Compensation consultants and the level, composition and complexity of CEO pay

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5.2 The effects of hedge fund interventions on strategic firm behaviour

This paper examines the impact of hedge fund interventions on target firms' strategic behaviour, specifically their voluntary disclosure and earnings management strategies. The paper finds a decrease in both the likelihood and the frequency of management earnings forecasts conveying bad news and an increase in the level of real earnings management following interventions by hedge fund activists. Additional evidence suggests that managers substitute between voluntary disclosure and earnings management strategies in resisting hedge fund attacks. The paper also finds that bad news withholding is more pronounced when hedge fund activists pose greater threats to the target firm's management and when the intervention lasts for a relatively short time period. The results are consistent with firms behaving strategically in response to heightened career/reputation concerns and endangered corporate control arising from hedge fund activism.

The effects of hedge fund interventions on strategic firm behaviour

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5.3 Does insider trading law change behaviour? An empirical analysis

Few issues in securities law have excited the popular imagination and generated scholarly interest like insider trading. Yet, a simple but foundational question about insider trading law has received relatively little scholarly attention: Does insider trading law actually influence the amount of insider trading that occurs? This article tackles this question in the context of one of the highest-profile changes in insider trading law in decades - the US Second Circuit's seminal 2014 decision in *United States v Newman*, which substantially weakened insider trading law concerning so called "tippee" liability. The article's empirical approach exploits Newman's change in law to empirically evaluate the effects of changes in insider trading law on insider trading. The article focuses on insider trading in advance of mergers announced in periods before and after Newman and, for its measure of the extent of insider trading, uses the runup in the stock price of the merger target in advance of the merger's public announcement. Based on that measure, the article finds that Newman had a dramatic effect on insider trading, with significantly greater insider trading occurring after Newman than before, thereby providing empirical evidence that insider trading is responsive to changes in insider trading law. The article provides the first empirical analysis of whether and the extent to which a specific judicial change in insider trading law can influence the amount of insider trading beyond just the trading of corporate insiders. The article's empirical findings advance the understanding of the functioning of securities law and inform important policy debates concerning insider trading.

Does insider trading law change behaviour? An empirical analysis

6. Recent Corporate Law Decisions

6.1 Proceedings against a company subject to a deed of company arrangement - Federal Court clarifies when litigation may take precedence

(By Rebecca Searle, King & Wood Mallesons)

Phoenix Institute of Australia Pty Ltd v Australian Competition and Consumer Commission [2017] FCAFC 155, Federal Court of Australia Full Court, Perram, Yates and Wigney JJ, 29 September 2017.

(a) Summary

The Full Court of the Federal Court of Australia recently delivered a judgment which sheds light on when a court may exercise its discretion to grant leave to bring proceedings against a company subject to a deed of company arrangement (DOCA).

A DOCA is a binding agreement between a company and its creditors to govern the management of the company's affairs. DOCAs can assist companies in financial trouble to avoid liquidation. In order to preserve the normal procedure under a DOCA and protect the interests of creditors, s. 444E(3) of the Corporations Act 2001 No. 50 (Cth) (Corporations Act) prevents a person from bringing proceedings against a company subject to a DOCA unless a court grants leave.

In deciding whether to grant leave to bring proceedings, thereby giving precedence to litigation over the normal procedure established by the DOCA, courts in exercising discretion should consider a number of factors. These factors include whether there is significant public interest in the litigation, the effects of delay in awaiting termination of the DOCA, and whether the relief sought in the proceedings is significantly wider than the relief available under the DOCA.

(b) Facts

The first applicant, Phoenix Institute of Australia Pty Ltd (Phoenix) was an approved VET course provider under the Higher Education Support Act 2003 No. 149 (Cth) (HESA). Phoenix was eligible to receive Commonwealth funding for course fees of students who enrolled with Phoenix and borrowed tuition funds from the Commonwealth. The second applicant, Community Training Initiatives Pty Ltd (CTI) provided among other things, call centre and document processing services to Phoenix.

The respondents, the ACCC and the Commonwealth of Australia, alleged that the applicants engaged in conduct that was misleading or deceptive, or likely to mislead or deceive, and unconscionable, in contravention of the Australian Consumer Law (Schedule 2 to the Competition and Consumer Act 2010 (1974) No. 51 (Cth)). The applicants allegedly targeted students from low socio-economic communities, and represented (among other things) that the courses were free and that VET FEE-HELP loans obtained from the Commonwealth were debts that would never have to be repaid. Students were often recruited for more than one course without their knowledge or consent and without the necessary skills or qualifications. Further, courses cost at least $18,000, and students were not informed of their rights to withdraw from courses. This was allegedly done to maximise revenue to Phoenix from Commonwealth payments made directly to Phoenix for each course enrolment.

The Commonwealth paid $106 million to Phoenix as an advance under the HESA (which meant that students had not yet incurred a debt to the Commonwealth), and was under an obligation to pay a further $253 million to Phoenix.

The Department of Education and Training had commenced an audit and reconciliation of Phoenix's enrolments to determine what Commonwealth funding had been validly provided, and what funding was due to the applicants' breaches of the Australian Consumer Law, and therefore should be repaid to the Commonwealth. This audit was ongoing at the time the primary decision was made.

At the time of the appeal, both applicants had ceased trading and were subject to DOCAs. Section 444E(3)(c) of the Corporations Act prevents a person from bringing proceedings against a company subject to a DOCA unless a court grants leave. The respondents therefore sought leave to displace the ordinary procedures established by the DOCAs and bring proceedings against the applicants seeking declarations, pecuniary penalties, refunds and other orders.

(c) Decision

(i) First instance decision to grant leave

The primary judge accepted the applicants' submission that defending legal proceedings would be costly. As the DOCA had limited funds to be distributed amongst creditors, this significant expenditure would be adverse to the interests of creditors. Despite this, the primary judge granted the respondents leave to bring the proceedings against the applicants.

The primary judge considered the following factors which supported displacing the normal procedure under a DOCA pursuant to s. 444E(3), and granting priority to litigation:

- the litigation involved significant public interest in informing and protecting consumers, and deterring similar conduct. The ACCC has a duty as an independent regulator to ensure accountability for contraventions of the Australian Consumer Law, promote competition and fair trading, and provide for consumer protection. These duties would all be advanced through this litigation. Further, declaratory relief that the enrolment contracts entered into by students were void, despite the fact that the students had not yet accrued a debt, would avoid financial prejudice to the students. This public interest outweighed the interests of specific creditors under the DOCAs;

- the relief sought in the proceedings was broader than the relief available under the DOCA. It included declarations to void the enrolment agreements, determinations on whether the applicants' conduct had been unconscionable, and pecuniary penalties to act as a general deterrent. The DOCA could only provide for repayment of Phoenix's debt to the Commonwealth. Therefore awaiting termination of the DOCA as the applicants had requested was not sufficient;
- a delay of the proceedings until the termination of the DOCA may impact the quality of the evidence, especially from lay witnesses; and
- there was a serious issue to be tried in the proceeding, and the claims were legally and factually complex. It was therefore appropriate for these issues to be considered by a court and not the Deed Administrators.

