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Bulletin No. 265

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1. Recent Corporate Law and Corporate Governance Developments

1.1 Study reveals boardroom gap on innovation

18 September 2019 - Directors are often too focused on short-term results and traditional risks, rather than the potential disruption facing their organisations, according to a study released by the Australian Institute of Company Directors (AICD), in partnership with the University of Sydney Business School.

The study, *Driving Innovation: The Boardroom Gap*, found that while Australian directors recognised the strategic importance of innovation, more needed to be done to prioritise its delivery.

Of those surveyed, 75% indicated their organisation had an innovation vision or that innovation featured prominently within their strategic plan. However, for almost half of respondents, momentum was lost over time with little oversight of how that plan was being realised.

The results show that 57% of directors were not aware what percentage of their organisation's total expenditure was allocated to Research and Development and innovation activities.

The study also revealed that Australian boardrooms have low innovation and digital literacy levels, emphasising the importance of up-skilling directors and refreshing board composition.

Notably, only 3% of directors said they hold science and technology expertise, only 3% indicated they had international experience, and 10% said they bring innovation-related expertise to the boardroom.

The study found that:

Australian directors recognise the importance of innovation, but more needs to be done to prioritise its delivery:

- Australian boards play a key role in fostering, driving, and monitoring innovation - but there remains a significant gap between strategy formulation and strategy implementation;
- comparatively, directors' responses indicated Australian boards are not prioritising innovation or disruption risks to the extent seen in overseas boardrooms, suggesting Australian boards under-estimate looming strategic risks; and
- directors identified key barriers to innovation as: human talent shortages; limited financial resources; and a focus on short-term financial performance. Directors see Australia's regulatory environment as contributing to a risk-averse corporate culture.

Australian boardrooms have low innovation and digital literacy levels:

- Australian boards lack critical technical and innovation skills, and need to increase access specialist advice. More must be done to broaden the director talent pool to include individuals with science and technology backgrounds, as well as bringing in stronger international experience; and
- while boards can take steps to address these specialist skills gaps by, for example establishing a specialist committee or advisory panel, it remains each director's responsibility to understand how technology will impact their organisation.

Board-Executive collaboration leads to better performance:

- boards that collaborate with their executive team to set and oversee an organisations innovation strategy are much more likely to realise their innovation objectives. This includes ensuring innovation features regularly on board agendas.

Recommendations for boards

The report outlined five key recommendations to ensure innovation is prioritised by boards:

- lift directors' technology and digital literacy;
- set clear expectations of management regarding calculated risk-taking to drive innovation;
- develop a shared language with management, and clear narrative for investors/members on innovation;
- ensure innovation features regularly on boardroom agendas; and
- establish a budget and executive incentives for long-term innovation.

The study comprised an AICD member survey, interviews with directors and chairs, and a global literature review.

1.2 ACSI study of CEO remuneration

17 September 2019 -The Australian Council of Superannuation Investors (ACSI) has published its latest study of chief executive officer (CEO) remuneration in the Australian Stock Exchange (ASX) 200 companies.

Key findings from the research include:

- only one eligible ASX100 CEO did not receive a FY18 bonus - a record low. In FY17, six ASX100 CEOs did not receive a bonus;

- the median ASX100 CEO received 70% of their maximum bonus entitlement - a figure almost unchanged in four years. Only 7% of ASX100 CEOs received less than 30% of maximum;
- the median bonus awarded to an ASX100 CEO in FY18 was $1.61 million - the second highest in the history of the survey;
- ten CEOs realised more than $10 million in FY18 - three of them in the ASX101-200;
- the median realised pay for an ASX100 CEO rose to $4.5 million (realised pay includes the market value of equity at the time of vesting);
- for ASX101-200 CEOs, the median realised pay was down marginally on FY17's record, falling 1.1% to $1.73 million; and
- exiting CEOs cost shareholders $25.15 million in FY18, down from $33.63 million in FY17 - largely due to a decline in the number of termination payments from 20 to 15.

View full report *CEO Pay in ASX200 Companies*.

1.3 CEDA national poll: Australians expect more from business than just profits

16 September 2019 - The Committee for Economic Development of Australia's (CEDA) nationwide poll has shown that Australians expect a broad contribution from business, focused not just on the bottom line, but on social and environmental performance as well.

The poll surveyed the general public and senior business leaders to examine community expectations of business and their views on the most important priorities for business. The results include community views on ethical business behaviour, business leaders speaking on social and environmental issues and intergenerational differences regarding business priorities.

CEDA stated that the report, based on a poll of more than 3000 people, found strong areas of alignment but also areas of disconnect. The performance of big business was seen to be good across many areas and the community and business leaders were aligned in a number of areas. Three key areas stood out:

- for eight of the top ten priorities for business, the community and business leaders were aligned;
- 72% of the general public and 88% of business leaders agree with the proposition that large companies should place equal importance on economic, environmental and social performance; and
- at least 78% of the general public and 96% of business leaders support corporate leaders speaking out on issues of national importance.

View full report *2019 Company pulse*.

1.4 Government consultation on new ASIC enforcement and supervision powers

11 September 2019 - The federal government has announced consultation on exposure draft legislation which will strengthen the Australian Securities and Investments Commission's (ASIC)

enforcement and supervision powers to protect consumers, in line with the recommendations of the ASIC Enforcement Review Taskforce.

The draft legislation:

- strengthens ASIC's licensing powers by increasing the standards required of an Australian Financial Services (AFS) licence holder, at both the time of application and on an ongoing basis;
- aligns the penalties for false and misleading statements in AFS licence and Australian credit licence applications;
- extends ASIC's powers so that ASIC may ban a person from performing functions in a financial services or credit business. The draft legislation also expands the grounds on which ASIC can issue banning orders;
- harmonises ASIC's search warrant powers across different Acts and brings them into line with the search warrant powers in the Crimes Act 1914 No. 12 (Cth); and
- allows interception agencies to provide lawfully intercepted information to ASIC for serious offences that ASIC can investigate or prosecute.

The exposure draft legislation is available on the Treasury website.

1.5 IMF discussion note on a capital market union for Europe

10 September 2019 - The International Monetary Fund (IMF) has published a staff discussion note, *A Captial Market Union for Europe* (the note), that considers the merits of a capital market union for Europe, identifies major obstacles in its path, and recommends a set of policy actions.

European capital markets are relatively small, resulting in strong bank-dependence, and are split sharply along national lines. Results include an uneven playing field in terms of corporate funding costs, the rationing out of collateral-constrained firms, and limited shock absorption. The benefits of integration centre on expanding financial choice, ultimately to support capital formation and resilience.

The note identifies three key barriers to greater capital market integration in Europe: transparency, regulatory quality, and insolvency practices. Based on these findings, the note urges three policy priorities, focused on the three barriers.

1.6 New Zealand Capital Markets 2029 report

9 September 2019 - The New Zealand Exchange and New Zealand's (NZ) Financial Markets Authority have welcomed the release of *Growing New Zealand's Capital Markets 2029* (the report).

The report highlights the vital role capital markets play in supporting the growth and productivity of NZ, and reinforces the importance of capital formation within NZ.

The recommendations in the report include:

- simplifying disclosure requirements for regulated offers;
- removing requirement to provide prospective financial information for first regulated offers;
- undertaking a review of continuous disclosure liability settings;
- excluding NZ listed bodies corporate from the definition of "overseas person" if no one overseas person (and any associate) holds more than 25% of the shares in the NZ listed entity;
- establishing a centralised process for compliance on anti-money laundering which market participants can rely on across Australasian capital markets;
- greater promotion and education of the alternative pathways to the listed market supported by a range of secondary recommendations; and
- implementing an online financial capability and literacy course for young people, including clear accountability for its implementation.

1.7 APRA updates enforcement approach

3 September 2019 - The Australian Prudential Regulation Authority (APRA) has updated its enforcement approach to outline how it will increase transparency around the use of its formal enforcement powers.

The revised document also sets out APRA's intention to take stronger action against institutions that fail to meet their legal obligations to report data to APRA in full and on time.

APRA's Enforcement Approach was published in April following a review of the it's historical approach to enforcement led by Deputy Chair John Lonsdale. It sets out APRA's willingness to use its powers more assertively to hold regulated entities and their leaders to account.

APRA's enforcement actions can range from the imposition of licence conditions and infringement notices, to disqualifications of accountable persons under the Banking Executive Accountability Regime.

The updated Enforcement Approach can be found on the APRA website.

1.8 Reforms to professional standards for financial advisers

30 August 2019 - The federal government has provided an update on reforms that aim to improve the quality of financial advice.

The government has increased the requirements for entities to investigate the full extent of financial adviser misconduct and inform and remediate customers that are affected, has introduced legislation into Parliament that ends the grandfathering of conflicted remuneration paid to financial advisers (the Treasury Laws Amendment (Ending Grandfathered Conflicted

Remuneration) Bill 2019 (Cth), and is establishing a new approach for disciplining financial advisers for misconduct through a central body.

The government has also established the Financial Adviser Standards and Ethics Authority (FASEA) - a body comprising industry, consumer ethics and education experts - to raise the education, training and ethical standards of financial advisers.

The standards require existing financial advisers to:

- complete a FASEA-approved exam;
- hold a bachelor's degree or equivalent qualifications;
- undertake continuing professional development;
- comply with a Code of Ethics; and
- be a member of an ASIC approved code monitoring scheme.

The government intends to legislate to provide additional time for existing advisers to meet new qualification and examination requirements set by FASEA. Under the new requirements, advisers who were registered on the Financial Adviser Register on 1 January 2019 must:

- complete the FASEA-approved exam by 1 January 2022 (one additional year); and
- meet FASEA's qualification requirements by 1 January 2026 (two additional years).

These changes will not apply to new advisers registered after 1 January 2019.

Further details on the professional standards for financial advisers are available on the FASEA website.

1.9 UK charity regulator concerned by quality of external scrutiny of charity accounts

28 August 2019 - A new study published by the United Kingdom (UK) Charity Commission (the Charity Commission), has found that only around half of charity accounts reviewed met the regulator's external scrutiny benchmark. This follows reviews of the quality of charity accounts which show that auditors and independent examiners are failing to identify significant failings in charity accounts.

A sample of 296 charities' accounts have been assessed against a new external scrutiny benchmark developed by the Charity Commission to determine whether a minimum standard of scrutiny by auditors and independent examiners has been met. Compliance with the benchmark does not amount to full compliance with the requirements of the Charities Statement of Recommended Practice; the benchmark is about ensuring that the basic requirements have been met, making these findings particularly concerning.

Failings included incomplete reporting of related party transactions. Of 77 cases in which these were not properly disclosed, although in all likelihood an oversight, none were reported to the Charity Commission by auditors or independent examiners. This raises additional concerns that the failure by trustees to manage conflicts of interest is also being under-reported.

The Charity Commission has updated its *Independent examination of charity accounts: guidance for trustees (CC31)* (the guidance) to make it more accessible to trustees. The guidance is aimed at helping trustees appoint an independent examiner with the right ability and practical experience to carry out a competent examination of the accounts, and allowing them to prepare appropriately.

1.10 APRA finalises revised requirements for superannuation trustees

28 August 2019 - APRA has finalised changes to its requirements for how superannuation licensees assess the outcomes they are delivering to their members.

APRA launched a consultation in April to clarify how *Prudential Standard SPS 515 Strategic Planning and Member Outcomes* (SPS 515) would interact with the government's new legislated outcomes assessment.

