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Index info.regulatory@saiglobal.com

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

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1. Recent Corporate Law and Corporate Governance Developments

1.1 IOSCO consults on code of conduct fundamentals for credit rating agencies

On 10 February 2014, the International Organisation of Securities Commissions (IOSCO) published a consultation report on its Code of Conduct Fundamentals for Credit Rating Agencies, which proposes significant revisions and updates to the current IOSCO code of conduct for credit rating agencies (IOSCO CRA Code).

The IOSCO CRA Code is intended to offer a set of robust, practical measures as a guide to, and a framework for, CRAs with respect to protecting the integrity of the rating process, ensuring that issuers and users of credit ratings, including investors, are treated fairly, and safeguarding confidential material information provided to them by issuers.

The IOSCO CRA Code was first published in 2004 when few jurisdictions had laws governing activities of CRAs. It was later revised in 2008 after the outbreak of the global financial crisis to include significant disclosure provisions that addressed concerns regarding the quality of information that CRAs relied on, suggestions that CRAs were too slow to review existing ratings and make downgrades as appropriate, and the possible conflict of interest arising from CRAs advising issuers on how to design structured finance products.

IOSCO proposes to revise the IOSCO CRA Code to take into account the fact that CRAs are now supervised by regional and national authorities. The goal is to create an updated IOSCO CRA Code that works in harmony with the CRA registration and oversight programs that many IOSCO members have implemented in recent years, and that continues to operate as the international standard for CRA self-governance.

The proposed revisions result, in part, from the experience of IOSCO members in supervising CRAs. They also are informed by IOSCO´s previous work on CRAs, including a survey report describing the key risk controls established by CRAs to promote the integrity of the credit rating process and the procedures established to manage conflicts of interest.

The proposed revisions are designed to strengthen the IOSCO CRA Code by:

- enhancing provisions regarding protecting the integrity of the credit rating process, managing conflicts of interest, providing transparency, and safeguarding non-public information;

- adding measures regarding governance, training, and risk management; and
- seeking to improve the clarity of the IOSCO CRA Code.

The code of conduct is available on the IOSCO website.

1.2 Financial statement complexity

On 10 February 2014, the European Financial Reporting Advisory Group and the National Standard Setters of the United Kingdom, France, Germany and Italy published a Bulletin on financial statement complexity to promote discussion on this issue, and to help form European views that are influential in the debate on the IFRS Conceptual Framework.

Many recent reports have expressed concern that financial statements have become too complex, to the detriment of users' understanding. These reports acknowledge that some of this complexity arises because transactions are becoming increasingly complex. However, they also note other possible causes, including the degree of complexity in IFRSs.

Despite this common concern about complexity in financial statements and the criticism of IFRS as being too complex, neither the existing Conceptual Framework nor the IASB's discussion paper on the review of the Conceptual Framework include or propose much guidance on the issue.

The Bulletin reflects in detail on the causes of complexity in accounting and suggests that additional guidance in the Conceptual Framework could be of help to minimise complexity.

The bulletin is available on the FRC website.

1.3 Proposals to strengthen the Singapore securities market

On 7 February 2014, the Monetary Authority of Singapore (MAS) and Singapore Exchange (SGX) released a joint consultation paper setting out proposals to strengthen the securities market in Singapore.

The proposals follow an extensive review by MAS and SGX of the securities market in Singapore. The review concluded that while the securities market remains sound, there were three areas for improvement:

- promoting orderly trading and responsible investing - minimum trading price, collateral requirements for securities trading, and short position reporting requirements;
- improving the transparency of market intervention measures - transparency of trading restrictions imposed by securities intermediaries; and
- strengthening the process for admitting new listings and enforcing against listing rule breaches - reinforcing the SGX listings framework, strengthening powers to enforce regulatory actions against breaches of listing rules.

SGX separately announced measures to strengthen market transparency, effective from 3 March 2014.

These include:

- an issuer's board of directors will be required to approve the issuer's reply to a public query by SGX;
- SGX will publish a "Trade with Caution" announcement whenever issuers are unable to explain the trading activities which SGX is querying; and
- issuers will be required to notify SGX of discussions or negotiations that are likely to lead to a takeover, reverse takeover or a very substantial acquisition.

SGX has also published FAQs on its website regarding the use of its regulatory powers to suspend and designate a stock. These two tools are used sparingly by SGX in exceptional cases where anomalies in trading are observed.

The consultation paper is available on the MAS website.

1.4 IOSCO issues report on risks and benefits of financial return crowd-funding

On 5 February 2014, the Research Department of the International Organisation of Securities Commissions (IOSCO) published a Staff Working Paper entitled "Crowd-funding: An Infant Industry Growing Fast".

The report provides a global overview of the crowd-funding industry along with a mapping exercise of the global regulatory landscape. It seeks to identify investor protection issues and to determine whether crowd-funding poses a systemic risk to the global financial sector.

Crowd-funding is an umbrella term describing the use of small amounts of money, obtained from a large number of individuals or organisations, to fund a project, a business or personal loan, and other needs through an online web-based platform. The report analyses financial return crowd-funding (FR crowd-funding), which refers to peer-to-peer lending and equity crowd-funding.

FR crowd-funding is a type of market-based finance that could help stimulate economic recovery by channelling capital to small and medium-sized enterprises (SMEs). However, FR crowd-funding poses many risks and raises an array of investor protection issues. The report says the challenge facing regulators and governments around the globe is to strike a balance between encouraging crowd-funding and mitigating the risks associated with its growth, while protecting investor interests. The FR crowd-funding market has doubled year on year for the last five years to an estimated $6.4 billion in 2013, driven by annual growth of 90% in peer-to-peer lending. Peer-to-peer lending has spread across the globe, making FR crowd-funding a global phenomenon. The equity crowd-funding market is more modest in size and has grown at a slower pace.

The working paper identifies the main benefits of FR crowd-funding as the following:

- provides a boost to economic growth through flows of credit to SMEs and other users in the real economy;
- fills a credit gap left by banks;
- offers lower cost of capital/high returns, leveraging off a lower cost basis; and
- provides a new product for portfolio diversification.

The main risks are:

- risk of default;
- platform risk;
- risk of fraud;
- risk of illiquidity; and
- risk of investor inexperience.

The report concludes that the FR crowd-funding market does not present a systemic risk to the global financial sector at present. However, the report indicates that various factors could modify this outlook in the future. With the next evolution of this industry being in the global nature of funding sources, the challenges ahead will include cross-jurisdictional contractual and legal harmonisation, dispute settlement and resolution issues. IOSCO as a global standard setter for securities market regulators can have a role to play here in aiding regulators in monitoring the development of the industry.

The staff working paper is available on the IOSCO website.

1.5 European Parliament votes to approve criminal sanctions for market abuse directive

On 4 February 2014, a vote by the European Parliament's plenary approved the European Commission's proposal for a Directive on criminal sanctions for market abuse. After publication of the Directive in the Official Journal, expected in June, Member States will have two years to implement the Directive in national law.

The adoption of the Directive means that:

- there will be common EU definitions of market abuse offences such as insider dealing, unlawful disclosure of information and market manipulation;
- there will be a common set of criminal sanctions including fines and imprisonment of four years for insider dealing/market manipulation and two years for unlawful disclosure of inside information;
- legal persons (companies) will be held liable for market abuses;
- Member States need to establish jurisdiction for these offences if they occur in their country or the offender is a national; and
- Member States need to ensure that judicial and law enforcement authorities dealing with these highly complex cases are well trained.

Further information is available on the European Commission website.

1.6 SEC publishes draft strategic plan for public comment

On 3 February 2014, the US Securities and Exchange Commission (SEC) published for public comment its Draft Strategic Plan that outlines the agency's strategic goals for fiscal years 2014 to 2018.

The SEC's draft plan surveys the forces shaping its environment and outlines more than 70 initiatives designed to support its primary strategic goals.

The draft strategic plan is available on the SEC website.

1.7 APRA releases harmonised standard and proposed guidance on risk management

On 31 January 2014, the Australian Prudential Regulation Authority (APRA) released a package that harmonises and enhances its current risk management requirements.

The package includes the final cross-industry Prudential Standard CPS 220 Risk Management (CPS 220), a proposed prudential practice guide on risk management, and a response paper that addresses submissions received by APRA on the CPS 220 consultation package released in May 2013. APRA is also releasing an amended Prudential Standard CPS 510 Governance (CPS 510) to ensure that governance requirements related to risk management are aligned with those of CPS 220.

CPS 220 applies to authorised deposit-taking institutions (ADIs), general insurers, life insurers and single industry groups (Level 2 groups). The prudential standard will also apply to conglomerate groups (Level 3 groups) that APRA intends to determine by 1 January 2015. The prudential standard ensures the consistent application of APRA's risk management requirements across its regulated industries and reflects its heightened expectations in this area.

The final CPS 220 consolidates existing risk management standards for insurers and includes some risk management requirements for ADIs that are currently spread across a number of ADI prudential standards. The prudential standard comes into effect from 1 January 2015. CPS 220 will not apply in superannuation; Registrable Superannuation Entity (RSE) licensees must comply with the superannuation-specific risk management standard that came into effect on 1 July 2013.

APRA will finalise this prudential practice guide over the course of 2014.

CPS 220, CPS 510, the draft risk management prudential practice guide and the response paper are available on the APRA website.

1.8 IOSCO publishes recommendations regarding the protection of client assets

On 29 January 2014, the International Organisation of Securities Commissions (IOSCO) published the final report titled "Recommendations Regarding the Protection of Client Assets", which seeks to help regulators improve the supervision of intermediaries holding client assets.

Events such as the Lehman Brothers and MF Global insolvencies have placed client asset protection regimes in the spotlight. This is the result of investors trying to better understand the potential implications of placing their assets with particular intermediaries and in certain jurisdictions. Regulators also have been seeking to address risks to client assets and how to transfer or return client assets in default, resolution or insolvency scenarios.

The eight principles provide guidance to regulators on how to enhance their supervision of intermediaries holding client assets by clarifying the roles of the intermediary and the regulator in protecting those assets.

Many jurisdictions have rules and regulations governing client assets, although their protection regimes may vary across these jurisdictions. The report outlines the intermediary's responsibility to ensure compliance with these rules, including through the development of risk management systems and internal controls to monitor compliance. Where the intermediary places client assets with third parties, the intermediary should reconcile the client´s accounts and records with those of the third party. While the intermediary must comply with the client asset protection regimes, the regulator has a role in supervising the intermediary's compliance with the applicable domestic rules and maintaining a regime that promotes effective safeguarding of client assets, according to the report.

The report is available on the IOSCO website.

1.9 Structural reform of the EU banking sector

On 29 January 2014, the European Commission proposed new rules to stop the biggest and most complex banks from engaging in the risky activity of proprietary trading. The new rules would also give supervisors the power to require those banks to separate certain potentially risky trading activities from their deposit-taking business if the pursuit of such activities compromises financial stability. Alongside this proposal, the Commission has adopted accompanying measures aimed at increasing transparency of certain transactions in the shadow banking sector. These measures complement the overarching reforms already undertaken to strengthen the EU financial sector.

The proposal on structural reform of EU banks will apply only to the largest and most complex EU banks with significant trading activities.

It will:

- ban proprietary trading in financial instruments and commodities, i.e. trading on own account for the sole purpose of making profit for the bank;
- grant supervisors the power and, in certain instances, the obligation to require the transfer of other high-risk trading activities (such as market-making, complex derivatives and securitisation operations) to separate legal trading entities within the group (subsidiarisation). This aims to avoid the risk that banks would get around the ban on the prohibition of certain trading activities

by engaging in hidden proprietary trading activities which become too significant or highly leveraged and potentially put the whole bank and wider financial system at risk. Banks will have the possibility of not separating activities if they can show to the satisfaction of their supervisor that the risks generated are mitigated by other means; and
- provide rules on the economic, legal, governance, and operational links between the separated trading entity and the rest of the banking group.

To prevent banks from attempting to circumvent these rules by shifting parts of their activities to the less-regulated shadow banking sector, structural separation measures must be accompanied by provisions improving the transparency of shadow banking. The accompanying transparency proposal will therefore provide a set of measures aiming to enhance regulators' and investors' understanding of securities financing transactions (STFs).

Further information is available on the European Commission website.

1.10 SEC charges KPMG with violating auditor independence rules

On 24 January 2014, the US Securities and Exchange Commission (SEC) charged public accounting firm KPMG with violating rules that require auditors to remain independent from the public companies they are auditing to ensure they maintain their objectivity and impartiality.

The SEC issued a separate report about the scope of the independence rules, cautioning audit firms that they are not permitted to loan their staff to audit clients in a manner that results in the staff acting as employees of those companies.

An SEC investigation found that KPMG broke auditor independence rules by providing prohibited non-audit services such as bookkeeping and expert services to affiliates of companies whose books they were auditing. Some KPMG personnel also owned stock in companies or affiliates of companies that were KPMG audit clients, further violating auditor independence rules.

KPMG agreed to pay US$8.2 million to settle the SEC's charges.

According to the SEC's order instituting settled administrative proceedings, KPMG repeatedly represented in audit reports that it was "independent" despite providing services to three audit clients that impaired KPMG's independence. The violations occurred at various times from 2007 to 2011.