(ii) Appeal by applicants

The applicants appealed this decision, stating that the primary judge had granted leave prematurely. The applicants submitted that the audit would determine the amount actually owed by Phoenix to the Commonwealth, and until the outcome of the audit was known, it could not be determined whether it was in the interests of their creditors to defend these proceedings. If the audit outcome was unfavourable, the Deed Administrators may choose not to defend the proceedings. The applicants therefore argued that the proceedings were a duplication of process and should not be brought until after the audit was completed, and the DOCAs terminated.

(iii) Full Court of the Federal Court of Australia upheld leave to bring proceedings

The Court heard the application for leave and the consequent appeal concurrently, as they covered the same factual and legal territory. The Court found that leave under s. 443(3) should be granted but dismissed the appeal, ordering the applicants to pay the respondents' costs.

The Court addressed the applicants' claim of substantial injustice caused by leave being granted prior to the completion of the audit process. The applicants argued that if the result of the audit was unfavourable, the proceedings may not be defended and significant costs would be avoided, which was in the interests of creditors. The Court accepted the primary judge's determination that despite the cost burden of defending the proceedings, public interest in the litigation, and the fact that the scope of relief sought in the proceedings was broader that what the DOCAs could offer, supported the granting of leave.

The Court defended the primary judge's discretion in deciding that the expenditure of funds that would otherwise be available to the applicants' creditors did not outweigh the importance of allowing the litigation to proceed. Section 444E(3) did not require specific interests of creditors to be prioritised over a generalised public interest.

Further, the Court rejected the applicants' submission that the finding of significant public interest in the litigation was not open to the primary judge. Significant public interest was a relevant consideration especially as it would be most effectively achieved by pursuing the litigation in a timely manner (for example by avoiding financial consequences for students who were liable to become indebted to the Commonwealth). The Court also upheld the primary judge's finding that general deterrence was an appropriate consideration, regardless of whether proceedings could be brought against other VET providers to achieve the same public interest outcomes.

Finally, the Court upheld the primary judge's exercise of evaluative judgment in finding that awaiting the termination of the DOCAs would cause substantial delay, and that the quality of evidence from lay witnesses would be impacted by such a delay.

6.2 Company documents that belong to the company, not the liquidator

(By Takako Yoshizawa, Ashurst)

In the matter of S.C.W. Pty Ltd [2017] NSWSC 1314, Supreme Court of New South Wales, Black J, 28 September 2017.

(a) Summary

Justice Black of the Supreme Court of New South Wales ordered that a majority of the disputed company's books and records held by a former liquidator be returned to the company. Whether the documents belonged to the company or the former liquidator depended on the purpose for which the preparation of documents were made: for the conduct of the company's business or for the personal or private purposes of the liquidator?

(b) Facts

In this case, the applicants were S.C.W Pty Limited (SCW); Mr Leslie Schirato and Schirato Pty Ltd (SPL) and the respondent was Mr Jamieson Louttit, former liquidator of SCW.

In April 2011, SCW was wound up because of a deadlock between its two shareholders and directors. Mr Jamieson Louttit was appointed liquidator until the Applicants sought orders for termination of the winding up in March 2017.

On 10 April 2017, Gleeson JA made orders that the winding up of the company be terminated; that the liquidator deliver the company books no later than 24 April 2017; and that $157,000 be retained by the liquidator on trust, pending determination of his remuneration.

The documents that the liquidator began delivering to SCW largely comprised documents initially provided by SCW to Mr Louttit in 2011. A dispute arose between the parties as SCW argued relevant financial documents were missing. Mr Louttit argued that some documents relating to the liquidation were privileged, were his own records and were subject to claims of commercial confidentiality as many of them were received or prepared by him in the course of discharging his obligations as an agent of SCW.

(c) Decision - Key question: Was the document obtained for the management of SCW's affairs?

(i) Liquidator is an agent of the company

His Honour at [13] referred to the principle that liquidators occupy the position of agent of the company and thus, "if the liquidators take some authorised step in carrying on the business of the company, that step is binding on the company as principal¡" Specifically, the liquidators' keeping of records prepared by them in their capacity as liquidators or administrators is conduct as agent for the company and those documents are books kept by a body corporate for the purposes of s. 1305 of the Act (Admissibility of books in evidence). A liquidator's functions are performed in its fiduciary capacity, embodied in s. 477 of the Act. (See also *ASIC v Edge* [2007] VSC 170; (2007) 211 FLR 137 at [42] Dodds-Streeton J)

(ii) Determining whether the document belongs to the liquidator or company

In determining whether the document belonged to the company or the liquidator, his Honour characterised the document by asking whether the document appeared to be within the scope of managing SCW's business.

The respondent argued that not all decisions of a liquidator will be made in his or her capacity as agent of the company and that there is case law concerning solicitors and professionals that internal records or memoranda could be the property of the creators. However, his Honour distinguished the performance of the liquidator's function in this case because the application of the above principle was relevant to a liquidator adjudicating a proof of debt. His Honour rejected the application of the principle in this case as the liquidator just received or prepared the documents in managing the company's business.

Further, it was noted that if the documents prepared by the liquidator would likely have been prepared by a director, employee or adviser to SCW if SCW was not in liquidation, then the document ought to have been returned to the company.

(iii) Distinction between books of the company and the books of the liquidator

His Honour stated that s. 542 of the Act imposes a duty on a liquidator in relation to "all books of the company and of the liquidator that are relevant to the officers of the company". When receivership is terminated, the company is entitled to the return of those documents in the receiver's possession which belong to the company. Ownership depends on the capacity in which the documents were prepared or acquired. The facts of the case pointed his Honour to categorise most of the documents as belonging to the company.

(iv) Categories of documents

The following documents were categorised as being prepared by the liquidator and his staff for their own purposes and as not being SCW's property:

- internal memorandums and file notes;
- payments and receipts prepared by the respondent's staff for their benefit during the liquidation to authorise payments kept as records for the firm; and
- file note regarding part of the outcomes of a Court application regarding sale of a cause of action of SCW that seems uncontroversial.