In its response letter, APRA has confirmed SPS 515 would require all registrable superannuation entity (RSE) licensees to perform an annual Business Performance Review to assess whether they are delivering sound, value-for-money outcomes for members. The Business Performance Review complements the requirements of the legislated outcomes assessment introduced by Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No.1) Act 2019 No. 40 (Cth).

SPS 515 will come into force from 1 January 2020.

In order to assist RSE licensees implement the new requirements, APRA has released a finalised *Prudential Practice Guide SPG 515 Strategic and Business Planning* (SPG 515), and a *Prudential Practice Guide Draft SPG 516 Business Performance Review* (draft SPG 516) for a six week consultation period. APRA expects to release the final version of SPG 516 in December.

APRA intends to start publishing additional information on superannuation performance by the end of the year. Starting with MySuper products, APRA plans to publish assessments of performance based on a range of measures and benchmarks in four key areas: investment returns, fees and charges, sustainability and (in due course) insurance.

Copies of the new SPS 515 and SPG 515, response letter and draft SPG 516 are available at on APRA's website, Consultations on strengthening superannuation member outcomes.

1.11 Draft legislation on the Financial Services Royal Commission recommendations on mortgage brokers

26 August 2019 - The federal government has released exposure draft legislation that introduces a best interests duty for mortgage brokers and reforms mortgage broker remuneration. Mortgage brokers have a strong presence in the home loan market, accounting for close to 60% of home loans.

Recommendation 1.2 of the *Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* (the Final report) recommended that mortgage brokers be required to act in the best interests of the consumer, and a breach of this duty should be subject to a civil penalty.

In response to Recommendation 1.3 of the Final Report, the government agreed to reform mortgage broker remuneration. This will be done by requiring the value of upfront commissions to be linked to the amount drawn down by borrowers instead of the loan amount; banning campaign and volume-based commissions and payments; and capping soft dollar benefits.

In addition, the government will limit the period over which commissions can be clawed back from aggregators and mortgage brokers to two years and prohibit the cost of clawbacks being passed on to consumers.

Remuneration structures for mortgage brokers, including upfront and trail commissions, will be reviewed in three years' time by the Council of Financial Regulators and the Australian Competition and Consumer Commission.

The exposure draft legislation is available on the Treasury website.

1.12 NZ survey of investor confidence

24 July 2019 - Confidence in NZ's financial markets has remained stable over the past two years, despite volatile global markets and a focus on the culture and conduct of major financial institutions in Australia and NZ.

The Financial Markets Authority (FMA) has released its annual survey into the public's *Attitudes towards New Zealand's financial markets* (the survey).

A total 65% of investors said they were confident in NZ's financial markets, in line with 66% last year. The main reasons given for an increase in confidence in the last 12 months included a rising economy and better understanding of financial markets.

The survey found that more investors are receiving information about their investments, with 58% of these investors finding the information helpful. The proportion of investors finding the materials they receive helpful has been steadily increasing since 2013.

A total 86% of New Zealanders aged 18 years or over have some form of investment. The most common forms of investments are KiwiSaver (66%), term deposits (34%), shares (17%), managed funds (14%) and residential property (14%).

For one-third of New Zealanders (32%), KiwiSaver is their only investment and their confidence level lags investors in other products. Just 64% of KiwiSaver investors said they were confident in financial markets, compared with 85% of investors in managed funds or investors who had bought their own shares.

FMA stated that this underlined the importance of continuing to improve the information provided to KiwiSaver members by their providers, as well as efforts to encourage KiwiSaver members to take a greater interest in their investment.

2. Recent ASIC Developments

2.1 Remake of "sunsetting" class order about changing scheme constitutions

17 September 2019 - ASIC has remade existing relief on changing scheme constitutions. The existing relief under *ASIC Class Order [CO 09/552]* was to end on 1 October 2019.

The new instrument, *ASIC Corporations (Changing Scheme Constitutions) Instrument 2019/700*, continues to provide relief in certain situations to vary how the constitution of a registered scheme may be modified, or repealed and replaced with a new constitution. ASIC also issued *ASIC Corporations (Repeal) Instrument 2019/885*, which repeals [CO 09/552].

The new instrument will continue the effect of the previous instrument with some minor amendments, which include simplifying the drafting to give greater clarity.

The relief was remade following ASIC's public consultation in *CP 320 Remaking ASIC class order on changing scheme constitutions: [CO 09/552]* (CP 320). ASIC did not receive any submissions in response to CP 320.

View:

- ASIC Corporations (Changing Scheme Constitutions) Instrument 2019/700;
- ASIC Corporations (Repeal) Instrument 2019/885; and
- CP 320.

2.2 ASIC makes product intervention order banning short term lending model to protect consumers from predatory lending

12 September 2019 - ASIC has used its product intervention power to ban a model of lending in the short-term credit industry which has been found to cause significant consumer detriment.

In its first deployment of this power, ASIC targeted a particular business model where a short-term credit provider and its associate charged fees under separate contracts.

The law allows short term credit providers to remain exempt from credit licensing, conduct and responsible lending obligations under the National Consumer Credit Protection Act 2009 No. 134 (Cth), if the fees charged for a loan of up to 62 days do not exceed 5% of the loan amount and 24% per annum interest.

Under the short-term lending model, the short-term credit provider charged costs within these limitations, however its associate charged significant upfront, ongoing and default related fees under a separate contract for management and administrative services in relation to the loan. When combined, these fees can add up to almost 1000% of the loan amount.

The model has been used by Cigno Pty Ltd and Gold-Silver Standard Finance Pty Ltd, and more recently by MYFI Australia Pty Ltd and BHF Solutions Pty Ltd.

In making the order, ASIC considered:

- submissions received in response to *CP 316 Using the product intervention power: Short term credit* (CP 316), with only two out of 35 submissions opposing ASIC's proposed product intervention order;
- data provided by industry participants, demonstrating the size and scale of the short-term credit industry; and
- ASIC complaints data in relation to the short-term lending model, which comprised over 200 reports of misconduct, with the majority being about excessive fees and charges.

The product intervention order does not seek to modify the existing exemption for short-term credit; rather, it ensures that short-term credit providers and their associates do not structure their businesses in a manner which allows them to charge fees which exceed the prescribed limits for regulated credit.

The product intervention order is an industry wide order made by legislative instrument and will apply to any person that attempts to use this short-term lending model or variations of the model. The product intervention order was registered with the Federal Register of Legislation on 12 September 2019, commenced on 14 September 2019 and remains in force for 18 months unless it is extended or made permanent. ASIC can extend the order's duration or make it permanent, but only with Ministerial approval.

There are criminal and civil penalties for breaching the product intervention order, including up to five years imprisonment and fines of up to $1.26 million per offence.

View:

- *ASIC Corporations (Product Intervention Order-Short Term Credit) Instrument 2019/917* (product intervention order);
- product intervention order Explanatory Statement;
- *Product Intervention Order Notice*; and
- CP 316 submissions.

2.3 Update on Royal Commission implementation

11 September 2019 - ASIC has provided its second update, *ASIC Royal Commission implementation update* (the update), on its actions in response to the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (the Financial Services Royal Commission).

The update outlines a number of ways ASIC is implementing the seven priorities highlighted in its *Corporate Plan 2019-23*, one of which is to prioritise the recommendations and referrals from the Financial Services Royal Commission.

ASIC has dedicated resources to investigating the referrals from the Financial Services Royal Commission and the case studies that came before the Financial Services Royal Commission. Some of these were matters that ASIC was already investigating at the time of the Financial Services Royal Commission.

As part of ASIC's strategic change program and strengthened governance arrangements, it has established an Office of Enforcement. It is leading the application of ASIC's "why not litigate?"

operational discipline to enforcement approach. As well, ASIC's more intensive supervisory programs and activities are targeting thematic and sectoral risks.

View the update.

2.4 Extension of relief for foreign financial services providers

10 September 2019 - ASIC has extended to 31 March 2020 licensing relief for foreign financial services providers (FFSPs) to allow them to provide certain financial services to Australian wholesale clients without needing to hold an Australian financial services (AFS) licence.

The licensing relief that has been extended by ASIC is:

- *ASIC Corporations (Repeal and Transitional) Instrument 2016/396* and *ASIC Corporations (CSSF-Regulated Financial Services Providers) Instrument 2016/1109*. FFSPs relying on this relief can provide specified financial services to Australian wholesale clients if their home regulatory regime has been assessed by ASIC as sufficiently equivalent to the AFS licensing regime; and
- *ASIC Corporations (Foreign Financial Services Providers-Limited Connection) Instrument 2017/182*. This instrument provides licensing relief for FFSPs that are only required to hold a licence because they have engaged in conduct that is intended to induce an Australian wholesale client to use the provider's financial services.

These instruments had been due to expire on 30 September 2019.

ASIC indicated in *CP 315 Foreign financial services providers: Further consultation* (CP 315) that it would extend the relief to 31 March 2020 pending consultation. Submissions to CP 315 closed on 9 August 2019.

The extension of the relief is contained in *ASIC Corporations (Amendment) Instrument 2019/902*.

View:

- CP 315;
- CP 301 Foreign financial services providers;
- *ASIC Corporations (Repeal and Transitional) Instrument 2016/396*;
- *ASIC Corporations (CSSF-Regulated Financial Services Providers) Instrument 2016/1109*;
- *ASIC Corporations (Foreign Financial Services Providers-Limited Connection) Instrument 2017/182*; and
- *ASIC Corporations (Amendment) Instrument 2019/902*.

2.5 Remake of "sunsetting" class order facilitating the offer of share and interest purchase plans

30 August 2019 - ASIC has remade the relief in *ASIC Class Order [CO 09/425]*, which was due to sunset on 1 October 2019.

The new instrument, *ASIC Corporations (Share and Interest Purchase Plans) Instrument 2019/547*, provides ASX-listed issuers of shares and interests under purchase plans with relief from the requirement to prepare a prospectus or Product Disclosure Statement if certain conditions are met.

The new instrument will continue the effect of the previous instrument while increasing the participation limit (for each registered holder in a 12-month period) from $15,000 to $30,000.

The relief was remade following ASIC's public consultation, as set out in *CP 304 Remaking ASIC class order on share and interest purchase plans: [CO 09/425]* (CP 304).

ASIC received three non-confidential submissions in response to CP 304 during the consultation period. ASIC's consideration of these submissions is detailed in *REP 629 Response to submissions on CP 304 Remaking ASIC class order on share and interest purchase plans: [CO 09/425]* (REP 629).

View:

- *ASIC Corporations (Share and Interest Purchase Plans) Instrument 2019/547*;
- REP 629;
- CP 304; and
- *RG 125 Share and interest purchase plans*.

2.6 Research highlights the importance of reforms for mortgage brokers and home lending

29 August 2019 - ASIC has released a report *REP 628 Looking for a mortgage: Consumer experiences and expectations in getting a home loan* (REP 628). As part of this research, ASIC followed over 300 consumers in the process of taking out a home loan and surveyed another 2,000 consumers.

This research examines consumer decision-making in relation to home loans to identify what factors influence their journey.

Key findings include:

- consumers who visit a mortgage broker expect the broker to find them the "best" home loan;
- mortgage brokers were inconsistent in the ways they presented home loan options to consumers, sometimes offering little (if any) explanation of the options considered or reasons for their recommendation; and
- first home buyers were more likely to take out their loan with a mortgage broker.