The report is available on the SEC website.

1.11 FRC seeks improvements in auditors' identification of a response to fraud risks, and consideration of laws and regulations

On 23 January 2014, the UK Financial Reporting Council (FRC) published a report of its Audit Quality Thematic Review into auditors' identification of and response to fraud risks, and their consideration of compliance with laws and regulations by audited entities.

The themes for the review, which looked at relevant aspects of 26 audits by the six largest audit firms, were chosen because they are matters of public interest where there are high expectations and common misunderstandings of the auditor's role. The report highlights a number of areas where auditors should improve the quality and effectiveness of their audit procedures and provides an overview of areas of good practice identified at one or more audit firms. These improvements would better position auditors to detect possible material misstatements in the financial statements due to fraud and non-compliance with laws and regulations. The extent to which improvements in these areas have been achieved will be assessed in the FRC's future inspections of individual firms.

Auditors are encouraged to increase their focus on identifying fraud risk factors when assessing the risks of the financial statements being materially misstated due to fraud. In particular, they should ensure their approach is tailored to the entity they are auditing. Auditors should also improve their identification and assessment of the laws and regulations affecting the specific audited entity, as well as exercising greater professional scepticism in relation to possible breaches that could affect the financial statements.

To assist Audit Committees, the report also identifies a number of areas in which their oversight of the audit process relating to fraud risks and laws and regulations might be enhanced. Further, when tendering their audit, Audit Committees are encouraged to enquire about the nature and frequency of the training firms provide on these areas to audit staff.

The report is available on the FRC website.

1.12 European Court of Justice rejects UK challenge to short-selling regulations

On 22 January 2014, the European Court of Justice (ECJ) dismissed the UK's challenge to the Short-Selling Regulation (SSR). The UK was challenging the power of ESMA to adopt emergency measures under the SSR, which in their view went against general EU principles. The ECJ rejected the plea finding that the SSR and the powers given to ESMA are compatible with EU law.

The court dismissed the UK's challenge on the following basis:

In 2012, the EU adopted a regulation aimed at harmonising short selling, against the background of the financial crisis. Short selling is a practice consisting in the sale of shares and securities not owned by the vendor at the time of the sale with a view to benefiting from a fall in the price of the shares and securities. In the event of disturbance on the financial markets, the regulation seeks, inter alia, to prevent an uncontrolled fall in the price of financial instruments as a result of the effect of short selling.

The regulation was adopted on the basis of Article 114 TFEU, which permits the adoption of harmonisation measures necessary for the establishment and functioning of the internal market. Article 28 of the regulation vests the European Securities and Markets Authority (ESMA) with certain powers of intervention. Accordingly, ESMA may adopt measures that are legally binding on the EU Member States' financial markets where there is a threat to the orderly functioning and integrity of financial markets or to the stability of the whole or part of the financial system in the EU.

In May 2012, the United Kingdom brought an action before the Court of Justice seeking annulment of Article 28 of the regulation. The United Kingdom contended, inter alia, that ESMA has been given a very large measure of discretion of a political nature which is at odds with EU principles relating to the delegation of powers. The United Kingdom also submitted that Article 114 TFEU is not the correct legal basis for the adoption of the rules laid down in Article 28 of the regulation.

In its judgment, the Court found, first, that Article 28 of the regulation does not confer any autonomous power on ESMA that goes beyond the powers granted to that authority when it was created. The Court also pointed out that the exercise of the powers laid down in that provision is circumscribed by various conditions and criteria which limit ESMA's discretion.

The full text of the judgment is available on the European Court of Justice website.

1.13 Recent trends in US securities class action litigation

On 21 January 2014, NERA Economic Consulting released a report on US securities class action litigation.

More securities class actions were filed in US federal court in 2013 compared to 2012 but the increase has been a small one, according to the report.

In 2013, 234 securities class actions were filed, compared to 213 class actions filed in 2012, representing a 10% increase and a slight increase compared to the 224 average number of filings in the period of 2008 to 2012.

Filings of securities class actions involving alleged violations of Rule 10b-5, s. 11, or s. 12, saw a 15% increase over 2012, thereby exceeding the filings in any year in the 2009 to 2012 period. Filings in the 5th Circuit alleging violation of Rule 10b-5 more than doubled in 2013 to 13, compared to six filings in 2012 and five in 2011.

The number of class actions settled in 2013 came close to the record low of 2012. Only 100 securities class actions were settled in 2013, compared to 94 settlements reached in 2012 and the 127 average settlements per year in the period of 1996 to 2011.

Average settlement amounts for "usual" securities class actions in 2013 broke prior records, reaching US$55 million, an increase of 53% over 2012 and a 31% increase over the previous high in 2009. (By "usual," is meant excluding settlements over US$1 billion, merge objection settlements, and IPO laddering settlements.) The median settlement amount for 2013 was US$9.1 million, a 26% decrease compared to 2012.

The report is available on the NERA website.

1.14 Cross-Border M&A: Annual review 2013

In January 2014, the International Institute for the Study of Cross-border Investment and M&A (XBMA) released its annual review. The report findings are outlined below.

(a) Global M&A volume: 1996-2013

While total global M&A volume has been relatively consistent over the last four years, hovering around US$ 2.5 trillion per annum, the deal activity making up the $2.5 trillion has varied considerably over this period, reflecting a few trends:

- private equity-backed M&A has been gaining steam steadily, growing from 6.3% of global M&A in 2009 to 15.6% of global M&A in 2013;
- growth of M&A involving emerging economies has outpaced their GDP growth, with Chinese domestic M&A showing increasing strength, but inbound and outbound M&A involving emerging economies ebbs and flows based on various exogenous factors;
- European M&A has been mixed over the last four years, exceeding US$200 billion only once since 2009, and ending 2013 down 16.5% from 2009 levels; and
- US share of global M&A continues to grow disproportionately as the recovery proceeds, on both the domestic and cross-border fronts.

(b) Cross-border M&A volume 2006-2013

- Cross-border M&A volume in 2013 was down 18% from 2012, marking its lowest level both in terms of absolute volume and as a percentage of overall volume since 2009, perhaps reflecting cooling markets in some emerging economies.
- Despite a strong fourth quarter, deals involving a developed - and emerging-market participant fell off in 2013. Notably, deal activity involving both a developed-market acquirer and an emerging-market target decreased for the third straight year.
- Cross-border M&A volume involving a Chinese target or acquirer declined in 2013, with Chinese inbound activity reaching its lowest level since 2009.

The full report is available on the XBMA website.

1.15 Book launch - The Protection of Employee Entitlements in Insolvency: An Australian Perspective

On 5 March 2014, Melbourne University Press will launch a new book authored by Melbourne Law School academic Associate Professor Helen Anderson titled "The Protection of Employee Entitlements in Insolvency: An Australian Perspective".

The book is the first detailed analysis of the law and policy dealing with employee entitlements such as wages, leave and redundancy payments that are threatened when companies fail. Although Australia has a government-funded safety-net scheme, currently known as the Fair Entitlements Guarantee, it does not cover all lost entitlements for all workers. Some argue that the scheme removes any incentive for companies to make adequate provision for their employees' entitlements, increasing the burden on the taxpayer.

As well as investigating ways to safeguard the entitlements of employees that are presently lost through the improper behaviour of directors, the book covers the history of Australia's present system and comprehensively sets out the avenues available to assist employees to recover their entitlements. It also canvases what might be done in the future to improve the protection of employee entitlements in Australia when companies become insolvent.

The publication is available in paperback and as an e-book. Further information is available on the Melbourne University Press website.

Details regarding the book launch are available on the Melbourne Law School website.

2. Recent ASIC Developments

2.1 ASIC information sheet on whistleblowers and whistleblower protection

On 18 February 2014, ASIC released information about its approach to dealing with whistleblower reports. The information sheet is part of ASIC's commitment to improve its communication and handling of information brought to its attention by whistleblowers. It explains:

- reporting important information to ASIC;
- how ASIC will communicate with whistleblowers;
- who is a whistleblower;
- the protections available to whistleblowers under the law; and
- how ASIC deals with information from whistleblowers.

ASIC has enhanced its approach to dealing with whistleblower reports. This includes:

- appropriate training and expertise in all stakeholder and enforcement teams for the handling of whistleblower reports
- a coordinated, centralised procedure for the tracking and monitoring of all whistleblower reports
- giving appropriate weight to the inside nature of the information provided by whistleblowers in ASIC's assessment and ongoing handling of the matter
- providing prompt, clear and regular communication to whistleblowers to the extent possible and appropriate during investigations; and
- maintaining the confidentiality of whistleblowers within the applicable legal framework.

The updated approach to whistleblowers extends to "insiders" who seek to provide information to ASIC but who are not defined in the legislation as corporate whistleblowers (e.g. because they are no longer an employee of the company involved at the time they make the disclosure or because they do so anonymously).

ASIC made a submission to the Senate Inquiry on its approach to dealing with whistleblower reports in 2013. This submission is available on the ASIC website.

The whistleblower information sheet is available on the ASIC website.

2.2 ASIC extends shorter PDS regime

On 10 February 2014, ASIC extended interim class order relief from the shorter Product Disclosure Statement (PDS) regime for multi-funds, superannuation platforms and hedge funds.

Class Order [CO 14/23] extends the relief in Class Order [CO 12/749] Relief from the Shorter PDS regime for a further 12 months, to 30 June 2015. The relief was due to expire on 22 June 2014.

The full PDS requirements under the Corporations Act 2001 (Cth) apply to products that have been excluded from the shorter PDS regime.

ASIC has extended the relief pending a future Australian Government decision on the application of the shorter PDS regime to superannuation platforms, multi-funds and hedge funds.

Background

ASIC issued guidance to assist issuers of superannuation products and simple managed investment schemes to comply with the shorter PDS regime in June 2012 (12-131MR). The shorter PDS regime started on 22 June 2012.

Class Order [CO 12/749] excludes:

- superannuation platforms from the shorter PDS regime. However, superannuation platforms may elect to be included in the shorter PDS regime;
- multi-funds from the shorter PDS regime. However, multi-funds may elect to be included in the shorter PDS regime; and
- hedge funds from the shorter PDS regime.

Further information is available from the ASIC website.

2.3 ASIC updates hybrid information for investors

On 4 February 2014, ASIC updated information on its consumer finance website, MoneySmart, to help investors understand the risks and complexities of hybrid securities.

ASIC also developed a quiz for investors to help them comprehend the terms of these offers and encourage them to be fully informed before they invest.

ASIC's focus on these complex products follow a rise in their popularity - in the 18 months to July last year, around $18 billion was raised through ASX-listed hybrid securities.

Using everyday language, the updated information on ASIC's MoneySmart:

- explains the differences between hybrids issued by banks and hybrids offered by other companies;
- highlights the features and risks of these securities and includes information on the new 'non-viability' clauses found in recent bank hybrids;
- compares the typical features of two forms of hybrid security - a capital note issued by a bank and a subordinated note issued by a company - to shares, corporate bonds and bank term deposits, to identify the additional risks investors may be taking on; and
- breaks down the common terms found in hybrid prospectuses, so readers can understand what 'interest deferral' or 'loss absorption' could really mean for them. Case studies are used to demonstrate how these terms operate in practice.

Further information is available on ASIC's MoneySmart website.

2.4 ASIC releases report on regulating complex products

On 31 January 2014, ASIC published Report 384 Regulating complex products (REP 384) following the review of its approach to regulating complex products.

REP 384:

- outlines the risks posed by complex products to retail investors;
- sets out ASIC's recent and current work on complex products, including considering the whole of the product lifecycle - development, distribution, sale, and post-sale; and
- identifies opportunities for further work, including working with industry, where appropriate.

The report is available on the ASIC website.

2.5 ASIC enforcement report - July to December 2013

On 31 January 2014, ASIC released its fifth six-monthly enforcement report, detailing outcomes achieved between 1 July 2013 and 31 December 2013.

ASIC achieved 340 enforcement outcomes. This included criminal as well as civil and administrative (e.g. a banning or disqualification) actions, and negotiated outcomes, including enforceable undertakings.

There were 112 outcomes achieved in the market integrity, corporate governance and financial services areas, and 228 in the small business area.

Current areas of focus for ASIC include a focus on misleading advertising of products and services, market misconduct, including insider trading, and the responsibility of gatekeepers.

The report is available on the ASIC website.

2.6 ASIC reports on relief applications - June to September 2013

On 28 January 2014, ASIC released its latest report outlining decisions on relief applications covering the period 1 June to 30 September 2013.

Businesses frequently approach ASIC for assistance to help make the law work better for them. ASIC uses its discretion to vary or set aside certain requirements of the law where there is a net regulatory benefit or where ASIC can facilitate business or cut red tape without harming other stakeholders.

This is a key part of ASIC's function and between 1 June and 30 September 2013, ASIC approved 303 relief applications.