The following documents were categorised as being prepared for the purpose of conducting SCW's business and as being SCW's property:

- correspondence with ASIC;
- summary of valuations for properties owned by SCW;
- checklist and decision sheets prepared to determine whether insurance and leasing arrangements were in place in respect of SCW's properties and whether selling agents had been appointed;
- file note to keep a record of the acceptance of offers made for SCW's properties;
- schedules to record various offers and valuations that had been made to assist the liquidator in assessing the offers and appointing real estate agents;
- schedule of property agents prepared by the liquidator's staff during the liquidation to assist him in making a decision as to which agent to appoint to market the properties for sale;
- summary of offers made to acquire a particular property;
- schedules and file notes prepared by the liquidator's staff to assist him in determining the sale value, sale process and sale offers of a substantial motor yacht; and
- a covering file note regarding ATO's comprehensive risk review.

(v) Conclusion

Mr Loutitt was ordered to return to SCW the documents which were SCW's property and granted the opportunity to remedy his non-compliance with Gleeson JA's previous order.

The applicants argued for indemnity costs, and an order that Mr Louttit would not be entitled to any remuneration for any work done in or incidental to the application or to recover any costs of or incidental to this application from SCW's monies that he still held. Justice Black stood the matter over for a further hearing.

6.3 Judicial review finds no improper conduct by ASIC during investigation

(By Stephanie Glover, DLA Piper)

Schlaepfer v Australian Securities and Investments Commission [2017] FCA 1122, 21 September 2017.

(a) Summary

ASIC conducted an investigation into trading in various securities on Australian markets by Merlito Securities Company Limited (Merlito) acting as agent for Select Vantage, Inc. (Select Vantage), being domiciled in the Cayman Islands. Mr Daniel Schlaepfer is Select Vantage's president and Chief Executive Officer. In October 2016, ASIC requested the Cayman Islands Monetary Authority (CIMA) to provide it with assistance with its investigation. CIMA subsequently issued a direction to Select Vantage which required it to provide certain specified information or documentation.

Select Vantage and Mr Schlaepfer (the president of Select Vantage) sought judicial review of ASIC's conduct in making the request to CIMA. ASIC then filed a notice of objection to competency. The Federal Court dismissed the application of Select Vantage and Mr Schlaepfer with costs.

(b) Facts

(i) Competency and jurisdiction

Select Vantage and Mr Schlaepfer sought to invoke the jurisdiction of the Court under s. 6(1) of the Administrative Decisions (Judicial Review) Act 1977 (Cth) (the ADJR Act) and also pursuant to the original jurisdiction of the Federal Court of Australia to hear matters arising under laws of Parliament pursuant to s. 39B(1A)(c) of the Judiciary Act 1903 (Cth) (the Judiciary Act). ASIC contended that the Court did not have jurisdiction to review the claim under any of these enactments.

(ii) Public interest immunity

Mr Schlaepfer and Select Vantage sought the production of ASIC's request to CIMA and related correspondence between ASIC and CIMA. ASIC claimed that it should not be compelled to produce those documents because they were the subject of a claim of public interest immunity, on the basis that ASIC and CIMA were both signatories to the International Organisation of Securities Commissions' Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information (MOU) which obliged ASIC to keep confidential all requests and other matters arising under the MOU, including consultations between regulatory counterparts.

(iii) Improper exercise of power, breach of rules of natural justice and procedural fairness

It was contended that ASIC's request to CIMA was an improper exercise of power in that it had the purpose or effect (or practical effect) of depriving Mr Schlaepfer of his privilege or immunity against giving testimonial evidence that might later be used against him in criminal or civil penalty proceedings, breached the rules of natural justice and amounted to a denial of procedural fairness.

(c) Decision

(i) Competency and jurisdiction

The Court held that it did not have jurisdiction to review the challenged conduct.

Conduct is only reviewable under s. 6 of the ADJR Act if engaged in "for the purposes of making a decision to which this Act applies" (including conduct that is preparatory to the making of a decision) and there was no basis for concluding that ASIC's conduct was engaged in for such a purpose here. Rather, the conduct of ASIC in making the request to CIMA was part of the procedure or decision-making process that would ultimately lead to ASIC making a decision in respect of its investigation under the ASIC Act. If a statute provides that various decisions may be made after or as a result of a particular administrative process, it does not necessarily follow that every act done in the course of that administrative process is reviewable as conduct engaged in for the purpose of making one of the possible decisions that might ultimately be made. Rather, the applicant who wishes to challenge conduct on this basis must show that the conduct was engaged in as part of the procedure of making a specific decision that is in contemplation or in the process of being made. The Court also observed that the requisite nexus between the procedural conduct and the decision and the conduct was absent in respect of the conduct in question because (among other things) there was no evidence of ASIC being in the process of making any relevant decision.

The Court held that it did not have jurisdiction to entertain this matter under s. 39B(1A)(c) of the Judiciary Act as the relevant matter does not arise under the ASIC Act cited or under any Commonwealth law.

(ii) Public interest immunity

The Court upheld ASIC's claim for public interest immunity and held that it did not need to inspect the relevant documents under the circumstances given that no legitimate forensic purpose in obtaining access to the documents was demonstrated. The Court took into account that Senior Counsel for Mr Schlaepfer and Select Vantage did not identify any legitimate forensic purpose for obtaining access to the documents other than "fishing" or articulate how any of the documents would advance the pleaded grounds of challenge to ASIC's conduct.

(iii) Improper exercise of power, breach of rules of natural justice and procedural fairness

The Court considered that these contentions were unsupported by the facts and evidence.

In relation to the contentions that ASIC intended to deprive Mr Schlaepfer of his privilege or immunity against self-incrimination and/or that ASIC failed to take into account a relevant consideration (being the fact that the likely result of making the request to CIMA would deprive Mr Schlaepfer of that privilege or immunity), the Court found that:

- there was no evidence to suggest that Mr Schlaepfer would be required to provide the documentation or information himself (as the request was directed at Select Vantage), let alone that he would be required to provide a representation or warranty as to the accuracy of the information provided by Select Vantage;
- the CIMA notice did not require Mr Schlaepfer to make an oral statement or sign a record, thereby not falling within the ambit of the "use immunity" under s. 68 of the ASIC Act;

- the relevant jurisdiction in which Mr Schlaepfer's claim to the privilege against self-incrimination would arise in any event would be the Cayman Islands; and
- it cannot be inferred that in making the request to CIMA, ASIC somehow intended to circumvent or abrogate any right that Mr Schlaepfer may have had to claim privilege against self-incrimination or any right he may hypothetically have had under s. 68 of the ASIC Act.