REP 628 shows that consumers taking out a loan directly through a lender were more likely to be a refinancer or have had previous experience taking out home loans. Consumers who went directly to a lender valued convenience, with 69% taking out their loan with a lender they had an existing relationship with.

Taking out a home loan is a complex process and consumers told ASIC it can be an "overwhelming" experience. Although most consumers set out to find the best loan they could, one in five consumers believed that they could have got a better interest rate on their home loan or were not sure whether they had even got a good rate.

2.7 ASIC outlines priorities for small business in 2019-2020

29 August 2019 - ASIC has released its *Corporate Plan 2019-23* (the Corporate Plan). The Corporate Plan's action items reflect that small business remains a large and important stakeholder for ASIC.

In the financial year ahead, ASIC will continue to review lenders' compliance with small business protections in light of the changes to unfair contract terms legislation as well as maintain engagement with important external stakeholders that have a key role to play in small business.

ASIC will also focus on assisting small business owners in culturally and linguistically diverse communities to increase their awareness of ASIC's role in assisting, engaging with and helping to protect small business, while also helping them access the information they need to improve their financial acumen.

Last financial year, ASIC prosecuted 382 individuals for 827 offences for failure to keep books and records which is often a classic indicator of phoenix activity. ASIC will continue conducting surveillance of potential illegal phoenix activity, which is estimated to cost businesses between $1.1 and $3.1 billion each year out of an overall cost to the economy of between $2.8 and $5.1 billion each year.

ASIC supports government initiatives to combat illegal phoenix activity such as the Phoenix Taskforce and Serious Financial Crime Taskforce, as well as supporting the proposed phoenix activity reforms contained in the Treasury Laws Amendment (Combatting Illegal Phoenixing) Bill 2019 (Cth).

Through *ASIC's Small Business Strategy 2017-2020* ASIC remains committed to assisting, engaging and helping to protect small businesses. Key highlights for 2018-2019 include:

- more than 375,000 new business names and 220,000 new companies were registered, and over 142 million searches of ASIC's registers were conducted;
- ASIC responded to over 670,000 enquiries through its various communications channels, and the small business page on ASIC's website was viewed over 54,000 times;
- there were over 14,500 downloads of the FirstBusiness App; and
- refreshing ASIC's small business online resources to make them easier to navigate.

For more information on the work ASIC is doing with and for small business, view:

- *REP 571 ASIC and small business*;
- *ASIC Small Business Strategy 2017-2020*; and
- Small business infographic *ASIC engages with small business and government*.

2.8 ASIC's Corporate Plan 2019-23

28 August 2019 - ASIC has published its *Corporate Plan 2019-23* (the Corporate Plan). The Corporate Plan sets out ASIC's change agenda and regulatory priorities, and how ASIC will act strategically to address misconduct in the financial system and improve consumer outcomes.

This year's Corporate Plan outlines ASIC's efforts towards becoming a more strategic regulator, its renewed approach for supervision and enforcement, and key regulatory activities over the next four years. It sets out how ASIC will be using the full suite of regulatory tools to target the threats and harms it sees in the financial system.

ASIC has identified seven principal strategic regulatory priorities. Together, they represent the most significant ways in which ASIC is:

- promoting better corporate cultures and behaviours, in particular the values of fairness and professionalism;
- addressing consumer harms (particularly where vulnerable individuals and communities are impacted) and improving consumer outcomes; and
- deterring, punishing and publicly denouncing wrongdoing via ASIC's "Why not litigate?" operational discipline.

ASIC will directly address the findings of the *Royal Commission into Misconduct in the Banking, Superannuation, and Financial Services Industry*, prioritising and acting on its recommendations.

The Corporate Plan explains how ASIC will bolster its capabilities so as to deliver its own change program and strategic priorities. This includes:

- expanding the use of behavioural sciences, data and technology;
- positioning ASIC as a strategic and agile regulator;
- developing and using new regulatory tools and remedies, such as the new product intervention power, the design and distribution obligations and tougher penalties; and
- scaling up ASIC to achieve these outcomes.

View the Corporate Plan.

2.9 Approval of AFCA rule change enabling the naming of firms

26 August 2019 - ASIC has approved changes to the Australian Financial Complaints Authority (AFCA) Rules to allow the scheme to name financial firms in published determinations.

In its first six months, AFCA received 35,263 complaints. About 4,500 to 5,000 complaints are currently expected to be finalised each year by way of determination. While the publication of determinations has been a longstanding feature of the external dispute resolution schemes in Australia, the names of firms involved in financial services, superannuation and credit complaints have not been published to date.

AFCA applied for approval to change their Rules to enable identification of firms following public consultation. Consumers who are party to a complaint will continue to be anonymised in all determinations.

In approving this change ASIC took into account stakeholder feedback to AFCA's public consultation and the statutory approval criteria.

ASIC's view is that naming firms in determinations can help identify conduct or market problems within firms or affecting specific products or services, as well as highlighting where firms have done the right thing. It will also enhance transparency and accountability of firms' performance in complaints handling and of AFCA's own decision-making.

To support the new Rules, AFCA will issue updated operational guidelines which set out examples of the circumstances in which a determination naming a financial firm would not be published. This includes where naming may expose confidential information about a firm's systems or policies.

Background

On 31 May 2019, AFCA conducted a public consultation on Rule changes to enable the scheme to name firms in determinations and received 25 submissions in response to that consultation.

ASIC approved this Rule change in accordance with legislative requirements in s. 1052D of the Corporations Act 2001 No. 50 (Cth) which require AFCA to seek ASIC approval of material changes to the AFCA scheme and establish the statutory approval criteria.

ASIC's consultation on updates to internal dispute resolution (IDR) policy settings and data reporting framework (*CP 311 Internal dispute resolution: Update to RG 165*) closed on 9 August 2019. ASIC's review of IDR policy and regulatory guidance is expected to be completed by the end of 2019.

2.10 Consumers see value in financial advice, but lack of trust remains an issue

26 August 2019 - ASIC consumer research reveals the barriers faced by consumers when considering financial advice.

ASIC's *REP 627 Financial advice: What consumers really think* (REP 627) presents independent research into consumer experiences of, and attitudes towards, financial advice and the advice industry. The research focused on the overall use of financial advisers, motivators and barriers to seeking personal advice and consumer attitudes towards the financial advice industry.

According to the research, while 41% of Australians intend to get personal financial advice in the future, many of them will not proceed because of these perceived barriers.

The research found that 27% of Australians had received financial advice in the past, and 12% of Australians received advice in the past 12 months. The research also highlighted that a significant majority of consumers sought financial advice because they felt advisers had expertise in financial matters and could recommend products that they, as consumers, could not normally find on their own.

The research found that consumers generally seek financial advice for investments such as shares and managed funds, retirement income planning, growing their superannuation and budgeting or cash flow management. Interestingly, it highlighted that use of digital advice (also known as robo-advice) is still very low (1%). However, 19% of research participants said they were open to getting digital advice once it was explained to them.

The quantitative research involved an online survey of 2,545 participants, which was weighted to ensure that it was representative of the Australian population.

View REP 627.

3. Recent ASX Developments

3.1 Response to consultation - Transfers to the CHESS Subregister

On 30 August 2019, ASX released its response to submissions on ASX's July 2018 *Consultation Paper Transfers to the CHESS Subregister* which proposed changes to the ASX Settlement Operating Rules and Procedures to streamline transfers to the Clearing House Electronic Subregister System (CHESS). The proposal was to remove the requirement for ASX settlement participants that are not ASX trading participants to receive and provide to the issuer, a registrable transfer document signed by or on behalf of the holder in order to effect transfer of an issuer sponsored holding to a CHESS holding.

Considering the consultation feedback, ASX has decided to limit the proposed removal of registrable transfer document requirements to a sub-class of settlement-only participants who meet certain qualifying criteria (referred to as "custodial settlement participants"). These custodial settlement participants will be further required to undertake pre-transfer validation checks.

Subject to regulatory clearance, these changes will be implemented through the ASX Settlement Operating Rules and Procedures on or around Q4 2019.

3.2 Updates to Guidance Note 9 - Disclosure of corporate governance practices

ASX has published an updated version of *ASX Listing Rules Guidance Note 9 Disclosure of Corporate Governance Practices*, which is due to be released on 1 January 2020, the same date the fourth edition of the *Corporate Governance Principles and Recommendations* comes into effect. The update includes additional guidance for entities intending to adopt early the fourth edition of the *Corporate Governance Principles and Recommendations*.

3.3 Monthly Activity Reports

On 15 August 2019, ASX released its Annual Report for Financial Year 2019.

On 5 September 2019, ASX released the ASX Monthly Activity Report for August 2019.

4. Recent Takeovers Panel Developments

4.1 Benjamin Hornigold Limited 05, 06 & 07 - Declaration of unacceptable circumstances

9 September 2019 - The Takeovers Panel (the Panel) has made a declaration of unacceptable circumstances after consideration of:

- a request dated 24 July 2019 from Benjamin Hornigold Limited (Benjamin Hornigold) to vary the final orders made by the Panel on 8 February 2019 and an application dated 8 August 2019 from Benjamin Hornigold in relation to its affairs; and
- an application dated 8 August 2019 from John Bridgeman Limited (John Bridgeman) in relation to the affairs of Benjamin Hornigold (see TP19/45).

Background

The following facts are in summary form (see Declaration for more background).

John Bridgeman is the exclusive investment manager for Benjamin Hornigold.

On 8 February 2019, the Panel in *Benjamin Hornigold Limited 02 and Henry Morgan Limited 02* [2019] ATP 1 made an order in relation to the affairs of Benjamin Hornigold (among other things) requiring John Bridgeman to repay a $4.5 million unsecured loan given by Benjamin Hornigold with any interest (Repayment Order) which the Panel considered that (in combination with other things) operated as a lock-up device.

Through a series of transactions between 28 February 2019 and 31 May 2019 pursuant to a services agreement between King's Currency Exchange Pty Ltd (King's Currency) and Benjamin Hornigold (the Services Agreement), John Bridgeman directed Benjamin Hornigold to place approximately $5.46 million in aggregate in foreign currency banknotes with King's Currency. The balance of foreign currency banknotes placed with King's Currency by Benjamin Hornigold was approximately $7.12 million as at 31 May 2019.

On 5 March 2019, John Bridgeman announced that it had determined not to proceed with an off-market takeover bid for all of the securities in Benjamin Hornigold that it had announced on 10 September 2018 (2018 Bid) and that all previous acceptances of the 2018 Bid were cancelled and the 2018 Bid would lapse.

On 6 March 2019, JB Financial Group Pty Ltd provided an unsecured loan facility to John Bridgeman for up to $7 million (JBFG Facility). On 7 March 2019 and 8 March 2019, John Bridgeman:

- drew down $4.5 million of the JBFG Facility (in two tranches) for the purposes of repaying Benjamin Hornigold in accordance with the Repayment Order; and
- made a repayment of $4.5 million to Benjamin Hornigold (in two tranches).

On 26 April 2019, John Bridgeman announced its intention to make a new off-market takeover bid for all of the securities in Benjamin Hornigold and offers opened on 17 May 2019 (2019 Bid).