Report 382 Overview of decisions on relief applications (June to September 2013) (REP 382), aims to improve the level of transparency and the quality of publicly available information about decisions ASIC makes when asked to exercise its discretionary powers to grant relief from provisions of the:

- Corporations Act 2001 (Cth) (the Corporations Act);
- National Consumer Credit Protection Act 2009 (Cth) (the National Credit Act); or
- National Consumer Credit Protection (Transitional and Consequential Provisions) Act 2009 (the Transitional Act).

REP 382 also discusses the various relevant publications released by ASIC during the three months.

The report summarises examples of situations where ASIC has exercised, or refused to exercise, its exemption and modification powers under the Corporations Act and the licensing and responsible lending provisions of the National Credit Act. The report also highlights instances where ASIC has considered adopting a no-action position regarding specified non-compliance with statutory provisions.

Finally, the report provides examples of decisions that demonstrate how ASIC has applied its policy in practice which ASIC thinks will be of particular interest for capital market participants and for participants in the financial services industry. The report includes an appendix detailing the relief instruments referred to in the report.

ASIC can modify or set aside certain provisions of Chapters 2D (officers and employees), 2J (share buy-backs), 2L (debentures), 2M (financial reporting and audit), 5C (managed investment schemes), 6 (takeovers), 6A (compulsory acquisitions and buy-outs), 6C (information about ownership of entities), 6D (fundraising) and 7 (financial services) of the Corporations Act.

ASIC also has powers to grant relief under the National Credit Act from the licensing provisions in Chapter 2 and the responsible lending conduct provisions in Chapter 3. ASIC has powers to give relief from the registration provisions in Schedule 2 of the Transitional Act.

The report is available on the ASIC website.

3. Recent ASX Developments

3.1 ASX to launch a new managed fund service

On 6 February 2014, ASX announced that it has received regulatory clearance to launch its new managed funds settlement solution - mFund Settlement Service. It will be launched in the first half of 2014 following the completion of customer connectivity.

mFund has been developed for investors, brokers and fund managers to improve the timeliness and reduce the costs associated with investing in managed funds. The service will replace the traditional paper-based processes and use the same electronic system (CHESS) familiar to investors and brokers for settling - or finalising - ASX share transactions.

mFund is an electronic processing service that allows investors to use an ASX broker when they buy and sell units in unlisted managed funds. CHESS will automate and track the process of these transactions and remove much of the paperwork.

Through the use of ASX's CHESS infrastructure, investors will receive a consolidated report that summarises all of their holdings in shares, other products such as Australian Government bonds and ETFs, and managed funds purchased using the mFund service. A broad range of unlisted managed funds (mFund products) will be admitted to ASX.

mFund products are unlisted and not traded between investors on the market, but will be settled directly with fund managers via CHESS. Unit prices are set by the fund manager, usually at the end-of-the-day.

The media release is available on the ASX website.

For more information on mFund, see the mFund page on the ASX website.

3.2 Clearing and Settlement Services for Approved Market Operators and Approved Listing Market Operators: Enhanced service levels and information handling standards

On 23 January 2014, ASX released a consultation paper entitled "Clearing and Settlement Services for Approved Market Operators and Approved Listing Market Operators: Enhanced service levels and information handling standards". In the consultation paper, ASX proposes to enhance its service level commitments and operational and technical standards for the Trade Acceptance Service and the Settlement Facilitation Service. ASX also proposes to update the information handling standards applicable to the provision of these services.

The consultation paper is available on the ASX website.

3.3 Reports

On 5 February 2014 ASX released:

- the ASX Group Monthly Activity Report;
- the ASX 24 Monthly Volume and Open Interest Report; and
- the ASX Compliance Monthly Activity Report

for January 2014.

4. Recent Takeovers Panel Developments

4.1 Agricultural Land Trust - Panel declines to conduct proceedings

On 31 January 2014, the Takeovers Panel announced that it had declined to conduct proceedings on an application dated 24 January 2014 from Ann Cathcart Pty Ltd in relation to the affairs of Agricultural Land Trust.

The application concerned the members' meeting of the Trust scheduled for 31 January 2014 to approve a proposed restructure of the Trust, and whether Emerald Securities Pty Ltd (the holder of 4.4% of the Trust) and Mr Allen Caratti were associated so that Emerald Securities should be excluded from voting on resolutions to be put at that meeting.

The Panel decided that there was no reasonable prospect that it would make a declaration of unacceptable circumstances because, among other things:

- the material put forward to support the allegation of association was equivocal or problematic;
- a considerable time has elapsed since concerns about association were first raised and it is unclear what other evidence could be adduced; and
- the Panel was informed that if the meeting was delayed, the Trust may suffer prejudice as a result of its financing arrangements.

The reasons for the decision are available on the Takeovers Panel website.

4.2 Dragon Mining Limited - Panel declines to conduct proceedings

On 7 February 2014, the Takeovers Panel announced that it had declined to conduct proceedings on an application dated 2 February 2014 from Dragon Mining Limited in relation to its affairs.

On 9 December 2013, Dragon Mining received a notice from Eurogold requisitioning a meeting to remove the majority of directors of Dragon Mining and appoint Mr Arthur Dew and Mr Brett Smith as directors. The meeting was scheduled for 7 February 2014. Eurogold has a 24% interest in Dragon Mining. Allied Properties Resources Limited has a 36% interest in Eurogold.

Allied Properties is controlled by Allied Group Limited, which is controlled by the Lee family. Between December 2012 and June 2013, COL Capital Limited acquired a 12% interest in Dragon Mining. Ms Chong ultimately holds a 72% interest in COL Capital.
Dragon Mining submitted, among other things, that Ms Chong and the Lee family (and their related entities) were associates and the shares acquired by COL Capital were in breach of the takeovers prohibition.

The Panel considered that there was not a sufficient body of evidence to justify the Panel making further enquiries. The Panel also considered that, in the circumstances, the application was not timely.

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 reasons for the decision are available on the Takeovers Panel website.

5. Recent Research Papers

5.1 The returns to hedge fund activism: An international study

This paper examines almost 1800 cases of shareholder activism across three regions, Asia, Europe and North America. The authors measure the block disclosure returns to activist announcements and to subsequent outcomes of the engagement, including changes to payout, boards, takeovers and other corporate restructurings. They compare the profitability of engagements with and without outcomes. There are large abnormal returns to shareholder activism at the block disclosure announcement of between 4.5 and 7.5% across the three continents. There are also large additional abnormal returns to the disclosure of outcomes from engagements, totalling 9.3% in Europe, and 6.6% in North America. The returns for Asia are much lower at 3%. Asia also has the lowest number of outcomes per engagement, with payout being the most common type. During the financial crisis activist returns declined significantly, primarily as a result of the lack of outcomes, particularly for takeovers. Overall, the paper shows that abnormal returns over the entire period of the engagement are significantly higher for engagements with outcomes compared with those without outcomes. These results suggest that the profitability of activism is based primarily on engagement with the target firm to achieve change rather than on "stock picking."

The paper is available on the SSRN website.

5.2 SOX after ten years: A multidisciplinary review

The authors review and assess research findings from 120 papers in accounting, finance, and law to evaluate the impact of the US Sarbanes-Oxley Act. They describe significant developments in how the Act was implemented and find that despite severe criticism, the Act and institutions it created have survived almost intact since enactment. They report survey findings from informed parties that suggest that the Act has produced financial reporting benefits. While the direct costs of the Act were substantial and fell disproportionately on smaller companies, costs have fallen over time and in response to changes in its implementation. Research about indirect costs such as loss of risk taking in the US is inconclusive. The evidence for and social welfare implications of claimed effects such as fewer IPOs or loss of foreign listings are unclear. Financial reporting quality appears to have gone up after SOX but research on causal attribution is weak. On balance, research on the Act's net social welfare remains inconclusive. The authors end by outlining challenges facing research in this area, and propose an agenda for better modelling costs and benefits of financial regulation.

The paper is available on the SSRN website.

5.3 Does board independence reduce the cost of debt?

Using the passage of the Sarbanes-Oxley Act and the associated change in listing standards as a natural experiment, the authors find that while board independence decreases the cost of debt when credit conditions are strong or leverage low, it increases the cost of debt when credit conditions are poor or leverage high. They also document that independent directors set corporate policies that increase firm risk. These results suggest that, acting in the interest of shareholders, independent directors are increasingly costly to bondholders with the intensification of the agency conflict between these two stakeholders.

The paper is available on the SSRN website.

5.4 Creating a culture of compliance: Why departmentalism may not be the answer

Over the past few decades, as corporate criminal liability rules, sentencing guidelines, and settlement incentives have changed, there has been increased emphasis on and resources devoted to the compliance function at large publicly held companies. In this article, the author traces the development of the compliance function at large corporations and questions the recent mandate by certain governmental entities that malfeasant corporations designate a chief compliance officer and separate the compliance gatekeeping function from the legal department so that this chief compliance officer does not report to the general counsel.

The author categorises the types of arguments made for and against departmentalisation and then analyses them from the perspective of the public's objectives to increase detection, monitoring, and prevention of corporate misconduct. By examining secondary literature, surveys, and interviews conducted with 70 general counsels and chief compliance officers, the author hypothesises that pre-emptive departmentalisation may not be in the public's best interest. It may not increase transparency into compliance transgressions at corporations, actual compliance by corporations, or the commitment by corporations to a culture of compliance and ethics. Further, such structural reorganisation of the compliance function may generate consequences that offset the potential benefits of departmentalisation and create a sense of false complacency that distracts from substantive cultural change that is integrated throughout the organisation .

Ultimately, the author concludes that a focus on culture and informal norms may have more potential to meet the public's objectives than a focus on organisational structure. Therefore, the author proposes the government revise its current focus on the external manifestations of compliance to inward, cultural change. Specifically, the government reward corporations that take an inward look at how work is actually being done within the company and at the networks and organisational culture that exists beneath the surface of the organisation chart, the mission statement, and code of conduct. Such focus could enable compliance structures and programs that promote public access to information about compliance transgressions, actual compliance by corporations, and a culture of compliance and ethics within a corporation.

The paper is available on the SSRN website.

5.5 Human rights meets securities regulation

Recent domestic legislation is blurring the line between securities regulation and human rights law. Securities law has traditionally regulated corporate disclosure on financial information, such as income statements and investment risks. By contrast, human rights law has traditionally operated in the international sphere and focused on state obligations.

That all changed in 2010 with the adoption of the Dodd-Frank Wall Street Reform and Consumer Protection Act, which includes ss. 1502 and 1504 on non-financial disclosure related to human rights and anti-corruption. In particular, s. 1502 is the first regulation to create binding rules on due diligence with regard to a company's supply chain. It imposes a new reporting requirement on publicly traded companies that manufacture products using certain conflict minerals. Companies must identify whether the sourcing of the minerals originated in the Democratic Republic of Congo (DRC) and bordering countries. If so, they must submit an independent private sector audit report on due diligence measures taken to determine whether those conflict minerals directly or indirectly financed or benefited armed groups in the covered countries.

The Dodd-Frank provisions are but one example of an emerging trend in international securities law. Over the past decade, an increasing number of governments and securities exchanges have passed mandatory regulations on corporate disclosure of social issues. In this Article, the author analyses a critical question: Is securities regulation the appropriate mechanism for achieving human rights compliance? By doing so, the author seeks to open a dialogue between two disparate streams of scholarship in private and public law and propose policy recommendations for effectively furthering the movement towards corporate accountability. While existing literature on ss. 1502 and 1504 addresses the history of the legislation and critiques its efficacy, the main contribution of the article is to analyse the normative implications of the broader strategy of using securities regulation to hold companies accountable for human rights abuses.

The paper is available on the SSRN website.

5.6 Challenges in global financial services

This is an edited transcript of the proceedings of the Yale Law School Conference on Challenges in Global Financial Services. The conference brought together policymakers, legal practitioners, members of the financial community, and academics from finance, economics and law to discuss the current challenges in the organisation and regulation of global financial services. The roundtable consisted of four panel discussions. The first panel considered "Bank Capital and Liquidity Requirements". The second panel addressed "Bank Transparency and the Financial Crisis". The third panel focused on the "Accountability and Structuring of Systemically Important Financial Institutions (SIFIs)". The fourth panel considered "Cross-Border Resolution".

The transcript is available on the SSRN website.

6. Recent Corporate Law Decisions

6.1 Credit card late payment bank fees found to be unenforceable penalties

(By Emma Newnham, King & Wood Mallesons)

Paciocco v Australia and New Zealand Banking Group Limited [2014] FCA 35, Federal Court of Australia, Gordon J, 5 February 2014

The full text of this judgment is available online.

(a) Summary

The key issue in this case was whether bank fees charged by Australia and New Zealand Banking Group Limited (ANZ) were penalties or otherwise unconscionable, unjust or unfair under relevant legislation.

Gordon J found that late payment fees charged to Mr Paciocco's consumer credit cards constituted penalties at common law and in equity and were therefore unenforceable. Her Honour found that the quantum of the credit card late payment fee was extravagant and unconscionable in amount and that the estimated damage suffered by

ANZ in respect of each fee charged was between $0.50 and $5.50, in contrast to the fees of $20 or $35 charged by ANZ.

Her Honour found that honour fees, dishonour fees, non-payment fees and over limit fees did not constitute penalties nor did they contravene the relevant statutory unconscionable conduct provisions.