For the above reasons the Court also found no merit in the contention that ASIC breached the rules of natural justice. Finally, the Court rejected the contention that ASIC had denied Mr Schlaepfer and Select Vantage procedural fairness, stating that this submission was speculative and premature on the basis that there was no evidence of any document actually having been produced in response to ASIC's request.

6.4 Mere involvement in the day-to-day running of a business is not sufficient to establish that a person is a "de facto" director

(By Nicholas Josey, Clayton Utz)

In the matter of Central Management (NSW) Pty Ltd [2017] NSWSC 1258, Supreme Court of New South Wales, Black J, 19 September 2017.

(a) Summary

The proceedings concerned a claim commenced against a former director of Central Management (NSW) Pty Ltd (Company) and another company of his for repayment of monies owed and breaches of his director's duties.

Mr Michael Smith of SmithHancock was appointed as the liquidator of the Company on 12 October 2012 following winding up proceedings commenced by the Deputy Commissioner of Taxation, for debts owed to the ATO. Mr Smith commenced these proceedings seeking to recover monies of the Company alleged to have been used by Samuel Henderson, a former director of the Company, to pay down loans of PP Hotel Investments 1 Pty Ltd (PPHI). Mr Henderson was also a director of PPHI, and there was no formal loan agreement in place.

A significant portion of the payments made by the Company for PPHI occurred after the date on which Mr Henderson ceased to be a director. As such, it was a question as to whether Mr Henderson was a de facto director in respect of the directors duties issues. Mr Smith and the Company alleged that Mr Henderson had breached ss. 180 to 183 of the Corporations Act 2001 No. 50 (Cth) (the Act), as well as his fiduciary duty owed to the Company as a director.

The Court held that it did not matter that there was no formal loan agreement in place; it was clear from the parties conduct that the monies were not a gift and were to be repaid (albeit without interest, and without a fixed time frame). As such, it held that the monies were repayable by PPHI.

The Court also held that Mr Henderson had been in breach of his duties as a director under the Act and in equity in directing such payments in the period where he was a director. However, the Court was not persuaded that post-resignation, Mr Henderson was sufficiently acting in the role as a director so as to make him a de facto director.

The decision provides a timely reminder that the threshold for establishing someone as a de facto director is quite high. Merely being involved in decisions of the company is not alone sufficient; the evidence must establish that the person, by the nature and extent of their functions, is for all purposes other than in the formal sense a director.

(b) Facts

Mr Henderson was the sole shareholder and director of PPHI which, in April 2009, purchased the business assets of the Central Hotel in Bundaberg, Queensland. The purchase was funded primarily through third-party finance, which was secured by personal guarantees from Mr Henderson and three others.

The Hotel Sale Agreement was varied in June 2009 to provide for vendor finance, which was also guaranteed by Mr Henderson and others. The purchase was completed in October 2009, at which time Mr Henderson and one other person entered into a guarantee and indemnity agreement with the previous owner for PPHI's obligations pursuant to a loan agreement.

Mr Henderson was also a director of the Company between 14 October 2009 and 31 December 2010 at which time he resigned from the role.

The Company managed the Central Hotel in Bundaberg for PPHI between 19 October 2009 and 12 October 2012. Mr Henderson and PPHI argued that in or about October 2009, PPHI, the Company and Mr Henderson entered into an agreement whereby PPHI agreed to license the Hotel to the Company (License). By that License, inter alia:

- the Company was, subject to its obligation to pay the License Fee, entitled to all profits from the "business" (as that term was defined), and would be responsible for all liabilities and losses incurred as a consequence of the operation of the Business;
- the Company was to pay all outgoings with respect to the Business; and
- the License fee was to be $100 per week (excluding GST).

The License Agreement was not validly executed in accordance with the Act, and there was no real evidence given about it as Mr Henderson did not appear as a witness.

Between March 2010 and November 2012, the Company's liability to the ATO increased from $50,000 to nearly $260,000.

From 13 July 2010, substantial payments were made by the Company to reduce PPHI's liability with respect to the third-party loan and vendor finance arrangement used to purchase the Central Hotel, to the total of $805,044.33. This was described to be an unsecured loan that was repayable on demand.

At trial, the evidence led suggested that the Company ceased to be the manager in or about April 2013.

By a letter dated 31 March 2015, the solicitors acting for Mr Smith and the Company demanded repayment from PPHI and Mr Henderson for the sum of $780,474.33. In a letter from its solicitors dated 8 April 2015, PPHI denied that it owed any monies.

Mr Smith and the Company alleged as follows:

- that the monies paid by the Company to reduce PPHI's liabilities were recoverable in the amount of $662,923.32 through a loan account; and
- that Mr Henderson had breached s. 180(1) of the Act and his fiduciary duty as a director in either causing or permitting the payments to be made for PPHI:
    - without ensuring that the Company received interest or some other benefit from doing so;
    - without taking appropriate or necessary steps to recover the monies from PPHI; and

- in circumstances where the Company did not have sufficient resources to meet its taxation liabilities.

Relevantly, the conduct to which the allegations relate concerned both the period during which Mr Henderson was, and was not a director of the Company.

(c) Decision

The Court dealt swiftly with the claim for monies owing by PPHI. It is settled law that a loan agreement does not necessarily have to be oral or written, and could be inferred from the conduct of the parties. Here, there was insufficient evidence to suggest that any license agreement was truly on foot, and in any event it was doubtful that payments owed in respect of the finance used by PPHI to purchase the Central Hotel constituted "liabilities and losses incurred as a consequence of the operation of the Business". As such, the Court gave judgment to Mr Smith and the Company in respect of the monies claimed.

As to the alleged breaches of director's duties, the Court held that Mr Henderson's conduct in the period prior to 31 December 2010 (when he resigned as a director) in causing the Company to pay liabilities of PPHI was in breach of his duties under s. 180 of the Act, which required that he act as a director with reasonable care and diligence. A director acting in such a manner would not have, the Court stated, permitted the payments for the benefit of PPHI to have been made in circumstances where the Company was short on funds to meet its own debts and such payments were not of benefit to the Company.

His conduct was also in breach of s. 181 of the Act, which required that he act in good faith in the Company's best interests and for a proper purpose. Mr Henderson was clearly in a position of conflict in that he owed duties to both the Company and PPHI, and was a guarantor in his personal capacity, in relation to the same transactions.

The Court did, however, state that any compensation for this breach was largely encompassed by the order for repayment of the loan account and the breach of s. 180. A similar outcome followed in respect of the claim under ss. 182 and 183 of the Act.