On 12 June 2019, a deed of variation was executed by King's Currency and Benjamin Hornigold on 12 June 2019 (Variation Deed) which (among other things) amended the Services Agreement to extend the period for the return of banknotes placed by Benjamin Hornigold from 30 days by providing that all banknotes placed by Benjamin Hornigold were not returnable until 12 November 2019. Later on 12 June 2019, all of the directors of Benjamin Hornigold (including Mr McAuliffe) and the company secretary resigned, and three new directors were appointed.

Declaration

The Panel considered that the circumstances were unacceptable in relation to the affairs of Benjamin Hornigold because the following transactions (individually and in conjunction, both of which occurred after the Panel made the Repayment Order) effectively replaced the loan subject of the Repayment Order and diminished the value of a material and important asset of Benjamin Hornigold, making it less attractive to a potential acquirer and less likely to attract competing proposals to the 2019 Bid (and as a result, diminished the value of Benjamin Hornigold if securityholders do not accept the 2019 Bid), in effect operating as a lock-up device:

- the placement by Benjamin Hornigold of approximately $5.46 million in aggregate in foreign currency banknotes with King's Currency; and
- the extension of the period for the return of all banknotes placed by Benjamin Hornigold with King's Currency pursuant to the terms of the Variation Deed.

The Panel did not consider it against the public interest to make the declaration, and in making it had regard to the matters in s. 657A(3) of the Corporations Act 2001 No. 50 (Cth).

Orders

The Panel is considering what final orders it will make (if any), including whether it should make an order varying the orders made by the Panel on 8 February 2019, and will publish details in due course.

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

4.2 Havilah Resources Limited - Panel declines to conduct proceedings

3 September 2019 - The Panel has declined to conduct proceedings on an application dated 21 August 2019 from Havilah Resources Limited (Havilah Resources) in relation to its affairs.

Havilah Resources is seeking shareholder approval under s. 611 (item 7) of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) for the issue of Havilah Resources shares to OneSteel Manufacturing Pty Ltd at a general meeting of Havilah Resources to be held on 12 September 2019. Havilah Resources submitted that Dr Keith Robert Johnson, a co-founder and former director of Havilah Resources, is associated with other shareholders (in contravention of s. 606 of the Corporations Act and the substantial holding provisions) and has sent correspondence to Havilah Resources shareholders containing misleading or deceptive statements (see TP19/46).

The Panel considered that Havilah Resources did not provide a sufficient body of material to justify the Panel making further enquiries as to whether there were any associations that may result in a contravention of s. 606 of the Corporations Act or a material contravention of the substantial holding provisions. The Panel also considered that Havilah Resources could publish corrective disclosure to clarify any statements by Dr Johnson.

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

The Panel has published the reasons for its decision on the Takeovers Panel website.

4.3 Mineral Commodities Limited - Panel declines to conduct proceedings

28 August 2019 - The Panel has declined to conduct proceedings on an application dated 22 August 2019 by Mineral Commodities Limited (Mineral Commodities) in relation to its affairs.

The application concerned whether Au Mining Limited (Au Mining), Tormin Holdings Limited and Mr Guy Walker, together with other persons alleged to be connected with those Mineral Commodities' shareholders, were associated and acting in concert in relation to the affairs of Mineral Commodities (see TP 19/47). Au Mining has nominated three directors for appointment at a spill meeting convened under ss. 250U and 250V of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act). The spill meeting was scheduled to be held 28 August 2019, at 10:00am (Perth time).

The Panel did not consider that there was sufficient probative material to satisfy it that proceedings should be conducted. Even if it had found sufficient material to justify making further enquiries, the Panel would have had reservations as to whether an extension of time under s. 657C(3) of the Corporations Act would be warranted. In that regard, the Panel noted the unexplained delay by Mineral Commodities in bringing the application, notwithstanding that Mineral Commodities had for some considerable time been aware of the circumstances relied upon in support of its claims as to a potential association.

Accordingly, the Panel declined to conduct proceedings.

The Panel has published the reasons for its decision on the Takeovers Panel website.

5. Recent Research Papers

5.1 Corporate purpose and firm ownership

Analysing data from approximately 1.5 million employees across 1,100 established public and private United States companies, the authors find that the strength of employee beliefs about their firm's purpose is lower in public companies. This difference is most pronounced within the salaried middle and hourly ranks, rather than senior executives. Among public companies, purpose becomes progressively lower with more concentrated shareholders, especially among firms with high hedge fund ownership. These patterns can be partly explained by differences in CEO backgrounds and remuneration: public firms, particularly those with strong shareholders, choose outsider CEOs at higher rates and pay them more relative to their employees. The authors' analysis suggest that these results are not driven solely by sorting effects, but appear attributable in part to the impact that firm owners have on their employees. In summary, shareholders appear to influence the strength of corporate purpose deep within organisations via the leadership and corporate practices they enable at the top.

View *Corporate Purpose and Firm Ownership*.

5.2 Twin peaks after Hayne: Tensions and trade-offs in regulatory architecture

Australia uses a Twin Peaks financial supervisory architecture, which comprises a prudential regulator and a market conduct regulator. The logic of Twin Peaks is that regulatory functions are allocated between agencies according to the objective, rather than the target. This article argues that there are three, rather than two, distinct underlying objectives for financial sector regulation. The third is consumer protection. Regulation would be strengthened by the establishment of a specialist regulatory agency with responsibility for consumer protection in the retail market for financial products and services. The article therefore parts company with the *Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry*, which recommended that the basic Twin Peaks architecture be retained.

View *Twin Peaks after Hayne: Tensions and Trade-Offs in Regulatory Architecture*.

5.3 Governing the energy transition: The role of corporate law tools

Conventionally the private sector has been considered a barrier to effective energy transition governance. However, in the wake of the *2015 Paris Agreement*, a range of international initiatives have emerged that focus on enhancing the positive role of the private sector in energy transition governance. These developments reinforce a gradual international shift in the business community to view climate change in financial risk terms. Climate change is seen as a matter of financial risk for corporations, and for the large institutional investors who invest in them, it has the potential to engage corporate law tools, such as requirements for risk disclosure, shareholder actions and the fiduciary duties of company directors. This article explores the potential, and limitations, of such corporate law tools to drive private sector action on sustainable energy transition. The article draws on empirical research examining business perceptions and practices relating to climate risk management and promotion of clean energy sources. Although there are promising signs of a more serious consideration of climate risk in business decision-making, corporate practices around climate risk disclosure, and shareholder and board engagement with clean energy issues, remain highly variable and in flux. If corporate law tools are to make a more substantial contribution to energy transition governance, they will likely need to be complemented by a robust regulatory framework for greenhouse gas emissions reduction.

View *Governing the Energy Transition: The Role of Corporate Law Tools*.

5.4 Shareholder value(s): Index fund activism and the new millennial corporate governance

The most pressing current debate in corporate governance is whether index funds, now the largest shareholders in many large companies, have incentives to provide effective shareholder oversight. Index funds don't seek to outperform the market and so, according to critics, cannot be expected to invest in improving shareholder value by disciplining management. Others have highlighted market features that could incentivise index funds to invest in at least some value-enhancing governance activities. The consensus of the literature is that index funds can be expected to engage, at most, in undertaking low-risk, high-value interventions that don't risk upsetting managers.

This article argues that the current debate is misguided. In focusing on the conventional framework of shareholder value maximisation, critics have overlooked that index funds have been outspoken, confrontational, and effective advocates of activist campaigns oriented to social responsibility. The authors show that these funds have challenged management and voted against directors to advance these ends. Most prominently, index funds have been instrumental in bringing gender diversity to the boards of large companies. They have also been out front in demanding that firms address issues related to sustainability.

The authors argue that this social activism reflects a transformative development. Index funds are locked in a fierce contest to win the soon-to-accumulate assets of the Millennial generation, and, as they show, Millennials place a premium on social values in their investments. Index funds, which have exhausted price competition and cannot compete on performance, compete fiercely in responding to these preferences. The importance of this development should not be understated: the largest pools of assets in the economy are being deployed to advance the social goals of investors using the traditional powers of share ownership. The authors marshal evidence for this new dynamic, situate it within the existing literature, and consider the implications for the debate over index funds as shareholders and corporate law generally.

View *Shareholder Value(s): Index Fund Activism and the New Millennial Corporate Governance*.

6. Recent Corporate Law Decisions

6.1 Inherent jurisdiction of the Federal Court to grant leave to commence and prosecute proceedings on behalf of a company in liquidation

(By Katrina Sleiman, Corrs Chambers Westgarth)

Scott Russell Constructions Pty Limited (In Liq) v Queensland Building and Construction Commission [2019] FCA 1378 (26 August 2019) Federal Court of Australia, Greenwood J

(a) Summary

Mr Russell, the former sole director and shareholder of Scott Russell Constructions Pty Limited (In Liq) (SRC), sought leave, *nunc pro tunc*, to bring a proceeding on behalf of or in the name of SRC in the Federal Court (the Court) in relation to a dispute with the building regulator, the Queensland Building and Construction Commission (QBCC), without the consent of SRC's liquidator.

The Court was satisfied that the question of whether leave *nunc pro tunc* is to be granted as an expression of the Court's inherent jurisdiction is a matter which falls within the Court's jurisdiction as conferred by s. 39B(1A) of the Judiciary Act 1903 No. 6 (Cth) (the Judiciary Act) and is a question incidental to matters the subject of jurisdiction under the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) and the Competition and Consumer Act (2010) 1974 No. 51 (Cth) (the CC Act). Nevertheless, leave was refused on the basis the alleged conduct did not involve an arguable cause of action.

(b) Facts

SRC engaged in the business of residential construction and had entered into a contract with certain homeowners. Mr Russell alleged that a QBCC manager provided SRC with a list of incomplete works and defects (Scope of Works) to be undertaken in respect of the homeowners' premises and that the QBCC manager subsequently represented, "in trade or commerce", that unless the homeowners provided SRC with access to their premises, QBCC would not take the matter further. Mr Russell further alleged that QBCC and a QBCC debt recovery officer represented, "in trade or commerce", that QBCC intended to initiate debt recovery proceedings against SRC due to a failure to respond to the Scope of Works.

QBCC denied the allegations and claimed that to the extent the representations were made, they were made in the course of QBCC's role as a government agency and regulator of the building industry in Queensland, and not "in trade or commerce."

QBCC paid $200,000 to the homeowners pursuant to a scheme described as the Home Warranty Scheme established under the Queensland Building and Construction Commission Act 1991 No. 98 (Qld). A dispute arose between Mr Russell and QBCC and Mr Russell alleged that by reason of a number of threats, he believed that SRC had no alternative but to pay $130,000 to QBCC in order to resolve the matter.

Mr Russell alleged that QBCC acted in an unconscionable manner pursuant to s. 21 of the *Australian Consumer Law* (ACL) in Schedule 2 (The Australian Consumer Law) of the CC Act, engaged in "harassment and coercion," in contravention of s. 50 of the ACL, and engaged in conduct constituting "misfeasance in public office". The originating application was filed on the footing that Mr Russell would seek leave, *nunc pro tunc*, to bring the proceeding on behalf of or in the name of SRC. That order was sought as an exercise of the inherent jurisdiction of the Court. QBCC led evidence that the liquidator had not consented to the proceeding and that Mr Russell's solicitor did not act for the liquidator or SRC.

(c) Decision

While Greenwood J determined that the Court had the jurisdiction to make the order sought by Mr Russell, his Honour refused to grant leave.