(b) Facts

Mr Paciocco and his company Speedy Development Group Pty Ltd (SDG) held accounts with ANZ. The terms of these various accounts allowed ANZ to charge late payment fees, honour fees, dishonour fees, non-payment fees, and over limit fees.

Mr Paciocco and SDG alleged that these terms constituted penalties at common law and in equity.

It was further contended that, if these were not penalties:

- ANZ had engaged in unconscionable conduct by including the terms and giving effect to them;
- the consumer credit accounts were unjust under the National Credit Code; and
- the terms in the consumer deposit account and consumer credit card accounts were unfair contract terms.

(c) Earlier proceedings

A representative action was commenced in 2010 against ANZ by some of its customers in respect of various fees charged by ANZ.

It was alleged in that proceeding that the fees payable by customers were void or unenforceable as penalties. At first instance, Gordon J held that the majority of the fees could not constitute penalties as they were not payable on breach of contract. The exception was the credit card late payment fees, which were capable of being penalties.

The question went to the High Court for consideration and, in September 2012, the High Court overturned previous case law to find that the law of penalties is not confined to payments imposed upon breach of contract (*Andrew v Australia and New Zealand Banking Group Ltd* [2012] HCA 30 (*Andrew v ANZ*)). The Court found that a penalty can also arise in respect of fees payable to secure an obligation or performance of a party.

In 2013, the further representative action addressed in this case note was brought against ANZ to determine the position following the High Court's decision.

(d) Decision

Gordon J set out certain tests that may be used when considering a penalty at common law and in equity.

This involves identifying whether a stipulation is:

- payable on breach of a term of the contract ("a necessary element at law but not in equity"). This involves considering whether the term is security for, and *in terrorem* of, the satisfaction of the term; or
- collateral to a primary stipulation in favour of one contracting party and the collateral stipulation, upon failure of the primary stipulation, imposes on the other contracting party an additional detriment (the penalty) in the nature of a security for, and *in terrorem* of, the satisfaction of the primary stipulation.

If the answer to either of these questions is yes, it is necessary to consider whether the sum stipulated is a genuine pre-estimate of damage or rather an extravagant (or exorbitant) and unconscionable amount in comparison with the greatest loss that could conceivably be proved. If the latter, the stipulation is unenforceable to the extent the stipulation exceeds that amount.

(i) Credit card late payment fees

ANZ contended that the late payment fees were not payable on breach but were rather fees charged by ANZ as part of operating the account.

These fees were argued to be in respect of:

- a further period of credit necessarily extended by the bank to a customer because of the absence of timely payment; and
- the increased risk of default in repayment of the sum borrowed.

Gordon J considered the stipulation in the letter of offer and conditions of use which required Mr Paciocco to pay an amount by the due date. The late payment fee was payable if this stipulation was not complied with. A plain reading of these terms led to the conclusion that the liability to pay the late payment fee was contingent upon breach of a contractual obligation by the customer.

Even if the late payment fee was not payable upon breach, Gordon J found that the stipulation in the relevant contracts with ANZ obliged Mr Paciocco to pay a sum by a certain time each month and that the late payment fee would be charged if the amount was not paid within the specified time. The payment of the late payment fee constituted a stipulation that was collateral to the primary stipulation in favour of ANZ that Mr Paciocco make a minimum monthly payment by the due date. Her Honour concluded that the collateral stipulation was, at law and in equity, to be viewed as security for, or *in terrorem* of, the satisfaction of the primary stipulation.

Further, her Honour found that the quantum of the late payment fees was extravagant and unconscionable relative to the loss actually incurred by ANZ in breach of this obligation. In this regard, her Honour relied on expert evidence adduced by Mr Paciocco and made findings that the loss and damage caused to ANZ in relation to each fee was between $0.50 and $5.50. This could be contrasted with the $20 to $35 charged by ANZ.

Accordingly, Mr Paciocco was entitled to receive the difference between the late payment fee charged and the finding of loss and damage caused to ANZ, adjusted for interest.

(ii) Other exception fees

The honour fees, dishonour fees, over limit fees and non-payment fees were not found to be penalties. These fees were properly viewed as arising from withdrawal or payment instructions given by a customer that would have the effect of overdrawing the customer's account or exceeding the account credit limit. They could be construed as a request from the customer for an advance or loan from ANZ, which ANZ could approve or decline at its discretion.

Consistent with that reasoning, Gordon J found that these fees did not involve breaches of contract. Nor was the liability to pay these fees collateral to a primary stipulation in favour of ANZ. The liability to pay the fee arose as a result of something additional to and different from the primary stipulation in favour of ANZ.

Further, none of the terms that entitled ANZ to charge these fees were found to contravene the statutory provisions raised.

(iii) Unconscionable conduct

Mr Paciocco and SDG contended that ANZ engaged in unconscionable conduct in respect of the honour fees, dishonour fees and over limit fees in contravention of the Australian Securities and Investments Commission Act 2001 (Cth), the *Fair Trading Act 1999 (Vic)* (now contained in the Australian Consumer Law found in Schedule 2 to the Competition and Consumer Act 2010 (Cth)) and the ASIC consolidated regime.

Mr Paciocco and SDG argued there were a number of matters that informed the "unconscionable" conduct by ANZ, including that ANZ had all or most of the bargaining power in the relationship and provided standard form contracts on a take it or leave it basis.

Gordon J rejected this contention. Her Honour noted the absence of dishonesty, oppression or abuse of a commercially powerful position or failure to disclose the terms of the relevant fees on entry by Mr Paciocco and SDG into the contracts. Her Honour also noted there was no allegation Mr Paciocco and SDG were unable to understand the terms of the relevant fees, nor any pressure on them to enter into the contracts or engage in the overdraw transactions.

(iv) Limitations

Another issue was whether ANZ could rely on limitation defences in respect of some of Mr Paciocco's penalty claims. The Limitation of Actions Act 1958 (Vic) (the Act) provides a six-year limitation period for actions founded on simple contract.

Mr Paciocco sought to rely on s. 27 of the Act, which extends limitation periods in cases of mistake. Under s. 27 of the Act, time does not begin to run until the plaintiff has discovered the mistake or could with reasonable diligence have discovered it. Mr Paciocco argued that until the High Court decision in *Andrew v ANZ* he believed ANZ was entitled to charge the exception fees and that he was obliged to pay the fees.

Gordon J accepted that s. 27 extended to Mr Paciocco's mistake of law. Accordingly, time did not begin to run until the proceedings in *Andrew v ANZ* commenced in 2010 and Mr Paciocco's claims were not statute-barred.

6.2 Liquidating trust assets without power of sale: The court's discretion to excuse

(By Edward Kus, DLA Piper)

Theobold in the matter of Finplas Pty Ltd [2014] FCA 31, Federal Court of Australia, Siopis J, 4 February 2014

The full text of this judgment is available online.

(a) Summary

This case considered the ability of the court to retrospectively empower the liquidators of a company to sell trust assets pursuant to s. 89 of the Trustees Act 1962 (WA) (the Trustees Act) in circumstances where the liquidators would otherwise be acting without power.

The case also considered the appropriateness of excusing the liquidators for any breaches, failures or omissions arising from their conduct pursuant to s. 1318 of the Corporations Act 2001 (Cth) (the Corporations Act) and s. 75 of the Trustees Act.

Siopis J concluded that, in the circumstances, the court should retrospectively empower the liquidators to sell trust assets in accordance with s. 89 of the Trustees

Act and that the conduct should be excused in accordance with s. 75 of the Trustees Act. However, Siopis J refused to excuse the conduct in accordance with s. 1318 of the Corporations Act.

This case follows the trend established in two similar cases which considered the ability to retrospectively empower a trustee to sell trust property, namely:

- *Re Pleash, in the matter of Suncoast Restoration Pty Ltd* [2013] FCA 355 (which considered s. 94 of the Trusts Act 1973 (Qld)) (*Suncoast*); and
- *Caterpillar Financial Australia Ltd v Ovens Nominees Pty Ltd* [2011] FCA 677 (which considered s. 63 of the Trustee Act 1958 (Vic)) (*Caterpillar*).

(b) Facts

Finplas Pty Ltd (in liquidation) (Finplas) as trustee of the Finplas Trading Trust (the Trust) carried on the business of plastics manufacture. The directors and shareholders of Finplas were also the beneficiaries of the Trust. The premises at which Finplas carried on its business (the Premises) was owned by Finira Pty Ltd (Finira). The directors and shareholders of Finira and Finplas were largely the same.

Finplas ceased to pay rent on a regular basis in relation to the Premises and built up a substantial liability to Finira, which was recorded in the books and records of Finira as an intercompany loan of approximately $2.46 million (Intercompany Loan).

Pursuant to a petition made by the Australian Taxation Office (ATO) to the Court, the Court made a winding up order in respect of Finira and appointed Mr Jeffrey Herbert as liquidator of Finira. Mr Herbert was assisted by Mr Simon Guy Theobald and other members of staff employed at the firm at which Mr Herbert was partner.

On 4 February 2013, Finira served a statutory demand on Finplas in respect of the outstanding balance of the Intercompany Loan.

On 15 March, Mr Herbert and Mr Theobald were appointed as joint and several liquidators of Finplas (in liquidation) by resolution of the shareholders of Finplas in a general meeting. Mr Theobald arranged for Grays Auctioneers to catalogue the plant and equipment owned by Finplas which was located at the Premises. Mr Theobald subsequently instructed Gray Auctioneers to sell the plant and equipment (which it did for a substantially higher sum than it valued).

On 25 March 2013, the liquidators received for the first time a copy of the Trust deed (the Deed). It was subsequently found that clause 16.3 of the Deed operated to remove Finplas as trustee of the Trust in the event Finplas went into liquidation. This effectively meant that Mr Herbert and Mr Theobald (as the liquidators of Finplas) did not have the power to dispose of the trust assets, as following its removal, Finplas was acting as a bare trustee. It is worth noting, however, that despite being a bare trustee, Finplas (and by implication the liquidators) continued to benefit from its right of indemnity and/or exoneration in respect of liabilities it incurred in conducting the trust business.

The liquidators sought an order under s. 89 of the Trustees Act, which empowers the court to, where it is expedient to do so, confer any necessary power on a trustee where the trustee would otherwise not have the power.

The liquidators also sought relief under either or both of s. 1318 of the Corporations Act and s. 75 of the Trustees Act, which allow the court to relieve a person of liability in respect of negligence, default or breach where the person has acted honestly and ought fairly be excused.

(c) Decision

(i) Relief under section 89 of the Trustees Act

Siopis J held that the relief sought under s. 89 of the Trustees Act should be granted and that the liquidators should retrospectively be empowered to sell the trust assets. In doing so, Siopis J made reference to the *Suncoast* and *Caterpillar* decisions, both of which related to similar circumstances. Importantly, Siopis J recognised that in this case, as was the situation in the *Suncoast* and *Caterpillar* decisions, the appointor under the trust deed had declined to appoint a trustee to replace the removed trustee. As a result, he found that the sale of the trust assets was "expedient in the administration of the property vested in Finplas" and that the "assistance of the Court is necessary to effect the disposition of the property".

(ii) Relief under section 1318 of the Corporations Act

Siopis J declined to relieve the liquidators under s. 1318 of the Corporations Act. This section of the Corporations Act requires the liquidators to "have reason to apprehend that any claim" arising from the sale of the trust property "will or might be made" against them before the court is empowered to grant relief. In interpreting this provision, Siopis J relied on the comments of Reeves J in the *Suncoast* decision, who observed that the words "have reason to apprehend" imported a "requirement for an objective basis for the apprehension". Furthermore, the term "might" in the context required "a real, not fanciful or remote possibility".

Four reasons were given by Siopis J as to why the liquidators failed the "real, not fanciful or remote possibility" test:

- the beneficiaries under the Trust were also the shareholders who appointed the liquidators. As such, the liquidators were giving effect to the beneficiaries and shareholders' purposes in appointing the liquidators;
- Finplas was "hopelessly insolvent". Accordingly, there was no incentive for the beneficiaries of the Trust to bring an action to recover the losses;

- the creditors were unlikely to bring an action against the liquidators because the liquidators had provided a benefit to the creditors in the form of greater proceeds upon the sale of the assets than was anticipated. Furthermore, there was no indication that the larger creditors of Finplas (Finira and the ATO) were considering bringing litigation against Finira; and
- ASIC did not appear to oppose the relief sought by the liquidators on the basis that ASIC was served with the liquidators' court application and chose not to appear.

(iii) Relief under section 75 of the Trustees Act

Finally, with respect to s. 75 of the Trustees Act, Siopis J granted the liquidators' requested declaration of relief. Despite the similarity between this section and s. 1318 of the Corporations Act, this section did not require the liquidators to have an apprehension that an action would be brought before the court was empowered to grant relief. As such, Siopis J was satisfied with the liquidators' evidence that they "genuinely and honestly believed that as liquidator of Finplas, [they] had the power to realise the trust assets in the liquidation of Finplas". Mr Theobold also confirmed in evidence that "had he been aware of the [relevant clause in] the trust deed [he] would not have proceeded with the sale in the manner which he did".