When the Court came to consider the claims relating to the period after 31 December 2010, it referred to the often-cited criteria from *Grimaldi v Chameleon Mining NL (No 2)* [2012] FCAFC 6 in respect of whether a person was acting as a director. Mr Smith and the Company relied heavily upon emails involving Mr Henderson to support their claims, including:

- correspondence between the third party financier and Mr Henderson in which Mr Henderson discussed sources of finance from which cash flow shortfalls would be met;
- correspondence involving Mr Henderson in which he requested details of amounts owing to the ATO, in superannuation and other liabilities;
- Mr Henderson discussed steps that needed to be taken prior to his resignation as a director, and the appropriate structuring for employees after certain dates;
- Mr Henderson proposed that the third party financier purchase the freehold, and liaised with an insurance broker for insurance for the hotel; and
- he received various breach notices for liabilities owing with respect to the Central Hotel.

The Court held that the above was "slight" evidence that he had assumed responsibility to act as a director after 31 December 2010. He was not held out to be a director by the Company, and the involvement he did have was consistent with his role as a director and shareholder of PPHI, whose financial interests were at risk.

Whilst his role and involvement certainly gave rise to a suspicion that he played a role in the management of the Company, it was not sufficient to demonstrate that he was a de facto director.

6.5 Whether to delay the winding up of a company for the purposes of negotiating a deed of company arrangement

(By Nikki Dalla Valle, Herbert Smith Freehills)

Australian Securities and Investment Commission v Diploma Group Limited (No 4) [2017] FCA 1107, Federal Court of Australia, McKerracher J, 19 September 2017.

(a) Summary

ASIC applied to wind up 21 companies in the Diploma Group (the Defendants). An application was made to adjourn the winding up application for the First Defendant, Diploma Group Limited (Diploma), so that the provisional liquidators could be appointed as administrators to facilitate creditors having the opportunity to further consider a deed of company arrangement (DOCA). This application for adjournment was bought by a number of parties related to the Defendants (Applicants).

McKerracher J ordered that the Defendants be wound up and dismissed the application to adjourn the winding up. Joint and several liquidators were appointed for all except the Fifteenth Defendant.

(b) Facts

On 12 May 2017 McKerracher J appointed provisional liquidators to each of the Defendants but stayed the operation of the order until 25 May 2017 in light of negotiations with creditors in relation to a DOCA. On 22 May 2017 the stay for the appointment of provisional liquidators was lifted and the Court concluded that:

- not only were the companies insolvent, but seriously so;
- there was strong evidence that the group as a whole was significantly insolvent; and
- there was a sound basis for lack of confidence in the running of the affairs of the group.

A report prepared by the provisional liquidators on 7 July 2017 indicated that the Defendants as a whole had millions of dollars of liabilities to third party creditors as well as through a number of intercompany loans. Diploma itself had an estimated deficiency of assets to liabilities totalling about $20.2 million dollars. The report also found that Diploma and its directors had contravened the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) in a number of ways.

(i) ASIC application

ASIC relied on a number of factors in proving a lack of confidence in the management of the Defendants in addition to the Defendants' insolvency, including that:

- they contravened s. 201(A) of the Corporations Act by failing to have the requisite number of directors;
- their directors and officers may have contravened s. 588FB (Uncommercial Transactions), s. 588FDA (Unreasonable Director Related Transactions), s. 588FD (Unfair Loans) and s. 588G (Insolvent Trading) of the Corporations Act;
- the provisional liquidators were unable to find financial records for two of the Defendants and therefore could not comment on their financial position; and

- their books and records contained unusual accounting entries.

Nicola di Latte, a director of Diploma, was unable to provide explanations for many of ASIC's concerns in relation to Diploma's accounting as he claimed he was not an accountant and was not involved in the day-to-day transactions. ASIC argued that Mr Latte's "deflection of responsibility" further concerned ASIC that the current officers of the Diploma Group could not be trusted to manage Diploma's affairs in accordance with the Corporations Act.

(ii) Application for adjournment of winding up

ASIC did not support the first or second proposed DOCA and considered the benefit to creditors to be minimal or elusive. The second DOCA was a proposal for Diploma only and had as its central consideration the right of unsecured creditors of Diploma offering shares in Diploma and no provision was made for creditors of the other Defendants. ASIC raised concerns in relation to the second DOCA proposals, including among other reasons, because it was unclear exactly what activities Diploma would engage in given that the entities which undertook construction were in liquidation and that only independent non-executive directors should be appointed.

The Applicants submitted in response that the board of directors of Diploma would comprise at least three independent non-executive directors and that Swiss Re, a creditor of Diploma, has agreed to support the second DOCA proposal.

The provisional liquidators stated by way of affidavit that they believed there was potential for a better outcome for creditors under the second proposed DOCA but that the estimated returns under the DOCA are conditional upon a number of events occurring and that they are unable to determine with certainty whether those conditions will be satisfied or whether a better outcome for creditors will be achieved.

(The provisional liquidators filed an application to be appointed as administrators in order to put the DOCA to the creditors and the Court decided on 6 October 2017 to grant leave to the provisional liquidators to act as administrators)

(c) Decision

McKerracher J ordered the winding up of the company to proceed and dismissed the application to adjourn ASIC's application on the basis that there was insufficient material to support the adjournment.

(i) The legal principle

Pursuant to s. 461(1)(k) of the Corporations Act the Court may order the winding up of a company if the Court is of the opinion that it is just and equitable that the company be wound up. This may occur where there is a justifiable lack of confidence in the conduct and management of the company's affairs and thus a risk to the public interest that warrants protection (*Australian Securities and Investments Commissions v Bilkurra Investments Pty Ltd* [2016] FCA 371 (at [55])).

(ii) Reasons

In light of the Defendant's clear insolvency and the concerns raised about the manner in which Diploma's business has been conducted in the past there was no good reason to depart from the decision to wind up the company. In relation to the fact that the provisional liquidators were unable to comment on the true and fair financial position for the Eighth and Ninth Defendants, the Court noted that this spoke volumes about the lack of care and management of the affairs of the companies, particularly relating to the books, records and documents of the companies.

In considering the application to adjourn, his Honour found that there was a shortage of rigorous support for the recently proposed DOCA and the fact that there is some possibility that creditors may be better off is not sufficient in the present circumstances to displace the prima facie position that the winding up should be ordered. In particular, the proposed DOCA did not provide a clearly quantifiable additional financial benefit to creditors of Diploma and provided no financial benefit to creditors of the Second to Twenty-First Defendants.

McKerracher J also noted that the possibility that a DOCA could produce a better outcome for creditors of Diploma would not be shut out by proceeding with winding up the companies. In relation to the provisional liquidators seeking appointment as administrators, it was noted that although it would be unusual for ASIC to seek the appointment of the provisional liquidators as liquidators, if a convincing case could be made, then such relief is capable of being granted.