(i) Does the Court have inherent jurisdiction

Relevantly, s. 471B of the Corporations Act provides that "while a company is being wound up in insolvency or by the Court ..., a person cannot begin ... a proceeding in a court 'in relation to property of the company'... except with the leave of the Court and in accordance with such terms, if any, as the Court imposes". Section 477 of the Corporations Act concerns the powers of the liquidator, including to address and compromise "all questions in any way relating to or affecting the property or the winding up of the company, on such terms as are agreed", including the power to bring/defend a legal proceeding in the name and on behalf of the company.

In *Chahwan v Euphoric Pty Ltd* (2008) 227 FLR 43 (*Chahwan*), the New South Wales Court of Appeal accepted that notwithstanding the statutory provisions, the inherent jurisdiction of the relevant Court remains, together with the statutory provisions, such that the relevant Court enjoys a jurisdiction to grant leave to a person to bring proceedings on behalf of a company under insolvent administration by a liquidator. The source of that jurisdiction is said to rest on the same principle on which a person could always have filed a bill in the old Court of Chancery against their trustee to be allowed to use their name to recover the trust property. Such procedure is said to be of "respectable antiquity". While Greenwood J noted that this notion seems inconsistent with the modern statutory foundation for the powers, duties and responsibilities of a liquidator of an insolvent company, his Honour accepted that an intermediate Court of Appeal in *Chahwan* held that this jurisdiction sits comfortably with the statutory arrangements. Moreover, it can be invoked by a creditor.

If the jurisdiction relied upon is the inherent jurisdiction, anchored in authorities of respectable antiquity, Greenwood J turned to consider how that jurisdiction arises in the Federal Court as a matter of federal jurisdiction. The Federal Court of Australia Act 1976 No. 156 (Cth) creates the Court as a superior court of record and a court of law and equity, capable of determining questions of law and equity in matters in respect of which it is invested with jurisdiction. Importantly, s. 39B(1A) of the Judiciary Act provides that the original jurisdiction of the Court includes, relevantly, jurisdiction "in any matter arising under laws made by the Parliament".

The Court is expressly invested with jurisdiction "with respect to civil matters arising under the Corporations legislation", s. 1337B of the Corporations Act. Relevantly, SRC is the subject of a winding up order under the Corporations Act and in a state of insolvent administration by a liquidator appointed under the Corporations Act. Accordingly, his Honour held that the question of an order made in the exercise of an inherent jurisdiction, concerns "a matter arising" under the Corporations Act as to the powers of the liquidator under the Corporations Act and the relationship between those powers and the extent to which they relate to and/or subsist coherently with a power to grant leave as an exercise of an inherent jurisdiction. The Court, seized of that matter, is seized of a matter arising under a Commonwealth Act which confers jurisdiction to determine that question.

Further, Mr Russell sought to maintain a proceeding on behalf of SRC in which a remedy was sought under the ACL which is a schedule to, and given force by, Part XI of the CC Act. The CC Act invests the Court with jurisdiction "in any matter arising under this Act in respect of which a civil proceeding has, whether before or after the commencement of this section, been instituted under this Part": s. 86(1).

Accordingly, his Honour was satisfied that the question of whether leave *nunc pro tunc* is to be granted as an expression of the Court's inherent jurisdiction is a matter which falls within the Court's jurisdiction as conferred by s. 39B(1A) of the Judiciary Act and is a question incidental to matters the subject of jurisdiction under the Corporations Act and the CC Act.

(ii) Is there a sufficiently arguable contravention of the ACL

Section 24 of the Fair Trading Act 1989 No. 84 (Qld) provides that the ACL applies to the State of Queensland so far as it carries on a business either directly or by an authority of the State. Thus, the ACL will only apply to QBCC (and its employees) to the extent that it carries on a business.

While Greenwood J was willing to accept that QBCC, so far as the statutory insurance scheme is concerned, is carrying on a business in that aspect of its activities, his Honour held that the impugned conduct, as pleaded, did not occur in the course of the QBCC conducting its insurance activities. Nor did the impugned conduct occur in the course of "trade or commerce". Rather, the conduct pleaded occurred in the course of the regulatory functions of QBCC and in connection with the recovery from SRC of monies paid by QBCC to the homeowners. As his Honour was not satisfied that the causes of action were arguably raised, the application was dismissed with costs.

6.2 Court clarifies the prohibition on unfair preference payments

(By Chris Yapanis, King & Wood Mallesons)

Re Eliana Construction and Developing Group Pty Ltd (No 2) [2019] VSC 546 (19 August 2019) Supreme Court of Victoria, Robson J

(a) Summary

The judgment of Robson J clarifies the circumstances in which the repayment of a debtor's debt by a third party is taken to be a payment made by the debtor to the creditor for the purposes of determining whether an unfair preference payment has been made under s. 588FA of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act). For Robson J, to satisfy s. 588FA of the Corporations Act, the payment by the third party must involve a reduction in the debtor's assets, which can be measured in money, and a consequential discharge of the creditor's debt by that sum. This will occur where the third party owes a pre-existing debt to the debtor which is greater than or equal to the debt owed by the debtor to their creditor. The mere authorisation and ratification of the third party's payment by the debtor is insufficient for the payment to be classified as a payment from the debtor for the purposes of s. 588FA of the Corporations Act.

(b) Facts

Eliana Construction and Developing Group Pty Ltd (Eliana) carried out a property development and building business. Eliana engaged Mad Brothers Earthmoving Pty Ltd (Mad Brothers) to carry out earthmoving works at various sites. By March 2016, Eliana had incurred a debt of $236,952.31 with Mad Brothers. On 23 March 2016, Mad Brothers issued a letter of demand to Eliana for payment of this outstanding debt. The letter stated that proceedings would be commenced against Eliana if the debt was not repaid by 29 March 2016. Eliana did not comply with the letter of demand.

In April 2016, Mad Brothers issued a statutory demand to Eliana for repayment of the debt. Eliana did not comply with this statutory demand. On or around 8 June 2016, Mad Brothers issued a winding-up application against Eliana, which was listed for hearing on 20 July 2016. The application was adjourned on three occasions. Prior to the final return date of the winding-up application, Eliana agreed to pay $220,000 to Mad Brothers in full discharge of the debt. In exchange, Mad Brothers agreed to settle the winding-up proceedings.

Rock Development & Investments Pty Ltd (Rock Development), a related company of Eliana, borrowed money from Nationwide Credit Pty Ltd on security provided by Rock Development. From this loan, Mad Brothers was paid $220,000 to discharge Eliana's debt pursuant to the settlement agreement.

Following the repayment of this debt, Eliana ceased trading. Eliana was then placed into voluntary administration. In November 2016, Eliana was placed into liquidation. The liquidator pursued the payment to Mad Brothers as a preference payment under s 588FA of the

Corporations Act. At first instance, Efthim AsJ decided that Eliana had made a preference payment to Mad Brothers under s 588FA of the Corporations Act, and that Mad Brothers could not establish the "good faith" defence under s 588FG of the Corporations Act.

(c) Decision

(i) Issues

The key overarching issue for Robson J was whether the conditions in s. 588FA(1) of the Corporations Act were satisfied in the circumstances. Specifically, this issue could be reduced to whether the payment received by Mad Brothers should be taken to have been made by Eliana. If s. 588FA(1) of the Corporations Act was satisfied, then a further issue arose as to whether Mad Brothers could establish the "good faith" defence in s. 588FG of the Corporations Act.

(ii) Was s. 588FA(1) of the Corporations Act satisfied in the circumstances?

To satisfy s. 588FA(1) of the Corporations Act, two conditions must be established. First, Eliana and Mad Brothers must be parties to a transaction (s. 588FA(1)(a) of the Corporations Act). Second, the transaction must result in Mad Brothers receiving from Eliana more than it would have received from Eliana in a winding up (s. 588FA(1)(b) of the Corporations Act). Prior to assessing the satisfaction of these two conditions, Robson J dealt with the contention that Rock Development owed moneys to Eliana, as this was critical for resolving condition two of the s. 588FA(1) test. Robson J ultimately concluded that the evidence was insufficient to establish that Rock Development was indebted to Eliana.

Robson J proceeded to analyse condition one of the s. 588FA(1) test. His Honour followed established case law in deciding that a relevant "transaction" is constituted for the purposes of s. 588FA(1)(a) of the Corporations Act where a debtor and third party enter into an arrangement whereby the debtor's creditor is paid by the third party. This type of arrangement occurred between Eliana, Rock Development and Mad Brothers. Therefore, Robson J found limb one of the s. 588FA(1) test to be satisfied.

Robson J continued on to the "critical question" of whether the second limb of s. 588FA(1) of the Corporations Act had been satisfied. For this second limb to be established, the payment to Mad Brothers must be taken to be made by Eliana. In situations where a debtor's debt is repaid to their creditor by a third party, there is conflicting authority on the test to be applied for determining whether the payment is taken to be made by the debtor.

In *Burness (as liquidator of Denward Lane Pty Ltd (in liq)) v Supaproducts Pty Ltd* [2009] FCA 893, Gordon J (in *obiter*) considered that it was not necessary for there to be evidence of a debtor/creditor relationship between the debtor and the third party in order for a third party payment to be a preference. For Gordon J, it was sufficient to characterise a debt as being paid by the debtor to the creditor where it was paid by a third party to the creditor, if the debtor authorised and ratified the payment by the third party. However, in *Re Evolvebuilt Pty Ltd* [2017] NSWSC 901, Brereton J (also in *obiter*) held that the decision of Gordon J on the second limb of s. 588FA(1) of the Corporations Act was in error. For Brereton J, the fact that the debtor merely requested or acquiesced in the third party repaying the creditor was insufficient to establish that the payment was made by the debtor.

Robson J ultimately sided with the judgment of Brereton J. For Robson J, a transaction involves a payment by the debtor to the creditor, which satisfies limb two of the s. 588FA(1) test, where the transaction involves a reduction in the debtor's assets which can be measured in money and a consequential discharge of the creditor's debt by that sum. Where a third party payment discharging the debtor's debt to the creditor is authorised and ratified by the debtor but only involves the debtor incurring a liability in favour of the third party, and no reduction of assets of the debtor, then the payment does not constitute a payment by the debtor to the credit under s. 588FA(1)(b) of the Corporations Act.

On the facts of this case, the only circumstances in which Rock Development's payment to Mad Brothers would involve a reduction in Eliana's assets would be if Rock Development owed Eliana a pre-existing debt of $220,000 or more. As previously discussed, Robson J determined that there was insufficient evidence to reach this conclusion. His Honour decided that the payment had not been made by Eliana for the purposes of s. 588FA(1)(b) of the Corporations Act. This finding was sufficient to decide in favour of Mad Brothers.

(iii) Could Mad Brothers satisfy the "good faith" defence?

Despite deciding the case on the basis that there had been no unfair preference under s. 588FA(1) of the Corporations Act, Robson J proceeded to assess the "good faith" defence under s. 588FG(2) of the Corporations Act. This analysis is strictly *obiter*. Mad Brothers challenged the findings of Efthim AsJ on evidentiary grounds. Robson J decided that Efthim AsJ erred in failing to have proper regard to matters occurring after the statutory demand was issued but prior to payment being received by Mad Brothers. According to Robson J, taking these matters into account ought to lead to the conclusion that the "good faith" defence was satisfied by Mad Brothers. This is because the facts and matters which subsisted at the time Mad Brothers received payment fell short of being capable of establishing a positive apprehension that Eliana was insolvent in the mind of a reasonable person.