6.3 Court finds that inventors are not de facto director and therefore have not breached their fiduciary duties by registering patents in the name of another company

(By Clementyne Rawlyk and Erica Chan, Corrs Chambers Westgarth)

Elsworth Ethanol Company Ltd v Hartley [2014] EWHC 99 (IPEC), High Court of Justice of England and Wales (Intellectual Property Enterprise Court), Hacon J, 3 February 2014

The full text of this judgment is available online.

(a) Summary

This case considers the circumstances in which an individual may be considered to be a *de facto* director of a company. The High Court of Justice of England and Wales has rejected a claim by Elsworth Ethanol Company Ltd (the 2002 Company) that ownership of a series of patents and patent applications should be transferred because they were supposed to be filed in its name and not in the name of Bioconversion Technologies Limited (BCTL). The primary basis for this claim was that the inventors of the patents were *de facto* directors of the 2002 Company and accordingly breached their fiduciary duty by applying for the patents in the name of BCTL.

Hacon J dismissed the claim, finding that there was no clear evidence that the inventors were *de facto* directors of the 2002 Company. In any event, Hacon J held that even if the inventors were considered to be *de facto* directors, only one of them could have been in breach of their fiduciary duties, and the circumstances of the case did not support this finding.

(b) Facts

On 5 March 2006, the managing director of the 2002 Company, Mr Bookless, met with the first three defendants to discuss the development of three new ideas for enhanced bio-ethanol technology. The parties decided at the meeting that a firm of patent agents should be instructed to prepare patent applications in relation to the projects. The minutes of meeting show that the parties agreed to assign the patent applications to "EECO", the then current name of the 2002 Company. However, the same minutes also show in a later section that the parties contemplated using Environment Ethanol Company Ltd (the 2005 Company) to develop the projects. The 2005 Company was a dormant company registered by Mr Bookless. The minutes suggest that all agreed that the 2005 Company would be a suitable corporate vehicle for this purpose. The parties also agreed to rename the 2005 Company "Elsworth Ethanol Company". Importantly for the case, the minutes did not indicate that the parties discussed the precise role of the 2005 Company, its ownership or its directors. Nor was there any final decision made as to the corporate vehicle to be used for the proposed projects.

After 11 March 2006, amended drafts of two of the patent applications were circulated from time to time showing "Elsworth Ethanol Company Limited" as the proposed applicant, which at that time was the proposed name of the 2005 Company.

On 24 March 2006, the parties provided two patent application drafts to the patent attorney firm Reddie & Grose. When asked which entity should be named as the applicant, one of the defendants stated that it should be BCTL. Mr Bookless gave evidence that he was surprised by this suggestion but did not object at the time. The patent applications were thus filed in the name of BCTL.

On 17 May 2006, Mr Bookless changed the name of the 2002 Company to "Elsworth Ethanol Company Limited" which, as noted above, the parties agreed would be the new name of the 2005 Company. On the same day Mr Bookless also changed the name of the 2005 Company to "EECO Limited". None of the defendants were aware of these changes. A couple of weeks later, Mr Bookless wrote to all three defendants terminating their posts as Senior Scientific Advisor, Director of Science and Director of Research & Development respectively of Elsworth Ethanol Company Limited (i.e. the 2002 Company). The defendants responded to Mr Bookless in a letter stating that they were not aware of being officially appointed as directors and "fully understand why you wish to sack us if that was the case".

In May 2007, Mr Bookless wrote to the defendants expressly challenging BCTL's ownership of the two patent applications filed in BCTL's name. The basis for Mr Bookless's claim was that the defendants were *de facto* directors of the 2002 Company and therefore breached their fiduciary duty by applying for the patents in the name of BCTL. Mr Bookless argued that the defendants were *de facto* directors because, amongst other things they participated in several board meetings of the 2002 Company, signed several of those minutes as "Chairman", and distributed business cards to third parties bearing various "director" titles and the names "Elsworth Ethanol Company" and "EECO".

(c) Decision

Hacon J held that there is no single test for determining whether a *de facto* directorship exists. Rather, the court must take into account all relevant factors.

In this case, Hacon J held that the relevant factors were:

- whether there was clear evidence that the defendants were acting on an equal footing with Mr Bookless (who was a true director) in directing the 2002 Company's affairs;
- whether the 2002 Company publicly held out the defendants as directors; and
- taking all the circumstances into account, whether the defendants were part of the corporate governing structure of the 2002 Company.

Hacon J dismissed the claim on the basis that the overall evidence did not support a finding that the defendants were *de facto* directors of the 2002 Company. In this regard, Hacon J determined that the defendants did not act on an equal footing with Mr Bookless in directing the 2002 Company's corporate affairs. This was because Mr Bookless clearly believed that he alone controlled the 2002 Company. For example, he unilaterally changed the name of the 2002 Company without notifying the defendants and he fired the defendants at will in a letter. The defendants' acceptance of their termination by letter indicated that they also held this view.

Hacon J also determined that the defendants were not represented to the public as being directors of the 2002 Company. In this regard, Hacon J found no evidence that the titles given to the defendants on the business cards (namely Director of Science and Director of Research & Development) were representations that the defendants were directors of either the 2002 or 2005 Companies. Rather, Hacon J found it more likely that these titles were intended to, and were taken to be, job titles and nothing more. In any event, there was no evidence put forward that the recipients of the business cards paid any attention to the titles or the companies that were written on them.

Finally, Hacon J found no evidence that the defendants were part of the corporate governing structure of the 2002 Company. This is because the "board meetings" in which the defendants allegedly took part were not true board meetings at all. This is firstly because the name of the company in the minutes was not often clearly identified, and even when it was identified as being "Elsworth Ethanol Company", the defendants had no reason to attach this name to the 2002 Company. Secondly, Hacon J contended that because the sole focus of those meetings was to discuss the progress of the projects, they were more akin to project meetings than board meetings. Importantly, Hacon J noted that this position may have been different had the parties been clear from the start which company would be used to carry the projects forward. However, this debate was never resolved.

Hacon J also rejected the claimant's argument that by signing several minutes as "Chairman of the Board", one of the defendants was involved in the governance of the 2002 Company. Hacon J found that the defendant himself was unlikely to have attached any significance to this title and in any event never circulated the minutes publicly so as to be considered as holding himself out as Chairman of the 2002 Company. Even if the bio-ethanol projects had unequivocally been the business of the 2002 Company, Hacon J found that the contributions of the defendants were more consistent with the acts of consultants than the acts of directing the company.

Finally, Hacon J concluded that even if the defendants were de facto directors of the 2002 Company, none of them breached their fiduciary duty in the circumstances primarily because they did not have sufficient knowledge of patent law to realise that applying for the patents in BCTL's name was contrary to the interests of the 2002 Company. Similarly, there was insufficient evidence to show that the defendant who had put forward BCTL's name as the applicant of the patents had deliberately and dishonestly breached his duties.

Although this is an English case, Australian courts have often relied on English cases for guidance on the current law. Indeed, the concept of *de facto* directors in the United Kingdom is similar to this concept in Australia. However, care should be exercised in relying on this case because, as Bryson J observed in *Omnicon Video v Kookaburra Productions* (1995) 13 ACLC 1795 at 1796:

> "Statutory provisions which extend for various purposes the range of persons who are to be treated as if they were directors by reference to their taking part in management are common in contemporary companies legislation. Notwithstanding the similarity of concept, care should be used. [P]rovisions differ in their purpose and also in their detailed expression, and their application must always be affected by the instant facts."

6.4 The definition of a constitutional corporation under section 51(xx) of the Constitution

(By Edward Tudor, King & Wood Mallesons)

United Firefighters Union of Australia v Country Fire Authority [2014] FCA 17, Federal Court of Australia, Murphy J, 31 January 2014.

The full text of this judgment is available online.

(a) Summary

The key issue in this case for the purposes of this case note was whether the Country Fire Authority (CFA) is a trading corporation for the purposes of s. 51(xx) of the Constitution.

Section 51(xx) provides that the Parliament shall have power to make laws with respect to "foreign corporations, and trading or financial corporations formed within the limits of the Commonwealth".

Murphy J confirmed the established law that whether a corporation is a trading corporation depends on its actual activities, and not the purpose for which the corporation was established. His Honour also confirmed the indicia of trading activity set out in *Aboriginal Legal Service of Western Australia (Inc) v Lawrence (No 2)* [2008] WASCA 254 (*Aboriginal Legal Service*).

To determine whether the CFA was a trading corporation, his Honour considered whether each of the CFA's revenue generating activities involved an element of exchange of service for fee, whether the CFA had discretion to negotiate the relevant fee, and whether the CFA had discretion to provide or not provide the relevant service. Services that did not have discretion as to fees or provision were not, in his Honour's view, sufficiently commercial to constitute trading activities.

His Honour considered that the CFA's trading activities (amounting to almost $13 million, or 2.7% of the CFA's total revenue) were not insubstantial in absolute or relative terms, and that a relative test was the correct test to apply. As the activities were not insubstantial, his Honour found that the CFA was a trading corporation for the purposes of s. 51(xx) of the Constitution.

(b) Facts

The case concerned an enterprise agreement between the CFA and United Firefighters Union of Australia (UFU) (the Agreement). The Agreement was an enterprise agreement which covered all CFA employees in the relevant employee classifications, and was approved by the Fair Work Commission in October 2010 pursuant to the Fair

Work Act 2009 (Cth) (the Fair Work Act). Under the Fair Work Act, the Fair Work Commission (the Commission) has jurisdiction to approve an enterprise agreement involving a "national system employer". Under s. 14 of the Fair Work Act, a national system employer includes a constitutional corporation under s. 51(xx) of the Constitution.

Under cl. 27 of the Agreement, the CFA agreed, amongst other things::

- to employ an additional 342 career firefighters over six years;
- to conduct a minimum of 3 recruit training courses per year, with each training course training a minimum of 30 recruits (or a greater number agreed between the UFU and the CFA); and
- on or before 1 September each year, to request that its employees approve a proposed variation to Schedule 1 of the agreement to record all staff deployments in the preceding year.

In early 2011 a dispute arose between the UFU and the CFA as to the operation of clause 27, and the UFU applied to Fair Work Australia in accordance with the dispute resolution procedure set out in the Agreement. In June 2011, Fair Work Australia published a statement setting out a resolution to the dispute, which provided that:

- the CFA would conduct four recruitment courses of 25 recruits each in 2012 and 2013; and
- any variation to the number of recruit training courses, their timing and the number of recruits would be by consent of the UFU and CFA, (the Agreed Resolution).

Despite the Agreed Resolution, in 2012 and 2013 the CFA failed to conduct the specified number of recruitment courses and failed to train the agreed number of recruits. The CFA also failed to request that its employees approve a proposed variation to Schedule 1 to the Agreement on or before 1 September 2012.

(c) Decision

His Honour found that the CFA was a trading corporation, and therefore a constitutional corporation under s. 51(xx) of the Constitution. However, his Honour further found that the relevant clauses of the Agreement were invalid as they limited the capacity of the CFA (as an agency of the State of Victoria) to determine the number and identity of its employees (a principle set out in *Re Australian Education Union; Ex Parte Victoria* (1995) 184 CLR 188) (*Re AEU*).

This case note only considers his Honour's reasoning in relation to the decision that the CFA is a constitutional corporation.

(i) What constitutes a "trading corporation"

The CFA contended that it was not a constitutional corporation for the purposes of s. 51(xx) of the Constitution, and therefore that the Commission's power to approve the Agreement only arises by operation of the Fair Work (Commonwealth Powers) Act 2009 (Vic). In contending this, the CFA sought to rely on the majority in *R v Trade Practices Tribunal; Ex parte St George County Council* (1974) 130 CLR 533 (*St George*) and submitted that corporations which are not formed for the purpose or predominant purpose of engaging in trading activities and which do not carry on activities for that purpose are not properly characterised as trading corporations.

While Murphy J accepted that the CFA's purpose was not one of trading or commerce, his Honour considered that the majority in St George was no longer good law. His Honour determined that the appropriate test was not a "purpose" test as set out in St George, but an evaluation of the corporation's actual trading activities. His Honour went on to note that it "is not to say that the purpose for which the corporation was created will never be influential . but where a corporation is active, it is what the corporation does rather than what it was set up to do that will usually be determinative".

In coming to this view his Honour relied on the majority in *R v The Judges of the Federal Court of Australia; ex parte The Western Australian National Football League* (1979) 143 CLR 190. In that case, Murphy J considered that "as long as the trading is not insubstantial, the fact that trading is incidental to other activities does not prevent it being a trading corporation". Mason J considered that "[w]hether the trading activities of a particular corporation are sufficient to warrant its being characterised as a trading corporation is very much a question of fact and degree."

(ii) What constitutes a trading activity??

Murphy J considered that the test for whether a corporation's activities are "trading activities" is a broad one. His Honour cited *Aboriginal Legal Service*, which establishes that the term "trading activities" generally connotes "activities of a commercial nature involving, in essence, the exchange of goods and services for reward".