6.6 Determining the interlinked issues once and for all - an accepted basis for leave to cross claim against a plaintiff in liquidation

(By Thomas Scott, Corrs Chambers Westgarth)

Active Adult Management Pty Ltd v Milstern Retirement Living Pty Ltd [2017] NSWSC 1238, Supreme Court of New South Wales, Ward CJ in Eq, 15 September 2017.

(a) Summary

In these interlocutory proceedings, the Supreme Court of New South Wales granted an application by the defendants in the principal proceedings (Milstern Retirement Living Pty Ltd and Milstern Health Care Pty Ltd) for leave to join an additional defendant (Milstern Retirement Services Pty Limited (MRS)) (together, Defendants) to the proceedings and leave to commence a cross claim against Active Adult Management Pty Ltd (in liquidation) (First Plaintiff)) in circumstances where such a cross claim might otherwise be prohibited by s. 500(2) of the Corporations Act 2001 No. 50 (Cth) (Act). The Court did limit the scope of the cross claim and made leave conditional on the Defendants withdrawing their proofs of debt in the administration of the First Plaintiff and the defendants being prohibited from enforcing any judgment against the First Plaintiff without further leave of the Court.

(b) Facts

The dispute in the principal proceedings, to which these interlocutory proceedings related, concerned the First Plaintiff's registered leasehold interests in 15 units located across three retirement villages in Sydney. The two other plaintiffs, LSW Debt Pty Ltd and Michael Kelso (Mortgagee Plaintiffs), respectively held the first and second registered mortgages over the assets of the First Plaintiff and were funding the costs of the proceedings. The Defendants were the registered proprietors and lessors of the 15 units.

In December 2009, the First Plaintiff, MRS and another party not involved in the proceedings, entered into an Operator Agreement, subject to the Retirement Villages Act 1999 No. 81 (NSW). Under the Operator Agreement, the First Plaintiff was to collect all gross revenue on behalf of MRS, discharge all operating expenses and pay any balance to MRS. Aside from receiving a management fee, the First Plaintiff was entitled to arrange the refurbishment of the units, to carry out other capital works, and to "buy-back" any of the units if it wished to do so (i.e. acquire the leasehold interest in the units). Additionally, MRS was required to grant the First Plaintiff a "limited power of attorney" to enter into

"Village Contracts" on behalf of MRS and sign all necessary documents to effect the sale on behalf of MRS of specified units.

Between December 2009 and February 2012, the First Plaintiff acquired the leasehold over 28 units in the retirement villages (including the 15 units the subject of proceedings) for the purpose of renovating and on-selling the leasehold interests for profit. The Defendants alleged that during this time the First Plaintiff exercised the power of attorney to execute documents varying the leases in respect of the units "bought back" by it, with the effect that while it was the operator of the relevant village, it was excused from liability for lessee's contributions to outgoings in respect of that unit. The First Plaintiff managed to sell 13 of the 28 units.

On 23 December 2011, MRS gave notice of its intention to terminate the Operator Agreement. On 3 January 2012, MRS served a statutory demand on the First Plaintiff in respect of claimed debts totalling $1,710,408.84 described as relating to unpaid fees owing under the Operator Agreement. On the same day, MRS revoked the power of attorney which had been granted to the First Plaintiff. In March 2012, the First Plaintiff commenced proceedings alleging that the Defendants were frustrating its attempts to sell the remaining 15 units by refusing to grant access to the retirement villages and refusing to make available the disclosure material required under the Retirement Villages Act. However, these proceedings were ultimately dismissed after the First Plaintiff went into liquidation in February 2013. MRS lodged proofs of debt in the administration of the First Plaintiff for management fees and outstanding outgoings.

Between the First Plaintiff going into liquidation and mid-2016, the 15 units remained vacant. The Plaintiffs claimed they made various attempts to sell their leasehold interests but that their efforts were frustrated by the Defendants. The Defendants argued that the leases had been abandoned and/or terminated. The Plaintiffs commenced proceedings in May 2017, after they learnt the Defendants had purported to re-let 3 of the 15 units.

(i) The Defendants' application for leave to cross claim

According to s. 500(2) of the Act, after the passing of a resolution for voluntary winding up of a company, no action or other civil proceeding is to be proceeded with or commenced against that company except by leave of the Court and subject to such terms as the Court imposes. The Defendants sought leave to bring a cross claim against the First Plaintiff including:

- claims based on breaches of the Operator Agreement;
- claims based on the alleged misuse of the power of attorney; and
- claims for loss or damage referable to the pleaded breaches of the Operator Agreement, alleged unauthorised actions under the power of attorney and pleaded breach of fiduciary obligation.

(ii) The Plaintiffs' position on the Defendants' Application

The Plaintiffs consented to MRS being joined as a defendant. The Plaintiffs did not oppose leave being granted for the Defendants to bring a cross claim in respect of the outgoings and retention fee for the 15 remaining units, as these would be "in play" in the proceedings (to use the terminology of *Brereton J in Re Equitrust Pty Ltd* [2012] NSWSC 1049 at [12]). However, they opposed leave insofar as it sought to expand the factual area of enquiry to include the conduct of the First Plaintiff during the period that it was the operator of the villages and to include claims concerning the 13 "sold" units (for outgoings and retention fees the subject of the proofs of debt that were lodged in November 2012). The Plaintiffs' submitted that were leave granted, then the proceedings will not be able to be ready for hearing commencing on 12 February 2018.

(c) Decision

Ward CJ in Eq granted leave under s. 500(2) for the bringing of a cross claim against the First Plaintiff, provided the Defendants withdrew their proofs of debt in the administration of the First Plaintiff and ordered that the Defendants be prohibited from enforcing any judgment against the First Plaintiff without further leave of the Court.

(i) Was leave necessary?

A preliminary issue arose as to whether leave under s. 500(2) was necessary at all, based on authorities that parties may take "defensive proceedings" without leave (see for example, *Skinner v Jeogla Pty Ltd* [2001] NSWCA 15). Her Honour observed that the proposed cross claim, although clearly responsive to the claim brought by the Plaintiffs and in that sense reflexive or defensive in nature, also sought to prosecute causes of action in its own right. The better view was that leave was required.

(ii) Arguable claim

Her Honour held there to be at least an arguable claim that the sums claimed by the First Plaintiff by way of damages for breach of the leases could be the subject of an equitable set-off in respect of damages for which the First Plaintiff may be held liable to the Defendants.

(iii) Prejudice to the winding up of the company and unsecured creditors

Her Honour accepted that the proofs of debts had been lodged in the administration of the First Plaintiff but held that since there is at least an arguable claim that any such amounts cross claimed could be the subject of an equitable set-off and since there is nothing to suggest that the conduct of such a claim against the company will prejudice the winding up of the company, this was not a determinative factor against the grant of leave.