6.3 Oppressive conduct in a "quasi-partnership"

(By Maggie Skow, Clayton Utz)

Re SRW Nominees Pty Ltd [2019] VSC 547 (19 August 2019) Supreme Court of Victoria, Robson J

(a) Summary

In a matter where a business was conducted as a "quasi-partnership", the Supreme Court of Victoria (the Court) has held that the conduct of one partner towards the other, namely exclusion from management and a failure to distribute profits for three years, amounted to oppressive conduct under s. 232 of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act).

(b) Facts

In 1999, Mr Reiner and Mr Wajsman entered into an agreement that was essentially akin to a partnership agreement (the 1999 Agreement). They founded various companies, including SRW Nominees Pty Ltd (SRW), the main trading entity that carried on the business of commercial kitchen cleaning. Together, the companies were referred to as the Big Ben Group (the Business). Mr Reiner's company Laurient Holdings Pty Ltd (Laurient) and Mr Wajsman's company Softpro Australia Pty Ltd (Softpro) each held an equal share in SRW. The 1999 Agreement entitled Mr Reiner and Mr Wajsman to share equally in the profits of the Business and to participate in management of the Business.

The Business was run in accordance with the 1999 Agreement until 2016, when Mr Reiner suffered a heart attack. At this point, he stopped assisting in management and moved to the US to recuperate for a year on the recommendation of his doctor. Mr Wajsman became solely responsible for running the Business in Mr Reiner's absence. During this time, Mr Wajsman:

- refused to distribute any profits to Mr Reiner or his company Laurient;
- removed Mr Reiner as a director of all companies in the Business without informing Mr Reiner and then refused to reinstate him when requested; and
- caused the companies to pay the personal expenses of Mr Wajsman to the detriment of Mr Reiner.

Mr Reiner and his company Laurient commenced proceedings against Mr Wajsman after one year, claiming the above three behaviours amounted to oppressive conduct under s. 232 of the Corporations Act.

Mr Wajsman alleged in defence that all acts were done for proper corporate reasons, that Mr Reiner had said that he did not want money whilst living overseas, that he absented himself from management and resigned as a director, meaning he was not entitled to demand profit or reinstatement.

(c) Decision

What constitutes oppressive conduct?

A court can make an order under s. 233 of the Corporations Act, if there is behaviour which is "oppressive to, unfairly prejudicial to or unfairly discriminatory against" a member.whether in that capacity or in any other capacity. Case law has held that the above factors should be considered as various aspects of the essential criteria, which is commercial unfairness to a member or members (*Hillman v Ample Source International Ltd (No 2)* (2012*)* 202 FCR 336). The court must determine whether, on the balance of probabilities, an objective commercial bystander would be satisfied that the affairs of the company were being conducted unfairly. The context is also relevant to determine the fairness of the conduct.

Was there a quasi-partnership?

Robson J held that the relationship between the parties had particular significance in a finding of oppression. In particular, the fact that the Business operated as a "quasi-partnership", fulfilling the elements set out by Lord Wilberforce in *Ebrahimi v Westbourne Galleries Ltd* [1973] AC 360. These were that:

- the association between the partners was of a personal relationship;
- there was an understanding that each shareholder would participate in the conduct of the business, as established in the 1999 Agreement; and
- the 1999 Agreement provided for the restriction upon the transfer of the members' interest in the company.

Grounds of oppression

(i) Exclusion from participation in management

Where a corporation operates as a "quasi-partnership", excluding a member from management can establish oppressive conduct.

Robson J held that Mr Wajsman excluded Mr Reiner from participation in management. Examples of this conduct included Mr Wajsman:

- removing Mr Reiner as a director;
- failing to reappoint him when requested;
- refusing to enable him to return to managing and working in the Business when he returned to good health; and
- failing to reinstate his access to the companies online bank accounts.

Further, Mr Reiner was not given an opportunity to remove his capital as Mr Wajsman would not buy his shares and his indispensability to the Business ensured he could control any sale.

(ii) Failure to distribute any funds to Mr Reiner

It is clear from case law that a failure to distribute profits can constitute oppression.

In this case, Mr Wajsman refused to make any distribution to Mr Reiner and instead used the companies' spare capital, after paying himself, to aggressively pay down companies' debts. Robson J dismissed Mr Wajsman's claims that it was a legitimate and necessary business decision. Particularly since this behaviour was an extreme change of practice, it was not justified by the level of debt owed by the Business and Mr Reiner was not consulted.

Robson J held that it was clearly commercially unfair to fail to make any payments to Mr Reiner, a 50% shareholder, for three years, without an adequate justification, particularly where the Business was his sole source of income.

(iii) Payment of personal expenses of Mr Wajsman

The third ground of oppression claimed was that Mr Wajsman caused the Business to pay his personal expenses, including his legal fees of approximately $70,000. This was to the detriment of Reiner, as no such payment by the Business was made for his legal fees. It is well established that the use of company funds to defend an oppression suit is, of itself, oppressive. As such, this ground was established.

(iv) Order

Robson J held that the conduct of the relevant companies caused by Mr Wajsman was contrary to the interests of the members as a whole and oppressive to, unfairly prejudicial to and unfairly discriminatory against Mr Reiner. As such, the above three grounds of oppression were made out.

Robson J made an order under s. 233 of the Corporations Act requiring Mr Wajsman and his company to complete what had been done in practice, to take full control of the Business and purchase Mr Reiner's share in the Business at a price to be determined by the Court.

This was held to be a fair remedy as it was not appropriate to wind up the Business or order a sale to the public as the Business had far more value to Mr Wajsman than a third party buyer due to Mr Wajsman's close association to the Business.

6.4 High Court holds that legal professional privilege may not found a cause of action

(By Andrew Harpur and Tim West, Ashurst)

Glencore International AG v Commissioner of Taxation [2019] HCA 26 (14 August 2019) High Court of Australia, Kiefel CJ, Bell, Gageler, Keane, Nettle, Gordon and Edelman JJ

(a) Summary

In a unanimous judgment, the High Court of Australia (the High Court) dismissed proceedings by companies within the global Glencore plc group (the Glencore group) seeking an injunction to restrain the Australian Taxation Office (ATO) from making any use of documents subject to legal professional privilege (the privilege).

The privileged documents obtained by the ATO were amongst the "Paradise Papers", a cache of over 13 million confidential electronic documents relating to offshore investments, leaked to the International Consortium of Investigative Journalists.

The High Court held that the privilege is not an actionable legal right capable of sounding in injunctive relief. The privilege is only an immunity from the exercise of powers that would otherwise compel the disclosure of privileged communications.

The effect of the High Court's decision is that if privileged documents become public, for example because of being illegally hacked, the document owner may be unable to recover them or prevent third parties using them. Document owners may still, however, be able to bring an action to prevent their misuse or disclosure by anyone who obtained or was proposing to disclose the documents in breach of confidence.

(b) Facts

In late 2017, the "Paradise Papers", a cache of over 13 million confidential electronic documents relating to offshore investments, was leaked to the International Consortium of Investigative Journalists.

The leaked material included documents relating to Glencore, relevantly advice from Appleby, the Bermudan law firm whose documents were stolen. That advice related to a restructure of four Australian companies within the Glencore group in a transaction called "Project Everest". In subsequent meetings with Glencore, the ATO indicated that it was in possession of the documents and that it was seeking to identify possible Australian links to tax avoidance.

Glencore commenced proceedings in the original jurisdiction of the High Court, seeking an injunction to restrain the ATO's use of the documents, and orders requiring that the ATO return the documents in its possession.

The Association of Corporate Counsel (the ACC) was granted leave to appear as *amicus curiae* at the hearing to make submissions in support of Glencore. The ACC sought to rely upon what it contended were important matters of public policy in support of extending the scope of the privilege. In particular, the ACC submitted that, in a world where law firms, corporations and governments are increasingly the target for sophisticated cyber-attacks, Australia is potentially at risk of becoming an attractive place for hackers to access and leak stolen privileged documents. This could in turn lead to the blackmailing of companies, and threats that the documents would be released to executive agencies unless the hackers' demands were met.

(c) Decision

In a unanimous judgment, the High Court dismissed Glencore's proceeding, refusing the injunctive relief sought.

(i) Legal professional privilege is a common law immunity

At the heart of Glencore's case was the proposition that, while the privilege has long been recognised as a fundamental common law right, the law is yet to, but should, recognise a complete set of remedies to protect that right.

Glencore also submitted that the scope of the privilege should reflect the policy of the law upon which it is based - namely, the administration of justice through fostering of trust and candour in the relationship between lawyer and client, and the recognition of an actionable right to restrain the use and recovery of privileged documents, advances this policy.

The High Court rejected these submissions, holding that Glencore's argument rested fundamentally upon the false premise that because the privilege is a legal right which is capable of being enforced it may also found a cause of action. Consistently with its decision in *Daniels Corporation v ACCC* (2002) 213 CLR 543 (*Daniels*), the High Court reaffirmed that the privilege is only available as an immunity from the exercise of powers to compel the disclosure of privileged communications (as opposed to the foundation for a cause of action).

The High Court also considered in some detail the historical operation of the privilege, drawing from those origins the conclusion that privilege arose in response to the exercise of powers by the state to compel the disclosure of confidential communications between lawyer and client.

The High Court held that the true character of the substantive "right" spoken of in various cases including by the High Court in *Daniels* was a right to resist the compulsory disclosure of information, or to decline to disclose or allow to be disclosed the confidential communications or documents in question.

In response to Glencore's submissions concerning the need for the scope of the privilege to reflect the policy of the law upon which it is based, the High Court held that the purpose of the law, in providing an immunity, is to enhance the administration of justice. By way of contrast, the law is not concerned to further a client's personal interest in preventing the use which might be made by others of that client's communications if they obtain them.

The High Court observed that, on the present state of the law, once privileged communications have been disclosed, the affected party must instead resort to equity and the doctrine of breach of confidence if it wishes to restrain the use of that material.

Glencore's argument for the grant of injunctive relief on any basis other than breach of confidence was inconsistent with how the common law develops - namely, by applying settled principles to new circumstances, and by reasoning from settled principles to new conclusions. The High Court was not persuaded that the policy considerations relied upon by Glencore justified what it considered would be an abrupt change in the law.

(ii) Implications

The equitable doctrine of breach of confidence may be called upon when privileged communications have been disclosed and an injunction is sought to restrain the misuse of confidential information. It appears that this avenue was not available to Glencore in this instance given that the ATO had obtained the documents from the public domain. In that sense it might be said that there is a gap in the law as it does not otherwise afford protection against the use of privileged documents, which by the very nature of their privileged status are presumed to be confidential to the client.

Other avenues to protect privileged material (for example, any tort of unjustified invasion of privacy) may be available to parties in different circumstances, and it remains to be seen whether those areas of law may be developed by the courts to meet the recognised need to adequately protect privileged material from sophisticated cyber-attacks.

For the time being, however, this decision should serve as a reminder that while the law recognises the privilege as an immunity from production or disclosure in certain circumstances, clients should remain vigilant and conscious of the risk that the contents of their privileged communications might be revealed due to matters beyond their control. This reinforces the need to be circumspect whenever committing matters to writing regardless of whether they are likely to be privileged, at least at the outset.