His Honour adopted the summary of Steytler P in *Aboriginal Legal Service* which established that:

- a corporation may be a trading corporation even though trading is not its predominant activity;
- the trading must be a substantial and not peripheral activity;
- trading extends to activities carried on with a view to earning revenue and includes trade in services;
- the making of a profit is not an essential prerequisite to trade, but is a usual concomitant;
- the fact that trading activities are conducted in the public interest will not necessarily exclude their categorisation as trade; and

- whether trading activities are sufficient for a corporation to be a trading corporation is a question of fact and degree.

(iii) Were the CFA's activities trading activities?

Numerous activities were identified as deriving revenue for the CFA. These activities included firefighting at uninsured properties, attendance at false alarms, fire equipment maintenance services, sale of goods, commercial and subsidised property rental, consultancy services, road accident rescue services and advice regarding dangerous goods. The CFA also derived revenue from insurance company contributions. The CFA submitted that certain activities were not trading activities because they were not of commercial character and charges were made to recover costs only, or not done for commercial purposes.

In considering whether each activity was a trading activity, his Honour turned his mind to whether each activity had a sufficiently commercial character.

His Honour considered the following factors were instructive in determining whether an activity was of commercial character:

- whether there was an element of exchange of the service for the payment of a fee;
- whether the CFA had the discretion to negotiate or bargain to set the relevant fee; and
- whether the CFA had a choice to provide the services or was under a statutory duty to do so.

Where the CFA had a choice to provide or not to provide the services, and where it had the ability to negotiate regarding the fees to be charged (such as in connection with its property rental, fire equipment and maintenance services and sale of goods), his Honour considered that these activities were trading activities. His Honour also considered that even though they were provided for under statute, the CFA's road accident rescue services were a trading activity, as the CFA had the discretion to charge a fee determined by it, and was not under a statutory duty to provide the services.

Where the CFA was under a statutory duty to provide services (such as preventing and suppressing fires in country Victoria or at uninsured properties), or where the CFA did not have discretion to set or negotiate the fees provided for services (such as for attendance at false alarms or provision of Hazmat or building protection services), his Honour considered that the relevant activities were not sufficiently commercial to be considered trading activities.

(iv) Is the CFA a trading corporation?

His Honour considered that whether the CFA is a trading corporation is to be determined by whether its trading activities are "not insubstantial".

The trading activities undertaken by the CFA resulted in $12.93 million in revenue, or 2.7% of the CFA's total revenue for the relevant period. The CFA contended that at 2.7% of total revenue, its trading activities were insubstantial in the context of its activities as a whole.

However, his Honour determined that the test should consider whether the activities were "peripheral, insignificant, incidental or trivial" and noted that he was disinclined to treat almost $13 million of revenue as insubstantial. While his Honour considered that the activities were significant in absolute terms, he appeared to favour a relative assessment. Acknowledging that this assessment was one of fact and degree and "not without difficultly", his Honour considered that the CFA's trading relative to its non-trading activities was "not insubstantial" and therefore it is a trading corporation.

6.5 No injunction granted for "watershed meeting" of creditors for registered foreign company

(By Amy Dunphy, Minter Ellison)

In the matter of Featherston Resources Limited (Receiver and Manager Appointed) (Administrators Appointed) [2014] NSWSC 12, Supreme Court of New South Wales, Black J, 23 January 2014

The full text of this judgment is available online.

(a) Summary

This case demonstrates the factors a Court may consider in deciding whether to grant an interlocutory injunction to restrain a registered foreign company from holding a creditors' meeting where it would be decided if the company should execute a deed of company arrangement (DOCA) as part of the voluntary administration process.

(b) Facts

Featherston Resources Limited (Receiver and Manager Appointed) (Administrators Appointed) (Featherston) is a New Zealand incorporated company. Featherston is a registered foreign company under the Corporations Act 2001 (Cth) (the Corporations Act).

It was accepted by both parties that Featherston was insolvent. The company was placed into voluntary administration. Under this process, a first meeting of creditors had occurred and a second "watershed meeting" was due to be held the day after the notice of motion was filed by the plaintiffs. A watershed meeting is equivalent to a second meeting of creditors under the voluntary administration process in the Corporations Act. At this meeting, the creditors were to decide whether the company should execute a DOCA proposed by a secured creditor Playman Group (Playman) and recommended by the administrators.

The plaintiffs sought an interlocutory injunction:

- to restrain the administrators of Featherston from conducting a vote of creditors on the DOCA at the watershed meeting; or
- to cause the administrators to adjourn the watershed meeting for 30 working days as allowable under the *Companies Act* (NZ); or
- for Playman to withdraw the DOCA proposed by it from consideration at the watershed meeting and to request that the meeting be adjourned for 30 days.

The interlocutory injunction was sought on the basis that separate proceedings were on foot in the New South Wales Supreme Court regarding alleged mismanagement by the directors said to contribute to Featherston's insolvency. These actions allegedly included the issue of convertible notes to another entity, FRCN Pty Limited (FRCN) which was apparently associated with two of Featherston's directors and a former executive. The plaintiffs contended that if the DOCA was passed under New Zealand voluntary administration process then the New South Wales proceedings would be rendered moot.

The plaintiffs had not applied to the High Court of New Zealand to set aside the administration.

(c) Decision

Black J dismissed the plaintiff's application for an interlocutory injunction.

In relation to the application for an interlocutory injunction, his Honour considered that the question was whether, having regard to the balance of convenience, the plaintiffs had established a sufficiently serious, arguable case so to justify the grant of interlocutory relief.

In dealing with the balance of convenience, Black J noted that the question is whether the grant, or withholding of, interlocutory relief carries the lowest risk of doing injustice to one party or to the other or to a third party: *Patrick Stevedores Operations No 2 Pty Ltd v Maritime Union of Australia (No 3)* [1998] HCA 30 at [41] - [42].

In the present circumstances, Black J was not satisfied that the balance of convenience favoured the plaintiff's application.

In support of this conclusion Black J noted that:

- the remedies available to the plaintiffs in a New Zealand Court were amply sufficient to protect their position;
- the Court should be cautious in taking steps which would significantly affect the conduct of an administration taking place in respect of a New Zealand company under the statutory regime established by the *Companies Act* (NZ);
- the administrators could not unilaterally adjourn the watershed meeting without the consent of the majority of creditors, which may not be given;
- the New Zealand Courts have the power to terminate a DOCA under s. 239ADD of the *Companies Act* (NZ), which is similar in its terms to s. 445D of the Corporations Act, including where misleading information is provided in respect of the meeting, where effect cannot be given to that deed without injustice or where the deed gives rise to oppression, unfair prejudice or unfair discrimination.

Ultimately, Black J found that it would be an intrusion into the supervisory jurisdiction conferred on the New Zealand Courts under the *Companies Act* (NZ).

Even if Featherson were in administration in Australia, Black J stated that he would have difficulty in upholding the plaintiffs' application. His Honour cited with approval the decision by Barrett J in *NA Enterprises Pty Ltd v Jonvana Enterprises Pty Ltd* [2011] NSWSC 125. There, the court refused the application of a secured creditor to restrain an administrator proceeding with a meeting of creditors of an Australian incorporated company. Although Barrett J considered there to be a serious question to be tried, he held that as the administrator had found the company to be insolvent, in order to justify the Court preventing the continuation of the administration, there would need to be strong countervailing evidence or factors presented by the plaintiff.

6.6 Quasi-partnership breakdown and mismanagement of affairs leading to a successful application for winding up

(By Edward Kus, DLA Piper)

Entwisle v Minken Pty Ltd (Receivers and Managers Appointed) [2013] VSC 709, Supreme Court of Victoria, Elliott J, 19 December 2013

The full text of this judgment is available online.

(a) Summary

This case concerned an application to wind-up companies pursuant to s. 461(1)(k) of the Corporations Act 2001 (Cth) (the Corporations Act).

In deciding that winding up the companies in this instance was just and equitable, Elliot J relied upon:

- the dysfunctional relationship between the parties;
- mismanagement by the defendant of the affairs of the companies in question;
- shortcomings in the evidence available with regard to creditors and certain agreements between the parties; and
- the fact that there was no viable alternative.

(b) Facts

Timothy John Entwisle (Entwisle) and Ian Andrew McGoldrick (McGoldrick) were in a quasi-partnership, pursuant to which they agreed to make equal contributions to their venture in property development (despite no written agreement being entered into).

A number of companies were established for the purposes of this venture - Minken Pty Ltd (receivers and managers appointed (Minken), Deer Park Holdings Pty Ltd (Deer Park), Control Group Services Pty Ltd (Control Group), and Henton Pty Ltd (Henton) - together, the Companies.

The relationship between Entwisle and McGoldrick broke down. Elliot J described the break down as "serious", and the relationship as not "functional", "entirely unsatisfactory" and "in disarray". As a result of the breakdown Entwisle and McGoldrick decided to enter into a Dissolution Agreement. Both parties submitted that a binding agreement existed, but the evidence as to its terms was inconsistent.

McGoldrick had seriously mismanaged the affairs of the Companies, as evidenced by the failure of each Company to lodge tax returns for extended periods of time and the inability of McGoldrick to comply with the court's document production orders, which demonstrated "at the very least .significant mismanagement".

Entwisle, along with Baraman Holdings Pty Ltd (Baraman) and Entwisle Pty Ltd (Entwisle Co), being companies associated with Entwisle, applied to have the Companies wound-up (together, the Plaintiffs).

(c) Decision

Before considering whether it was just and equitable to wind-up the Companies in accordance with s. 461 of the Corporations Act, Elliot J first considered whether the Plaintiffs had standing to bring the claim pursuant to s. 462 of the Corporations Act:

- Deer Park and Control Group - standing was straightforward with respect to Deer Park and Control Group, as ntwisle and Baraman were registered shareholders respectively;
- Henton - Elliot J found that the existence of a loan agreement between Henton and Entwisle for the sum of $52,000 meant that Entwisle was a creditor of Henton. Additionally, Entwisle Co had transferred $389,927.38 to Henton (the Further Funds) of which $77,805.84 has been recovered by Entwisle Co. There was competing evidence on the characterisation of the Further Funds, though ultimately Elliot J found that the Further Funds were best classified as a loan and similarly gave rise to the characterisation of Entwisle Co as a creditor; and
- Minken - Elliot J found that Baraman was a creditor of Minken on the basis that it was a shareholder of Minken. McGoldrick held half of the issued share capital in Minken (the Minken Shares) as bare trustee for Baraman. On 8 May 2013 Baraman sent a letter to McGoldrick requesting that McGoldrick transfer the Minken Shares to Baraman. The Plaintiffs sought an order pursuant to s. 51 of the Trustee Act 1958 (Vic) that the Minken Shares be vested in Baraman. Elliot J confirmed that such an order can be made where "a trustee neglects or refuses to convey any property". As such, an order was made to vest the Minken Shares in Baraman and retrospectively amend the register of shareholders of Minken to reflect this.

Upon establishing that the Plaintiffs had the necessary standing to bring a claim under s. 462 of the Corporations Act, Elliot J then considered whether a winding-up order should be made with respect to the Companies. Elliot J held that it was just and equitable to wind up the Companies for the following reasons:

- McGoldrick had clearly shown he was not a person who could be expected to act consistently with the duties and obligations imposed upon a director and shareholder of a company in which another person has a substantial interest;
- the Companies' accountant now refuses to communicate at all with McGoldrick. By contrast a liquidator would have powers to compel meaningful responses;
- there were serious concerns regarding the Companies' compliance with tax obligations;
- there were serious concerns regarding the records of the Companies generally;
- there was little reason to be confident that the intermingling of the Companies' funds has been appropriate;
- the relationship between McGoldrick and Entwisle was "in disarray".

His Honour additionally considered the following submissions:

- McGoldrick argued that the Companies' creditors would be disadvantaged by a winding-up order. In response to this submission, Elliot J stated that "the court simply [had] not been informed of the relevant facts" and that the evidence relating to this was ambiguous. Accordingly his Honour drew no inference that any creditors would be any worse off if a winding up order were made;

- McGoldrick argued that Entwisle's conduct in relation to the Companies should disentitle him to the benefit of a winding up order. Similarly, Elliot J did not accept this argument, as Entwisle's conduct (including failing to make certain contributions) was due to Entwisle walking away from the quasi-partnership to perform his obligations under the Dissolution Agreement;
- McGoldrick argued that he should have an opportunity to buy-out Entwisle. However, Elliot J stated that "I am firmly of the view that a buy-out would be totally inappropriate in this case." In particular McGoldrick led no evidence of his financial capacity to effect the buy-out. There was also evidence before the court that McGoldrick was "technically insolvent"; and
- McGoldrick argued that Entwisle's application to the Court to have the Companies wound up was an abuse of process with respect to another proceeding between the parties. In response, Elliot J held that Entwisle's application was "entirely appropriate".

6.7 Application by former administrators for determination of remuneration under section 449E of the Corporations Act

(By Laura MacLeod, Minter Ellison)

Strazdins v DNPW Pty Ltd [2013] FCA 1368, Federal Court of Australia, Besanko J, 16 December 2013

The full text of this judgment is available online.

(a) Summary

In this case the Court found that s. 449E of the Corporations Act 2001 (Cth) (the Corporations Act) extends to former administrators so that they can apply for a determination of remuneration. Further, the Court found that it has a power terminate an application under s. 449E at an early stage where such an application would be futile or doomed to fail.