(iv) Concerns as to increased length of the hearing

Her Honour was not concerned as to the increased length of the hearing as the First Plaintiff was indemnified as to costs from the Mortgagee Plaintiffs and there is no suggestion that delay in completion of the winding up would prejudice unsecured creditors.

(v) Concerns as to hearing date likely being vacated

Her Honour did express concern that the hearing date may not be able to be maintained and the likely prejudice to other litigants because of listing issues caused by the vacation and re-listing of hearing dates that have already been fixed as warranting an expedited hearing. Nonetheless, the Court accepted that, on account of the significant overlap in the issues potentially to be raised in the principal proceedings and any potential appeal to the Court in relation to any determination by the liquidator, there was good reason to depart from the proof of debt procedure and to determine the interlinked issues once and for all.

(vi) The scope of the cross claim

Despite granting leave to the cross claim, her Honour did restrict its scope:

- so as to exclude the broad fiduciary duty claims; and
- to hold the Defendants to their position that the alleged breach of fiduciary duty involving the exercise of the power of attorney is limited to what follows from the proper construction of the power of attorney.

6.7 Navigating the legislative criteria for a statutory derivative action under s. 236 of the Corporations Act

(By Manisha Pannu, MinterEllison)

Aaron J Homes Pty Ltd v Damjanovic [2017] VSC 541, Supreme Court of Victoria, Riordan J, 13 September 2017.

(a) Summary

This case concerned an application by a former director and shareholder of Aaron J Homes Pty Ltd (AJH), for a statutory derivative action under s. 236 of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) to issue proceedings against the current director of the company. It considers the statutory criteria that need to be satisfied in order for leave to be granted to enable the derivative action to be brought. The Court in this case ultimately granted leave subject to a number of conditions aimed at imposing the responsibility of all costs of the proposed proceedings on the applicants.

(b) Facts

AJH was a residential home builder incorporated on 8 September 2005. The initial directors and shareholders were Mr Damjanovic and Mr Short. On 25 October 2012, Mr Damjanovic resigned as a director of AJH and Mrs Damjanovic was appointed in his place.

From May 2013 onwards, the relationship between the Mr and Mrs Shorts (the Shorts) and Mr and Mrs Damjanovic (the Damjanovics) started to deteriorate, resulting in a number of applications being made in court, which are not directly relevant to these proceedings. On 9 November 2016, the Damjanovics executed personal insolvency agreements under Part X of the Bankruptcy Act 1966 No. 33 (Cth).

Pursuant to a business sale agreement dated 23 March 2017, AJH sold its business to Elara Homes Pty Ltd (EH) for the sum of the "assumed liabilities" (as that term was defined in the sale agreement) plus one dollar. Mr Short was the sole director and shareholder of EH. The agreement was executed by Mr Short in his capacity as the sole director and company secretary of both AJH and EH.

The Damjanovics sought an order pursuant to s. 237 of the Corporations Act for leave to issue proceedings against Mr Short and EH.

(c) Decision

Section 237(2) of the Corporations Act provides that the Court must grant leave to allow an eligible person under s. 236(1)(a) of the Corporations Act to bring proceedings "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

- o it is appropriate to grant leave even though the subparagraph (i) is not satisfied".

Riordan J noted that the power to grant leave under s. 236 is not discretionary and can only be exercised if the five criteria set out in s. 237(2) are satisfied. It was common ground that the Court should be satisfied of the matters set out in subsections 237(2)(a) and (e). Accordingly, Riordan J had to consider the matters set out in subsections 237(2)(b), (c) and (d) only.

(i) Is there a serious question to be tried?

The Damjanovics had a number of claims with varying degrees of substance and prospects of success. Riordan J noted that it is not appropriate for the Court "to enter into the merits of the proposed derivative action to any great degree". However, his Honour found there to be a strong case that Mr Short's conduct in authorising the sale of AJH's assets to a related company, EH, involved a breach of his director's duties in equity and under s. 182 of the Corporations Act. At the time of the sale, Mr Short was a director of both AJH and EH and was therefore in a position where his duty as a director of AJH was in conflict with his duty as a director of EH and his personal interest as a shareholder of EH. It was concluded that there was a real question to be tried about whether AJH had suffered damage as a result of his conduct.

(ii) Are the Damjanovics acting in good faith?

Riordan J highlighted a few facts which supported the conclusion that the Damjanovics were acting in good faith. In particular, the Damjanovics were prepared to provide a bond of $50,000 as security for the potential costs liability of AJH, pay all costs of the proposed proceeding and indemnity AJH for such costs. The Court further imposed a condition that the Damjanovics do not pledge the credit of AJH. Riordan J also noted the Court would supervise the proposed proceeding so that insubstantial claims would not be brought by the Damjanovics to vex the proposed defendants.

(iii) Is it in the best interests of AJH that leave be granted?

Riordan J cited the decision in *Blakeney v Blakeney* (2016) 113 ACSR 398 in which Buss and Murphy JJA and Beech J commented that the pursuit of an action by or on behalf of a company against its officers for breach of their duty would ordinarily be in the best interest of the company, provided that there are reasonable prospects of success, suitable costs arrangements are made and the judgment can be successfully executed.

The Court ultimately granted leave to the Damjanovics to bring proceedings against the proposed defendants on the conditions that the Damjanovics undertake to the Court to pay the costs of bringing the proposed proceeding, indemnify AJH against any liability for these costs, not pledge the credit of AJH against these costs and provide security for the indemnity by way of bank guarantee in the amount of $50,000.

6.8 Federal Court clarifies when a bailment will result in a deemed PPS lease

(By Annabelle Horwood, King & Wood Mallesons)

Bredenkamp v Gas Sensing Technology Corporation, in the matter of Welldog Pty Ltd (in liq) (receivers and managers appointed) [2017] FCA 1065, Federal Court of Australia, Barker J, 7 September 2017.

(a) Summary

This decision addressed two proceedings which both concerned whether Gas Sensing Technology Corporation (GSTC) or the receivers of Welldog Pty Ltd (in liquidation) (the Company) were entitled to possession of four categories of equipment which had been left in the care of the Company by GSTC.

Barker J made a declaration that GSTC was entitled to possession of each of the categories of equipment. In coming to this decision, the central question before the Court was whether the equipment was the subject of bailment that satisfied the requirements for a PPS lease under s. 13 of the PPSA as it applied on 20 March 2017. Section 13(1) was later amended by the [Personal Property Securities Amendment (PPS Leases) Act 2017 (Cth)] (the PPSA) as of 20 May 2017.