6.5 ASIC's responsible lending test case has failed, (but it's still a live issue?)

(By Kate Hlider and Mark Standen, MinterEllison)

Australian Securities and Investments Commission v Westpac Banking Corporation (Liability Trial) [2019] FCA 1244 (13 August 2019) Federal Court of Australia, Perram J

(a) Summary

On 13 August, Perram J handed down his landmark decision on the boundaries of responsible lending obligations in *Australian Securities and Investments Commission v Westpac Banking Corporation (Liability Trial)* [2019] FCA 1244. The case, brought by the ASIC as a "test case" has received a high level of media coverage, especially in the context of ASIC's proposed updates to its responsible lending guidance and in light of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry.

The Federal Court dismissed ASIC's case and ordered the regulator to pay the bank's costs. ASIC announced on 10 September that it would appeal the decision.

Perram J found that a lender "may do what it wants in the assessment process" and is not obliged under the National Consumer Credit Protection Act 2009 No. 134 (Cth) (the NCCP Act) to take into account a prospective borrower's actual/declared expenses when assessing whether a loan will be unsuitable to consumers.

ASIC has said "it took on the case against Westpac because of the need for judicial clarification of a cornerstone legal obligation on lenders, this is why ASIC refers to this case as a "test case". As a regulator, it is ASIC's role to test the law".

(b) Facts

The the NCCP Act requires lenders to assess whether loans will be unsuitable for consumers. The litigation related to Westpac's home loan assessment process during the period December 2011 and March 2015, during which approximately 260,000 home loans were approved by Westpac's automated decision system.

ASIC alleged that Westpac breached its responsible lending obligations under the NCCP Act because its automated decision system:

- did not have regard to consumers' declared living expenses when assessing their capacity to repay home loans (instead relying on the Household Expenditure Measure (HEM)); and
- Westpac used the incorrect method when assessing a consumer's capacity to repay a home loan at the end of the interest-only period. ASIC alleged that Westpac was required to have regard to the higher repayments at the end of the interest-only period in assessing home loans of this kind but, did not do so.

(c) Decision

Perram J rejected ASIC's case on both grounds

(i) ASIC's case failed on the first ground both on the facts "and as a matter of statutory construction"

On the first ground, Perram J rejected ASIC's case on the basis that as a matter of fact, "Westpac did have regard to.declared living expenses". Perram J went on to observe that even if this were not so, "the NCCP Act does not operate as ASIC alleges".

No requirement to use a prospective borrower's declared living expenses

Perram J observed that "the NCCP Act requires a credit provider to ask itself only whether 'the consumer will be unable to comply with the consumer's financial obligations under the contract' or, alternatively, whether the consumer 'could only comply with substantial hardship'" (the s. 131(2)(a) Questions). Further, though the NCCP Act "requires a credit provider to ask the consumer about their financial situation (s. 130(1)(b)) and, in turn, to ask itself-and to answer the s. 131(2)(a) Questions, there is no "further consequence that the credit provider must use the consumer's declared living expenses in doing so".

In fact, Perram J observes that the NCCP Act is "silent on how a credit provider is to answer the s. 131(2)(a) Questions. The NCCP Act "contains neither an express statement that a credit provider must use the consumer's declared living expenses in doing so nor, in my opinion, can such a requirement be discerned from its terms as a matter of necessary intendment".

Perram J went on to state that the only way that one or more declared living expenses can be shown to be necessarily relevant to the issue of whether the consumer can afford to make the repayments is by identifying some living expenses "which simply cannot be foregone or reduced beyond a certain point'. In illustration, Perram J observed, "I may eat Wagyu beef everyday washed down with the finest shiraz but, if I really want my new home, I can make do on much more modest fare. Knowing the amount I actually expend on food tells one nothing about what that conceptual minimum is. But it is that conceptual minimum which drives the question of whether I can afford to make the repayments on the loan".

Ultimately, Perram J took the view that "a credit provider may do what it wants in the assessment process, so far as I can see; what it cannot do is make unsuitable loans. ASIC's argument creates a whole new range of implied rules which appear altogether unnecessary".

Use of the Household Expenditure Measure (HEM) benchmark

ASIC did not allege that Westpac was entirely prohibited by the NCCP Act from using the HEM benchmark in assessing whether a loan was unsuitable (i.e. answering the s. 131(2)(a) Questions).

Rather, ASIC's case was that Westpac was obliged not to place sole reliance on it (and instead was required to take into account the consumer's declared living expenses). Given Perram J's rejection of this view, he observed that the use of the HEM "was of marginal relevance" by the conclusion of the trial.

"ASIC is either right or wrong in its contention that Westpac was obliged to base its assessment of unsuitability on the consumer's declared living expenses. If ASIC is right about that, it is irrelevant whether the HEM benchmark is a good, bad or indifferent proxy for substantial hardship because, regardless, this can have no impact on the fact that Westpac failed to take into account any of the declared living expenses. If, on the other hand, ASIC is wrong about that, the qualities of the HEM benchmark also do not matter because they have no impact on the result. This is because ASIC will, on that hypothesis, already have failed. Consequently, the capacity of the HEM benchmark to serve as a proxy for substantial hardship is not an issue which is actually live in the litigation" Perram J states.

Perram J went on to say that he could see "no utility in resolving the issue. Beyond the fact that the HEM benchmark appears to be a mechanism for assessing hardship and Westpac thought it to be such, I see no relevance to this material".

(ii) ASIC's case also failed on the second ground

Perram J also rejected ASIC's argument that Westpac breached the NCCP Act in the manner in which it answered the s. 131(2)(a) Questions in the case of loans having an initial interest only period before payment of principal was required.

"Westpac's legal obligation was to ask and answer the s. 131(2)(a) Questions. The fact that it did so as if the loan did not involve an initial interest only period does not mean that it did not ask and answer those questions. ASIC alleges that Westpac contravened the Act in this way on 154,351 occasions across the same period as its first allegation (these loans are a subset of the 261,987 loans which figure in ASIC's primary case). ASIC's case on these loans fails too" Perram J found.

(iii) Responses to the decision

Westpac has welcomed the clarity provided by the decision

In a short statement by Westpac acknowledging the responsible lending ruling, Westpac Chief Executive (Westpac Consumer Division) David Lindberg, said: "Westpac has always sought to lend responsibly to customers and takes its lending obligations very seriously. This is an important test case for the industry, and we welcome the clarity that today's decision provides for the interpretation of responsible lending obligations".

The statement adds that "Westpac aims to build and maintain constructive and trusted working relationships with its regulators, including when we have a genuine difference of opinion. When this occurs, our preference is to resolve the difference in an open, transparent and respectful way".

ASIC's initial response: "as a regulator, it is our role to test the law and its ambit". In a statement, ASIC Commissioner Sean Hughes said that "ASIC took on the case against Westpac because of the need for judicial clarification of a cornerstone legal obligation on lenders, this is why ASIC refers to this case as a 'test case'. As a regulator, it is our role to test the law and its ambit. The obligation to assess loan applications builds on the requirement for banks to make inquiries about a borrower's financial circumstances and capacity to service a loan and to verify the information that borrowers give banks". He added that "ASIC is reviewing the judgment carefully".

Commenting on the impact of the decision on ASIC's proposed updates to its responsible lending guidance, The Australian Financial Review quotes Mr Hughes as saying that he does not believe that the decision "in and of itself in any way undermines our [ASIC's] additional guidance and if anything cements why we need guidance in the first place".

(iv) Still a live issue? ASIC has filed an appeal

On 10 September, ASIC announced that it had filed an appeal with the Full Federal Court against the decision. ASIC Commissioner Sean Hughes explained that the regulator is appealing the decision because ASIC "considers that the Federal Court's decision creates uncertainty as to what is required for a lender to comply with its assessment obligation, nor does ASIC regard the decision as consistent with the legislative intention of the responsible lending regime".

Note: ASIC's notice of appeal is available on the ASIC website and provides further detail.

6.6 Voiding insolvent transactions in New Zealand: statutory requirements are the only requirements

(By Natalie Sher, King & Wood Mallesons)

Robt. Jones Holdings Limited v McCullagh [2019] NZSC 86 (9 August 2019) Supreme Court of New Zealand, Glazebrook, O'Regan, Ellen France, Arnold and Kós JJ

(a) Summary

The Supreme Court of New Zealand (the Supreme Court) has confirmed that a liquidator seeking to void an insolvent transaction only needs to establish that the transaction meets the statutory requirements outlined in s. 292 of the *Companies Act 1993 (NZ)* (the *Companies Act*).

Section 292(1) of the *Companies Act* provides that a transaction is voidable by the liquidator if it is an "insolvent transaction" and it is "entered into within the specified period" (the period of two years before the liquidator is appointed).

Section 292(2) of the *Companies Act* provides that an insolvent transaction is a transaction by a company that is entered into at a time when the company is unable to pay its due debts, and enables another person to receive more towards satisfaction of a debt owed by the company than the person would receive, or would be likely to receive, in the company's liquidation.

The Supreme Court unanimously confirmed that there is no additional common law principle requiring that the transaction have diminished the net pool of assets available to creditors.

(b) Facts

(i) Background

Northern Crest Investments Ltd (Northern Crest) leased a property owned by Robt. Jones Holdings Limited (RJH). Northern Crest fell behind on its rent payments, and the parties entered into various settlement agreements under which they agreed on the amount necessary to satisfy Northern Crest's liability to RJH under the lease.

A subsidiary of Northern Crest, MSH No 2 Pty Ltd (MSH2), made a payment of $262,758.05 to RJH on behalf of Northern Crest in partial satisfaction of Northern Crest's liability to RJH under the lease (MSH2 payment).

Liquidators were ultimately appointed to Northern Crest, and they sought to recover the MSH2 payment on the basis that it was a voidable transaction under s. 292 of the *Companies Act*.

It was agreed that the MSH2 payment was made within the period of two years prior to the liquidation of Northern Crest. By the time this case reached the Supreme Court, RJH had also accepted that the MSH2 payment met the other statutory requirements of s. 292 of the *Companies Act*.

However, RJH submitted that there was an additional requirement of diminution, and that no such diminution had occurred because of the way in which the MSH2 payment was structured. In particular, RJH argued that as the payment was made by MSH2 directly to RJH, there was no change in the position of Northern Crest insofar as other creditors were concerned. RJH contended that by replacing Northern Crest's debt to RJH with a debt for the same amount to MSH2, the transaction simply substituted one creditor for another.

(ii) Issues

RJH contended that the requirement of diminution arose under common law, and had survived the reforms introduced by the *Companies Act*.

The liquidators argued that the statutory requirements outlined in s. 292 of the *Companies Act* were exhaustive. The liquidators contended that an additional common law requirement of diminution would:

- undermine the intended simplicity of the corporate insolvency regime;
- have broader consequences for other types of payment, including payments made from overdrawn accounts. Such payments are funded by bank debt and offset by a contemporaneous increase in debt owed to the bank; and
- create artificiality based on how transactions are structured, rather than focusing on the ultimate economic effect of such transactions.

(c) Decision

The Supreme Court upheld the Court of Appeal's earlier decision, unanimously confirming that a liquidator seeking to void an insolvent transaction only needs to establish that the transaction meets the legislative criteria outlined in s. 292 of the *Companies Act*.

The Supreme Court confirmed that there is no additional common law principle of diminution.