(b) Facts

On 24 April 2008, Andre Strazdins and Nick Cooper were appointed joint and several voluntary administrators of DNPW Pty Ltd (DNPW). They were then appointed joint and several deed administrators on 22 September 2008 upon the execution by DNPW of a deed of company arrangement.

Mr Strazdins and Mr Cooper resigned as deed administrators on 10 August 2011.

At a creditors meeting of DNPW held on 26 August 2008, the creditors resolved that Mr Strazdins and Mr Cooper be remunerated for their services rendered from 24 April 2008 to 31 July 2008 in the sum of $193,232.25 plus GST.

The creditors discussed the remuneration of Mr Strazdins and Mr Cooper again at the creditors meeting on 16 February 2011.

At that meeting, the creditors voted against the following resolutions:

- the amount of $106,960.50 plus GST be approved for payment of services rendered by Mr Strazdins and Mr Cooper from 1 August 2008 to 21 September 2008; and
- the amount of $902,898.80 plus GST be approved for payment of services rendered by Mr Strazdins and Mr Cooper from 22 September 2008 to 7 January 2011.

On 9 May 2013, Mr Strazdins and Mr Cooper applied to the Court for an order that they be allowed to make an application under s. 449E of the Corporations Act in their capacity as former administrators and deed administrators and for leave to file such an application.

Section 449E of the Corporations Act provides for the determination of the remuneration to which administrators are entitled. Mr Strazdins and Mr Cooper were under the impression that they could not apply for such an order in their capacity as former administrators and deed administrators. Accordingly, Mr Strazdins and Mr Cooper applied for an order that s. 449E of the Corporations Act operate so as to entitle them to make an application under that section.

By the time of the application, DNPW had sold its assets and the proceeds had been distributed. It had no property which Mr Strazdins and Mr Cooper could pursue for recovery of their remuneration. Mr Strazdins and Mr Cooper had however, commenced separate civil proceedings against the creditors of DNPW in the Northern Territory and South Australia Supreme Courts and they referred to this application in the Federal Court for determination of their remuneration in those proceedings.

There was also a further action between Mr Strazdins, Mr Cooper and two of the creditors of DNPW in the Northern Territory Supreme Court, which concluded that Mr Strazdins and Mr Cooper had a conflict of interest during at least part of the period in relation to which they now claim a determination of their remuneration.

DNPW and its creditors submitted that the Court has discretion under s. 449E of the Corporations Act to refuse to entertain an application for the determination of remuneration or to summarily dismiss such an application.

The reasons advanced by DNPW and the creditors for exercising the discretion were:

- there was no property of DNPW left for the recovery of Mr Strazdin and Mr Cooper's remuneration;
- Mr Strazdin and Mr Cooper did not ask the creditors to determine their remuneration in the first instance as required under s. 449E of the Act;
- there was delay by Mr Strazdin and Mr Cooper in bringing the application; and
- comity given the finding of conflict of interest by the Northern Territory Supreme Court.

(c) Decision

(i) Whether former administrators need an order to be able to make an application under section 449E of the Corporations Act

The Court found nothing in the terms of s. 449E of the Corporations Act which requires an applicant to be an existing administrator at the time of their application or at the time that the application is determined by the Court. It was also noted that the section should be construed broadly in light of the fact that an administration might come to an end quite quickly. The Court concluded that a former administrator may bring an application for determination of their remuneration under s. 449E of the Corporations Act without an order allowing them to do so. Mr Strazdin and Mr Cooper would therefore need to amend their application to claim a determination under s. 449E of the Corporations Act.

(ii) Whether the Court has a discretion under section 449E of the Act to refuse to entertain, or to summarily dismiss, an application

The Court noted that it does have the power to terminate an application under s. 449E at an early stage where such an application would be futile or doomed to fail and therefore an abuse of process.

However, the Court declined to exercise that power after noting that:

- the determination of Mr Strazdin's and Mr Cooper's remuneration was relevant to separate civil proceedings instituted by them against the creditors of DNPW;
- Mr Strazdin and Mr Cooper took the question of their remuneration to the creditors of DNPW twice;
- there is no time limit for making an application under s. 449E of the Corporations Act and the delay caused little prejudice to DNPW and its creditors; and
- the Northern Territory Supreme Court was not considering an application by Mr Strazdin and Mr Cooper for a determination of their fees when it found a conflict of interest.

6.8 Consideration of affidavits supporting applications to set aside creditors' statutory demands

(By Peter Motti, Minter Ellison)

Reavill Farm Pty Ltd v Burrell Solicitors Pty Ltd [2013] FCA 1295, Federal Court of Australia, Edmonds J, 4 December 2013

The full text of this judgment is available online.

(a) Summary

This case examines whether affidavits filed by the plaintiffs were affidavits supporting their applications under s. 459J(1)(b) of the Corporations Act 2001 (Cth) (the Corporations Act) to set aside creditors' statutory demands under s. 459G of the Corporations Act. Furthermore, the case considers whether sufficient information was contained within the affidavits to fairly alert the defendant to the nature of the plaintiffs' case and whether the Court should use its discretion under s. 459J(1)(b) of the Corporations Act to set aside the statutory demands.

(b) Facts

On 27 September 2013, each of the plaintiffs filed originating applications under s. 459G of the Corporations Act to set aside a creditor's statutory demand dated 10 September 2013 for a debt in the sum of $188,005.11, described as "Judgment/Order of the Supreme Court of NSW Case Number 2013/00255030 made on 22 August 201[3]". Section 459G of the Corporations Act prescribes that:

- a company may apply to the Court for an order setting aside a statutory demand served on the company;
- an application may only be made within 21 days after the demand is so served; and
- an application is made in accordance with this section only if, within those 21 days:
    - an affidavit supporting the application is filed with the Court; and
    - a copy of the application, and a copy of the supporting affidavit, are served on the person who served the demand on the company.

Section C of each of the plaintiffs' applications stated:

"The application is brought pursuant to s. 459G on the Corporations Act 2001, on the ground stipulated in s. 459J(1)(b) of that [Corporations] Act, in that there is a genuine dispute about the debt that is the subject of the statutory demand."

Section 459J of the Corporations Act states that:

- on an application under s. 459G, the Court may by order set aside the demand if it is satisfied that:
  - because of a defect in the demand, substantial injustice will be caused unless the demand is set aside; or
  - there is some other reason why the demand should be set aside; and
- except as provided in subsection (1), the Court must not set aside a statutory demand merely because of a defect.

On the same day, each of the plaintiffs filed an affidavit, sworn by a Mr Champion on 26 September 2013, allegedly in support of the applications annexing a copy of the Creditor's Statutory Demand served on 12 September 2013.

On 3 October 2013, each of the plaintiffs repeated the processes described above, but this time in respect of a debt of $349,302.42, which was described as "Judgment/Order of the Supreme Court of NSW Case Number 2013/00255045 made on 22 August 201[3]".

(c) Decision

(i) Affidavit supporting the application

Edmonds J explained that the combined effect of ss. 459G(1) and (2) of the Corporations Act is that a company can only apply to the Court for an order setting aside a statutory demand served on the company if the application is made within 21 days after the demand is so served (there was no dispute that the four applications in this case satisfied that requirement). His Honour went on to say that the combined effect of ss. 459G(1), (2) and (3) of the Corporations Act is that an application will only be in accordance with s. 459G of the Corporations Act if, within those 21 days:

- an affidavit supporting the application is filed with the Court; and
- a copy of the application, and a copy of the supporting affidavit, are served on the person who served the demand on the applicant company.

Therefore, the principal issue before his Honour was whether the affidavits were indeed "affidavit[s] supporting the application[s]".

His Honour noted that each of the applications were:

> "grounded in s 459J(1)(b) of the [Corporations] Act, namely, 'there is some other reason why the demand should be set aside' which, construed in context, means some reason other than because of a defect in the demand. In other words, paras (a) and (b) of s 459J(1) are mutually exclusive".

Therefore, the primary question to be answered was whether Mr Champion's affidavits sworn 26 September and 2 October 2013 were "affidavit[s] supporting the application[s]" grounded on s. 459J(1)(b) of the Corporations Act. His Honour considered that they were, citing in each case, the second and third sentences of paragraph 5, which read:

> "Annexed to this affidavit and marked "D" is a copy of the Amended Cross Summons in proceedings no. 2011/365912, filed 6 May 2013, and the Amended Statement of [Cross] Claim in those proceedings, filed 6 May 2013. The sums claimed in those proceedings are in excess of the debt the subject of the Creditor's Statutory Demand".

His Honour found that the Amended Cross-Summons and the Amended Statement of Cross-Claim contained sufficient information and material to "fairly alert" the defendant "to the nature of the case" the plaintiffs "will seek to make in resisting the statutory demand" (citing the judgment of Barrett J in *Process Machinery Australia Pty Ltd v ACN 057 262 590 Pty Ltd* [2002] NSWSC 45 at [22]), irrespective of whether the Court adopted the "clear delineation" test of Barrett J in *Process Machinery*, or "the more elastic test" of White J in *Hansmar Investments Pty Ltd v Perpetual Trustee Co Ltd* [2007] NSWSC 103 at [32] and [33].

As his Honour found that each of the Mr Champions affidavits were in fact "affidavit[s] supporting the application[s]", it followed that his Honour held that the applications were made in accordance with s. 459G of the Corporations Act.

(ii) The Court's discretion under section 459J(1)(b)

Edmonds J then considered whether the existence of the cross-claim, "arising as it [did] out of the same subject matter or circumstances upon which the judgment debts are constituted," was a reason why the demands should be set aside under s. 459J(1)(b) of the Corporations Act. His Honour referred to the decision of the Full Court of the Federal Court in *Hoare Bros Pty Ltd v Deputy Commissioner of Taxation* (1996) 62 FCR 302 at 317:

> "Whatever view is taken of the relationship between s 459J(1)(a) and (b), the Court has a discretion in a case which does not involve a defect in the demand to set aside the demand, if some appropriate reason is shown. The discretion may be exercised in favour of a company, even without a showing that substantial injustice would otherwise be caused... It would be unwise to attempt to mark out the limits of the discretion conferred by s 459J(1)(b)".

His Honour re-affirmed that the only restraint on the Court's discretion under s. 459J(1)(b) of the Corporations Act is "whether the reason is the existence of a defect in the demand", and took the view that in this case, the Court's discretion was not in any way fettered if there was "some other reason why the demand(s) should be set aside".

Ultimately, his Honour decided to exercise the Court's discretion under s. 459J(1)(b) of the Corporations Act to set aside the demands. His Honour considered that there was:

> "undoubtedly a genuine dispute between the defendant and the plaintiffs, not about the existence or amounts of the judgment debts upon which the demands are founded, but about the costs assessments which constitute the basis upon which the judgment debts were entered and whether those assessments are 'infected' by the cause of action raised in the cross-claim such that there is no liability to pay the moneys claimed under those costs assessments."

6.9 Transfer of shares and units before delivery of judgment held to be a voidable disposition under section 37A of the Conveyancing Act 1919 (NSW)

(By Lily Zhang, Ashurst)

Ingram v Y Twelve Pty Ltd [2013] NSWSC 1777, Supreme Court of New South Wales, Stevenson J, 3 December 2013

The full text of this judgment is available online.

(a) Summary

The Court held that the transfers of shares and units by HM&O Investments Pty Ltd (HM&O) to Y Twelve Pty Ltd (Y Twelve) prior to delivery of judgment in proceedings to which HM&O was a party was deemed voidable by the Court pursuant to s. 37A of the Conveyancing Act 1919 (NSW) (the Conveyancing Act).

(b) Facts

Mr and Mrs Ingram (Ingram) conducted business involving the manufacturing and design of outdoor playground equipment from 1985 to 2007. In 2007, Ingram sold their business to HM&O and Teach & Play Pty Ltd (T&P), both now in liquidation.

HM&O and T&P later alleged that Ingram had engaged in misleading or deceptive conduct in relation to the sale. Counsel for HM&O warned Mr Salmon, a director of HM&O and T&P, of the risk of losing the case against Ingram and being ordered to pay Ingram's costs of the proceedings.

Mr Salmon enquired of his counsel as to whether he could "disperse" or "dispose" of "some of the companies' assets" and was told by counsel that he could not.

On 29 August 2012, the Court informed the parties that judgment would be delivered on 31 August 2012. Later that day, Mr Salmon implemented the transfers of shares and units owned by HM&O to a newly formed company, Y Twelve. The transfers were prepared and executed on 30 August 2012.

On 31 August 2012, judgment was delivered, ordering Ingram to pay nominal damages of $10,000 to HM&O and T&P and on 26 September 2012, the Court ordered that HM&O and T&P pay Ingram's costs of the proceedings.

Ingram sought a declaration that the transfers constituted an "alienation of property, made.with intent to defraud creditors" for the purposes of s. 37A of the Conveyancing Act.

(c) Decision

Section 37A(1) of the Conveyancing Act states that "every alienation of property.with intent to defraud creditors, shall be voidable at the instance of any person thereby prejudiced".