As the Court did not find a deemed security interest, the interest GSTC had in the equipment was not required to be perfected by registration on the Personal Property Securities Register (PPSR). The effect of this was that there was no vesting of the equipment in the Company upon insolvency and GSTC was entitled to possession of the relevant equipment.

(b) Facts

The Company was a wholly owned subsidiary of GSTC. The equipment in question comprised four categories of equipment owned by GSTC that was stored, or in respect of certain IT equipment, used at the Company's Toowomba base.

In 2016, to secure payment of secured monies, the Company entered into a General Security Agreement with ProX Pty Ltd (ProX) whereby the Company granted a security interest over all its PPSA personal property and a fixed charge over all other property. The GSA was registered on the PPSR on 6 August 2016.

In March 2017, administrators were appointed to the Company. This gave rise to an insolvency event under the GSA, rendering it enforceable. ProX subsequently appointed receivers over the assets of the Company.

It was uncontroversial that the equipment in question was personal property pursuant to s. 10 of the PPSA. The critical issue between the parties was whether the equipment was the subject of a bailment that satisfied the features of a PPS lease under s. 13 of the PPSA. If the equipment was deemed to be the subject of a PPS lease that had not been perfected by GSTC by registering it on the PSSR, by virtue of the deeming provisions in s. 267 of the PPSA, upon the appointment of the administrators to the Company, the equipment would vest in the Company on insolvency.

(c) Decision

Prior to its amendment as of 20 May 2017, s. 13(1) of the PPSA provided, among other things, that a PPS lease means a lease or bailment of goods that is for a term of more than one year or for an indefinite term (even if the lease or bailment is determinable by any party within one year of entering into the lease or bailment). Section 13(2) lists the circumstances where a PPS lease will be found not to exist. Relevantly for the facts of this case, s. 13(2)(b) provides that a PPS lease does not include a bailment by a bailor that is not regularly engaged in the business of leasing or bailing goods. Section 13(3) also provides that s. 13 only applies to bailment for which the bailee has provided value.

(i) Was there a "bailment"?

Section 13(1) states that a PPS lease means a "lease or bailment". Therefore, the first issue the Court had to consider was whether there was a "bailment" for the purposes of the PPSA. The term "bailment" is not defined under the PPSA. GSTC's primary argument was there was no bailment of the equipment. The critical difference between the parties' arguments was whether, as GSTC argued, exclusive possession by the Company was required for there to be a bailment for the purposes of the PPSA (which GSTC contended the Company did not have).

Barker J held that it was not necessary for the receivers to establish that GSTC did not have exclusive possession of the relevant equipment to prove, at the material times in the case, there was a bailment of the equipment under the general law. Barker J accepted the receivers' reliance on the legal meaning of the term "bailment" established in *Hobbs v Petersham Transport Co Pty Ltd* (1971) 124 CLR 220 at 238 (Hobbs), namely that "[a] bailment comes into existence upon a delivery of goods of one person, the bailor, into the possession of another person, the bailee, upon a promise, express or implied, that they will be re-delivered to the bailor or dealt with in a stipulated way."

In applying the criteria in Hobbs to the facts of the case, Barker J agreed with the receivers that a bailment existed because:

- the Company had possession of each of the four categories of equipment and it was entitled to use the equipment;
- the Company's staff took delivery of the equipment;
- the Company's staff used some of the equipment; and
- GSTC could demand the return of the equipment at any time it liked or the Company could otherwise deal with the equipment as required by GSTC.

(ii) Was the bailment for an indefinite term?

Having found that there was a bailment of the relevant equipment, the next question for the Court to consider was whether s. 13(1)(b) was satisfied. This provision at the material time provided that a PPS lease will be deemed to exist if the bailment of goods is "for an indefinite term (even if the lease or bailment is determinable by any party within a year of entering into the lease or bailment)". GSTC's argued that if there was an alleged bailment, none of them had terms that were indefinite. The Court found that the bailments were in each case bailments described at general law as being "gratuitous" bailments as they could be terminated on demand, and so for an indefinite term. The Court therefore agreed with the receivers' argument that on the circumstances of the case, if there is no definite term of the bailment, it must be considered to be one of an indefinite term. This was particularly so as the facts of the case made it such that there was a degree of speculation and uncertainty as to when each bailment would end.

(iii) Was GSTC regularly engaged in the business of bailing personal property and was the bailment provided for value?

Having found a bailment that satisfied the requirements of s. 13(1) of the PPSA (as it applied at the time), the next question the Court had to consider was whether an exception was available to GTSC, namely there was no PPS lease because:

- the bailor did not regularly engage in the business of bailing goods (s. 13(2)(b)); or
- the bailment was not provided for value (s. 13(3)).

GSTC argued that it was not regularly engaged in the business of bailing goods and as such, fell into the exception in s. 13(2)(b). GSTC referred by analogy to *Re Arcabi Pty Ltd (Receivers and Managers Appointed) (in liq)* [2014] WASX 310 where it was found that the investors in that case, although having a bailment arrangement, were not in the business of profiting from the bailment itself. GSTC argued that in its own circumstances, it did not profit from bailing property to the Company's clients, instead GSTC's profits came from supplying services to clients using its skilled personnel and its equipment. Barker J agreed with this argument. The Court was not convinced that the evidence supported the conclusion that GSTC was regularly engaged in the business of bailing goods to the Company. Even if GSTC did derive some income from the Company, it was not shown that there was some "business model" where GSTC made money by placing the equipment with the Company.

Assuming that the Court was wrong in its finding that GSTC was not regularly engaged in the business of bailing goods, the Court went on to consider whether the GSTC could rely on the application of s. 13(3), which provides that the PPS lease provisions only apply "to a bailment provided for value".

The term "value" is defined in s. 10 of the PPSA. The receivers argued that the relevant part of the definition of value was set out in s. 10(a) which provides, that value means "consideration that is sufficient to support a contract". The receivers purported to argue that consideration should be given its legal meaning and that the value had been given on the basis that "consideration" was provided by the Company to GSTC in the form of secure storage, GSTC charged a management fee for the assistance provided by GSTC and the Company issued invoices for completion of some works using the equipment.

The receivers also contended that the fact that no specific fee was paid by GSTC to the Company for the bailment was not the point. The relevant issue was whether, looking at the relationship in entirety, value was given by the Company. The Court rejected this argument and instead accepted the proposition put forward by GSTC that the relevant value must be more specific than global financial or business arrangement. The Court came to this view after finding difficulty in concluding that the financial benefits identified in the application would be sufficient to support a contract. The consideration was too uncertain. It was also too indirectly related to the provision of the goods to support the conclusion that the goods were bailed for such benefits.

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.