(i) Plain text reading of s. 292 of the *Companies Act*

The Supreme Court held that a plain text reading of s. 292 of the *Companies Act* does not indicate that there is any unstated requirement of diminution in addition to the express statutory requirements of the section.

(ii) Purpose of the regime

The Supreme Court rejected RJH's contention that the primary purpose of the voidable transactions regime is to prevent a reduction in the pool of assets available to creditors.

The Supreme Court noted that there are other key policy objectives of such a regime, including ensuring creditor equality and deterring creditors from prematurely pushing companies into liquidation.

(iii) Existence of a common law diminution requirement in relation to predecessor provisions is not authoritative

The Supreme Court considered that while there may be established authority to the effect that a diminution requirement was applied to predecessor provisions, such authority is of limited weight in relation to s. 292 of the *Companies Act*.

The Supreme Court noted that the predecessor provisions had been formulated with a focus on debtor intention, which provided greater scope for the imposition of an additional common law requirement of diminution. By contrast, s. 292 of the *Companies Act* focuses solely on the effect of a transaction.

Accordingly, the Supreme Court held that cases decided in relation to previous statutory regimes cannot be said to support the existence of a common law diminution requirement in relation to s. 292 of the *Companies Act*.

(iv) Policy considerations

The Supreme Court considered that the imposition of an additional common law requirement of diminution would result in significant complexity and artificiality. According to the Supreme Court, this would undermine Parliament's stated purpose in reforming the voidable transactions regime to promote simplicity and efficiency.

6.7 Court approves application for validation of plaintiff's acquisitions of shares in company

(By Davina Khoo, DLA Piper)

In the matter of Rand Mining Limited [2019] VSC 529 (9 August 2019) Supreme Court of Victoria, Gardiner AJ

(a) Summary

Rand Mining Limited (Rand) acquired shares in Tribune Resources Limited (Tribune), and sought validation of the acquisition to subsequently dispose of the subject shares. The acquisition would otherwise be void due to s. 259C of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act). Section 259C(1) of the Corporations Act provides that the issue or transfer of shares of a company to an entity it controls within the meaning of s. 259E of the Corporations Act is void, subject to certain exemptions. Section 259C(2) of the Corporations Act provides that

ASIC may exempt a company from the operation of this section but the authorities dealing with this provision make clear that such an exemption can only be issued prospectively.

The key considerations were whether to grant orders under s. 1322(4) of the Corporations Act to validate the share transfer, whether it was just and equitable to make such an order, or whether the order led to a substantial injustice. The transfer was validated. Gardiner AJ was satisfied that there was no substantial injustice caused by the transfer of the relevant shares, or the orders sought by the plaintiffs. It was deemed just and equitable that the orders sought be made.

(b) Facts

Rand and Tribune are both resource companies listed on the ASX. On 26 January 2010, Tribune held 8,317,364 shares in Rand, representing approximately 20.51% of the total voting power in Rand. On 27 January 2010, Tribune acquired a further 18,359,400 ordinary shares in Rand pursuant to a rights issue, and underwrote this rights issue. Tribune acquired approximately 43.85% of the total voting power in Rand, and obtained "control" of Rand. Between 7 January 2014 and 15 January 2014, Rand acquired 1,135,000 shares in Tribune (Relevant Shares) from Melanie Verheggen and Kim Parham (the Vendors). On 8 January 2014, Rand held 11,923,904 shares in Tribune, and approximately 23.70% of the voting power. Mr Billis, director of both Rand and Tribune, deposed that Ms Verheggen's husband approached him on behalf of the Vendors, requesting that Rand purchase their shares in off-market transactions. Mr Verheggen stated that the Vendors were seeking to sell their shares as they were experiencing financial difficulties, and because the market for the stock in Tribune was illiquid, were unable to sell their shares on-market.

On 26 October 2018, the Takeovers Panel made orders (the 2018 Orders) for the divestment of the shares held by Rand in Tribune, other than the Relevant Shares. On 26 November 2018, a Review Panel varied the 2018 Orders (the Variation of Orders) by removing the requirement for the Appointed Seller as defined in the 2018 Orders to notify ASIC in certain circumstances and clarifying the operation of the 2018 Orders, but otherwise affirming the 2018 Orders.

Following the Variation of Orders, Rand's shares in Tribune (other than the Relevant Shares) were vested in the Commonwealth on trust for Rand to be sold. A Form 605 Notice of ceasing to be a substantial holder (Form 605 Notice) noting that Rand ceased to be a substantial holder in Tribune was lodged with ASIC. The annexure to the Form 605 Notice referred to the fact that the Relevant Shares were not subject to the Takeovers Panel divestment orders and that Rand intended to seek a court order to clarify the position to enable the Relevant Shares to be sold and for the proceeds of sale to be distributed to Rand. Rand's solicitors provided the Form 605 Notice in draft form to ASIC, consulted with ASIC on it prior to lodging the form, and wrote to ASIC detailing the nature of the application.

ASIC responded to that letter in an email of 26 March 2019, requiring a third party broker be appointed by Rand to undertake the sale of the Relevant Shares but agreeing to a longer sale period. The applicant's solicitors responded, attaching an updated proposed order providing for the appointment of a third party broker and specifying a six month sale period. ASIC replied, stating that the updated proposed orders were in an acceptable form.

(c) Decision

Gardiner AJ made orders pursuant to s. 1322(4) of the Corporations Act for validation of share transfers that would otherwise be void under s. 259C of the Corporations Act. ASIC was on notice of the application and was content for it to proceed subject to the inclusion of undertakings. It was just and equitable that the orders sought be made. Counsel for Rand, submitted that the factors that supported the court order included:

- the acquisition of the Relevant Shares occurred more than five years ago, and for the last five years, the Relevant Shares have been treated as being those of Rand. In particular, dividends have been paid by Tribune in relation to the Relevant Shares, which have been reflected in taxation returns filed by Rand;
- the acquisitions were disclosed to the market at the time;
- the sellers of the Relevant Shares initiated the sales and received valuable consideration for the acquisition of their shares;
- there has been public disclosure by Rand in the Form 605 Notice;
- ASIC confirmed that the undertakings proposed to be given by Rand are in a form acceptable to it. They include undertakings to appoint an independent broker to sell the Relevant Shares, to sell the Relevant Shares within six months of the order; and excluding Rand's directors and their associates from acquiring any of the Relevant Shares (other than via an anonymous on-market sale); and
- there is no way of regularising Rand's holdings and enabling it to dispose of the void shares, other than with the assistance of the relevant court.

6.8 Disagreement in Federal Court over director recommendations of schemes

(By James Sippe, Herbert Smith Freehills)

Re Kidman Resources Limited [2019] FCA 1226 (30 July 2019) Federal Court of Australia, O'Callaghan J

(a) Summary

The Federal Court of Australia (the Court) granted orders allowing Kidman Resources Limited (Kidman) to convene and hold a meeting of ordinary Kidman shareholders to consider and, if thought fit, approve a scheme of arrangement under Part 5.1 of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) under which Wesfarmers Lithium Pty Ltd, a wholly owned subsidiary of Wesfarmers Limited, would acquire all of the ordinary shares in Kidman.

In his reasons, O'Callaghan J disagreed with the decision of Farrell J in *Re Gazal Corporation Limited* [2019] FCA 70 (*Re Gazal*), in which her Honour expressed the view that directors with an interest in the outcome of a scheme should, in general, not make a recommendation to shareholders as to how to vote on the scheme. In O'Callaghan J's view, the law ordinarily requires directors to make a recommendation, one way or the other, whether they stand to gain if the scheme is approved or not. His Honour considered that the appropriate way to deal with a director's interest is to ensure it is appropriately explained to shareholders in the scheme booklet.

(b) Facts

Kidman applied to the Court for standard orders to convene and hold a meeting of its ordinary shareholders to consider and, if thought fit, approve a scheme of arrangement under Part 5.1 of the Corporations Act under which Wesfarmers Lithium Pty Ltd, a wholly owned subsidiary of Wesfarmers Limited, would acquire all of the ordinary shares in Kidman for $1.90 per share.

The scheme booklet submitted to the Court for the purposes of the application included a unanimous recommendation by the directors of Kidman that shareholders vote in favour of the scheme. A unanimous recommendation had been agreed by Kidman and Wesfarmers in the implementation deed relating to the scheme.

The scheme booklet also disclosed that the Managing Director of Kidman, Mr Martin Donohue, would receive a bonus payment of one year's salary if the scheme were implemented. In addition, Mr Donohue held 972,954 performance rights which, if the scheme became effective, would convert into the same number of ordinary Kidman shares and so Mr Donohue would receive $1.90 for each of those shares.

(c) Decision

Counsel had drawn O'Callaghan J's attention to the decision by Farrell J in *Re Gazal* (and related decisions).

In *Re Gazal* (at 30), her Honour said that:

While it is most important that there be prominent disclosure in a scheme booklet of those matters which might, realistically, affect a director's judgment in making a recommendation about whether shareholders should vote in favour of approving a scheme, directors who are interested in the outcome of the scheme because they stand to receive a bonus or benefit (other than as a shareholder) only if the scheme proceeds should exercise caution in making recommendations and, in my view, generally should not do so.

O'Callaghan J acknowledged her Honour's view but stated that he respectfully disagreed, and preferred the earlier decision by Robson J in *Re SMS Management & Technology Ltd* [2017] VSC 257.

His Honour noted that:

- s. 412(1)(a) of the Corporations Act requires that the scheme booklet state any material interests of the directors, whether as directors, as members or creditors of the body or otherwise, and the effect on those interests of the compromise or arrangement in so far as that effect is different from the effect on the like interests of other persons (and the Corporations Regulations 1990 No. 455 (Cth) (Corporations Regulations) list certain specific information that must be disclosed); and
- r. 5.1.01(b) of, and r. 8301(a) of Schedule 8 to the Corporations Regulations provide, among other things, that the scheme booklet must set out, for each director, whether the director recommends the acceptance of the scheme or recommends against acceptance, and in either case, his or her reasons for so recommending, or that the director does not desire to make, or does not consider himself or herself justified in making a recommendation, and if the director so requires, his or her reasons for not wishing to do so.

In O'Callaghan J's view, this statutory and regulatory regime ordinarily requires directors to make a recommendation, one way or the other, whether they stand to gain if the scheme is approved or not. His Honour considered that shareholders would ordinarily expect the directors to make a recommendation, absent an explanation as to why the director has not done so, and that shareholders should have the benefit and guidance of the knowledge and expertise of the directors who are responsible for the operation and management of the target company and therefore ought to be best placed to express a view on whether the scheme is in shareholders' best interests.

O'Callaghan J held that the appropriate way to deal with any benefit that a director stood to receive if the scheme were approved is to ensure that it is sufficiently explained to shareholders in the scheme booklet. Having regard to the disclosures in the scheme booklet and the materials submitted to the Court by Kidman, his Honour was satisfied that there was adequate disclosure of Mr Donohue's incentive payment and the proposed treatment of his performance rights and that there was a reasonable commercial basis for both the proposed payment and the treatment of those performance rights.

O'Callaghan J granted the orders sought by Kidman.

His Honour also noted Farrell J's reference in *Re Gazal* (at 30) to the "common practice" of a director declining to make a recommendation to shareholders as to how they should vote and explaining the reason for so declining by reference to the substantial benefit to be received by that director if the scheme proceeds. His Honour stated that he was, with great respect, unaware of any such practice.