The transfers of shares and units to Y Twelve were intended to defraud creditors, particularly Ingram. The Court ordered HM&O to pay Ingram's legal costs and the transfers were deemed voidable by the Court.

(i) Intention of the debtor

In determining the intention of HM&O under s. 37A of the Conveyancing Act, the Court drew principles from relevant case law as follows:

- "intent" in s. 37A of the Conveyancing Act is satisfied where there exists an intention to hinder, delay or defeat creditors;
- the intention of the debtor to hinder, delay or defeat creditors does not need to be the sole, predominant or substantial intention;
- the intention must be to deprive the creditors of something to which they would otherwise be (legally) entitled; and
- the relevant intention of the debtor may be established by inference, and the debtor's intention may be inferred from the making of a disposition.

Further, the Court held that it was unnecessary to show that the debtor wanted its creditors to suffer a loss or that the debtor had a purpose of causing loss.

(ii) Prejudice to creditors

The Court held that the reference to "creditor" in s. 37A of the Conveyancing Act extended to future creditors as well as prospective or contingent creditors.

A creditor may establish prejudice where:

- a debtor disposed of an asset which would be available to his creditors with the intention of prejudicing them by putting the asset, or its worth, beyond their reach; or
- there would be an increase in the assets available for the benefit of creditors if the transfer were to be avoided.

The Court held that HM&O's intention in effecting the transfers was, at least in part, to place beyond the reach of Ingram assets which might have been available to them were they to succeed in the proceedings and obtain a favourable costs order.

6.10 Privilege against self-incrimination: not always enough for a stay of proceedings

(By Alexandra Eggerking, Herbert Smith Freehills)

White v Australian Securities and Investments Commission [2013] QCA 357, Court of Appeal, Supreme Court of Queensland, Muir and Gotterson JJA and Applegarth J, 3 December 2013

The full text of this judgment is available online.

(a) Summary

On an appeal by one of several defendants to civil proceedings brought by the Australian Securities and Investments Commission (ASIC), the Court of Appeal of the Supreme Court of Queensland (Court of Appeal) upheld the primary judge's (Fryberg J) decision that a stay of the proceedings until the determination of a simultaneous criminal trial in New Zealand should not be granted.

(b) Facts

ASIC brought proceedings against a number of parties, including a company in liquidation which was the responsible entity for a registered scheme under the Corporations Act 2001 (Cth) (the Corporations Act) for breaches of duties under s. 601FC of the Corporations Act, including misapplying funds and providing false information to a range of persons (the ASIC proceedings). Among the other defendants to the proceedings were directors and senior officers of the company, who were alleged to have brought about the contraventions, or have derivative liability for them. One such defendant was the appellant in the proceedings before the Court of Appeal (the Appellant), against whom ASIC had sought civil penalties and disqualification orders.

The New Zealand Financial Markets Authority filed criminal charges in the Auckland District Court against two of the individuals who were defendants to the ASIC proceedings, including the Appellant, for signing a registered prospectus which contained untrue statements, and being director of a company which issued debt securities and distributed an advertisement which contained untrue statements.

The Appellant applied for a stay of the ASIC proceedings until the determination of the New Zealand prosecution. The primary judge dismissed the application for a stay of proceedings..

(c) Decision

The Appellant alleged four appealable errors in the primary judge's exercise of discretion which related to his fundamental privilege against self-incrimination. The Court of Appeal held that each alleged error was not established, and dismissed the appeal.

(i) Inference of prejudice

The Appellant alleged that, instead of inferring prejudice to the Appellant, the primary judge wrongly imposed a requirement on the Appellant to go into evidence and to waive the privilege against self-incrimination he sought to protect as a pre-condition the favourable exercise of the discretion to grant a stay. The Court of Appeal held that the primary judge considered the potential prejudice to the Appellant in feeling compelled to give evidence in the ASIC proceedings, but was not satisfied that the Appellant had demonstrated that he would suffer significant disadvantage by maintaining a claim of privilege rather than giving evidence.

(ii) Loss of tactical advantage

The Appellant alleged that the primary judge erroneously characterised the advantage to the New Zealand prosecution in knowing in advance the nature of the evidence the Appellant would likely give in his defence as nothing more than the loss by the appellant of a tactical advantage. The Court of Appeal held that the primary judge plainly considered the possibility that the Appellant may suffer a material disadvantage in the New Zealand proceedings by going into evidence in the ASIC proceedings and being subjected to cross-examination, and recognised the fundamental nature of the privilege against self-incrimination.

(iii) Elevation of case management principles

TThe Appellant alleged that the effect of the refusal of the stay was to elevate case management principles above the Appellant's fundamental common law right to the preservation of his privilege against self-incrimination. The Court of Appeal held that this complaint lacked a factual foundation. The primary judge had been assisted by the guidelines articulated by Wootten J in *McMahon v Gould* (1982) 7 ACLR 202 at 206-208 to be taken into account in a stay application, and engaged in a process of balancing the relevant competing interests.

(iv) Section 1317N of the Corporations Act

The Appellant alleged that the primary judge erred in failing to find that s. 1317N of the Corporations Act evidenced a legislative intent that criminal offences arising out of the same factual matrix be heard ahead of civil penalty proceedings. The Court of Appeal held that the primary judge's findings on this point were unexceptional and did not display error. In particular, the Court of Appeal noted that s. 1317N was not applicable to foreign criminal proceedings.

(v) Further considerations against the grant of the stay

The Court of Appeal held that, even if the Appellant had succeeded in showing appealable error on the part of the primary judge, certain considerations would have led the Court of Appeal to exercise its discretion against the grant of a stay. Notwithstanding the practical compulsion to give evidence that the Appellant might face if the ASIC proceedings were not stayed, the Appellant had no absolute right to a stay of the proceedings. Considerations against the grant of a stay included the effect of granting the stay on the other respondents, risks to the quality of the evidence in the ASIC proceedings as a result of further delays to the proceedings, and the public interest in having claims such as the one in question resolved in a timely way.

6.11 Solicitors' duty of care where the interests of the client company and instructing executive directors conflict

(By Katrina Sleiman and Sam Jian, Corrs Chambers Westgarth)

Newcastle International Airport Ltd v Eversheds LLP [2013] EWCA Civ 1514, England and Wales Court of Appeal (Civil Division), Moore-Bick, Rimer and Underhill LJJ, 28 November 2013

The full text of this judgment is available online.

(a) Summary

The claimant, Newcastle International Airport Limited (NIAL), instructed the respondent solicitors, Eversheds LLP (Eversheds), to draft service contracts for its two executive directors. The executive directors provided the instructions to Eversheds and the contracts were executed by NIAL. The contracts had the unintended effect of entitling the executives to bonuses totalling some £8 million upon the completion of NIAL's refinancing and releasing the executives from certain restrictive covenants. Neither NIAL's board nor its remuneration committee (the RC), which comprised non-executive directors, understood that the contracts had such effects when NIAL signed them.

At first instance, Proudman J dismissed NIAL's negligence claim against Eversheds, finding that Eversheds did not breach their duty of care to NIAL. Her Honour held that the real reason that NIAL suffered loss was because its non-executive directors failed to carry out their obligations to NIAL.

The Court of Appeal allowed NIAL's appeal and found that Eversheds did breach their duty of care to give NIAL a proper explanation of the contracts. However, the Court awarded nominal damages on the basis that NIAL's loss was caused by the incompetence and carelessness of the Chairperson of the RC, Ms Radcliffe, and not by Eversheds's breach.

(b) Facts

NIAL retained Eversheds to draft new service contracts for its two executive directors, Mr Parkin and Mr Friis (the Executives), by making revisions to their existing contracts. Ms Radcliffe authorised the executives to provide instructions on the drafting to Eversheds.

The revised contracts had the effect of entitling the Executives to bonuses totalling 3% of any "refinancing proceeds" and narrowing the restrictive covenants. The final version of the draft contracts were in a form ready for signature so that the revisions were not apparent. Ms Radcliffe reviewed the draft contracts, believed that they fully accorded with the principles agreed to by the RC, and signed both contracts on NIAL's behalf. It later emerged that she had only read through the draft contracts cursorily and had materially misunderstood the revised terms.

The RC approved the revisions in the draft contracts, but never discussed or questioned the meaning of "refinancing proceeds". Members of the RC generally understood it as referring to the difference between the old and new debt, and that the executives would receive a bonus of 3% of the amount returned to shareholders. In fact, Mr Parkin instructed Eversheds to define "refinancing proceeds" as the total value of the refinancing of the company minus the value of any pre-existing bank bond or loan notes debt. After the contracts were signed, NIAL's loans were refinanced for the total value of £282 million, resulting in the executives receiving much larger bonuses than the RC intended. Mr Parkin instructed Eversheds on the definition of "refinancing proceeds" and the relaxation of the restrictive covenants without first obtaining Ms Radcliffe's authority on the content of these terms.

At first instance, Proudman J found that the executives exceeded the scope of their actual authority by giving instructions on the restrictive covenants and refinancing proceeds. However, they had apparent authority to instruct Eversheds to draft the contracts, as Ms Radcliffe held them out to Eversheds as having such authority. Her Honour also held that Eversheds did not breach their duty of care to NIAL by failing to provide separate advice to Ms Radcliffe on the meaning and effect of the revisions, and that NIAL's own conduct broke the chain of causation because Ms Radcliffe failed to read the draft contracts and related documents properly.

(c) Decision

As a preliminary comment, the Court noted that the fact that Eversheds were prepared to, and did, take their instructions from the executives, primarily Mr Parkin, was surprising. Eversheds knew their client was NIAL and that they were not acting for either executive. Yet the matter in which they were retained was the re-drafting of service agreements between NIAL and the executives. The Court considered there was an obvious conflict of interest between the parties to each contract.

The end result of Eversheds's handling of their instructions was that whilst they could be confident that Mr Parkin understood and agreed with their drafts, they went to no lengths to ensure that representatives of NIAL acting exclusively in NIAL's interests had a like understanding and, as it turned out, they did not.

(i) Did the executive directors have NIAL's authority to instruct Eversheds?

The Court upheld Proudman J's finding that the executives had apparent authority to give Eversheds instructions. This necessarily included authority to answer questions on drafting matters which Eversheds required clarification, such as the scope of the restrictive covenants and the definition of "refinancing proceeds". The Court noted that Eversheds's task was merely to produce draft contracts and Eversheds were entitled to assume NIAL would not execute the contracts without first satisfying itself as to their content.

(ii) Did Eversheds breach its duty of care to NIAL?

The Court held that Proudman J erred in finding that Eversheds did not breach their duty of care to NIAL. The Court accepted that in a conventional case where a company authorises its executives to instruct solicitors in relation to a matter in which the executives had no personal interest, the solicitors' advice to the executives will ordinarily stand as advice to the company.

However, in the present case there was a clear conflict between the interests of the executives and those of NIAL in relation to the drafting exercise; a conflict which Eversheds was or ought to have been aware of. The Court held that in the particular circumstances of this case, part of Eversheds' duty of care to NIAL was to ensure that Ms Radcliffe, the person reviewing the contracts with NIAL's interests exclusively in mind, understood the effect of the revisions. The Court found that in order to satisfy this duty, Eversheds ought to have provided Ms Radcliffe, as Chairperson of the RC, with a memorandum summarising the revisions to the existing contracts and how they worked in practice.

The Court found that if Eversheds had provided such a memorandum and Ms Radcliffe had carefully read and understood it, it is likely that the revised terms would have been amended. The Court held that by failing to provide such a memorandum to Ms Radcliffe, Eversheds breached its duty of care to NIAL.

(iii) Did Eversheds's breach cause loss or damage to NIAL

The critical question was whether Ms Radcliffe would in fact have read and understood a memorandum summarising the revisions if it was provided by Eversheds. In deciding this issue, the Court was critical of the RC, and in particular, Ms Radcliffe. The Court considered Proudman J's assessment of Ms Radcliffe's approach to performing her duties. This included her reluctance to read important documents and attachments or, as she did with the draft contracts, to read them in a superficial manner, and her tendency to misunderstand the contents of documents. Proudman J considered that Ms Radcliffe "seemed to think it was not her job to read any documents which could be categorised as legal documents". The Court cited a passage of Proudman J's reasons which revealed that although Ms Radcliffe maintained that she did read the refinancing bonus provision in the draft contract, she failed to understand that it entitled the executives to a minimum bonus payment; instead she thought the refinancing bonuses were purely discretionary until the trial. Proudman J was highly critical, noting "I can only assume that her grasp of what was happening was foggy and that she thought that her role as a non-executive director was much more constrained than in fact it was. She has therefore had to re-write history, as much apparently for her own amour propre as to convince others. I say that because her belief as to the discretionary nature of the bonuses is impossible on any other basis to reconcile with what actually happened".

The Court upheld Proudman J's finding that even if Ms Radcliffe had read a memorandum provided by Eversheds, she would have misunderstood the parts dealing with the refinancing bonuses, with the result that contracts containing the same refinancing bonus provision would still have been signed. NIAL therefore failed to prove causation.

The Court allowed NIAL's appeal with respect to Eversheds's breach of duty and ordered Eversheds to pay nominal damages of £2.