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From: SAI Global Information Services <corporatelawbulletin@saiglobal.com>
Sent: Monday, July 27, 2020 6:58 PM
To: Ian Ramsay
Subject: SAI Global Corporate Law Bulletin No. 275

27 July 2020 > Regulatory Newsfeed

SAI Global Corporate Law Bulletin No. 275>

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Bulletin No. 275

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Published by SAI Global on behalf of Centre for Corporate Law, Faculty of Law, The University of Melbourne with the support of the Australian Securities and Investments Commission, the Australian Securities Exchange and the leading law firms: Ashurst, Clayton Utz, Corrs Chambers Westgarth, DLA Piper, Herbert Smith Freehills, King & Wood Mallesons, Minter Ellison.

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1. Recent Corporate Law and Corporate Governance Developments

1.1 SEC adopts rule amendments for proxy advisors

22 July 2020 - the United States Securities and Exchange Commission (SEC) has adopted amendments to its rules governing proxy solicitations which, according to the SEC, "aim to facilitate the ability of those who use proxy voting advice - investors and others who vote on investors' behalf - to make informed voting decisions without imposing undue costs or delays that could adversely affect the timely provision of proxy voting advice".

In brief, the amendments require proxy advisors to disclose material conflicts of interest in their proxy voting advice. In addition, proxy advisors must provide their reports to SEC registered issuers at least simultaneously with distribution to clients, and proxy advisors must notify their clients of issuer responses prior to voting. The amendments condition the availability of two exemptions from certain of the federal proxy rules often used by proxy voting advice businesses on compliance with conflicts of interest disclosure requirements.

The exemptions are also conditioned on two requirements designed to ensure that: (1) SEC registrants that are the subject of proxy voting advice have such advice made available to them in a timely manner, and (2) clients of proxy voting advice businesses are provided with an efficient and timely means of becoming aware of any written responses by SEC registrants to proxy voting advice.

In addition, the amendments codify the Commission's longstanding view that proxy voting advice generally constitutes a solicitation under the proxy rules, and make clear that the failure to disclose material information about proxy voting advice may constitute a potential violation of the antifraud provision of the proxy rules.

View the amended SEC rule: Exemptions from the Proxy Rules for Proxy Voting Advice.

1.2 Global M&A data for second quarter 2020

15 July 2020 - The International Institute for the Study of Cross-Border Investment and M&A (XBMA) has published its quarterly review for the second quarter of 2020.

Global M&A activity in Q2 2020 dropped to its lowest quarterly levels in more than a decade, as corporate dealmakers paused to weigh the effects of the COVID-19 pandemic, including the responses of governments, businesses and consumers across the world, and many companies devoted all available resources to existence-preserving activities and not growth or diversification.

Global M&A volume was US$517 billion in Q2 2020, a decrease of 25% from Q1 2020 and 53% from Q2 2019 and the lowest quarterly volume since Q3 2004. Global M&A volume was US$1.2 trillion for the first half of 2020, a decrease of 42% from the first half of 2019 and the lowest first-half volume since 2013.

The decline in global M&A volume in Q2 2020 reflected a reduction in M&A volume in the United States, in large deals (transactions valued between US$1 billion and US$5 billion) and in mega deals (transactions valued at US$5 billion or greater), which had been primary drivers of the M&A boom over the prior several quarters.

Other regions of the world, however, experienced either less severe declines (Europe and India) or increases (Asia-Pacific (excluding Japan), the Middle East and Oceania) in Q2 2020 volumes as compared to Q1 2020.

Notably, Q2 2020 M&A volumes in Europe and China were each greater than US volumes - the first time since Q2 2012 for Europe and since data has been available for China.

Cross-border M&A activity in Q2 2020 exceeded Q1 2020 volume but remained low by recent historical levels as governments, central banks, executives and investors grappled with the continued effects of unprecedented shutdowns, rising unemployment, social unrest and economic uncertainty. Cross-border M&A volume was US$241 billion in Q2 2020, a 20% increase over Q1 2020, but an 11% decrease from Q2 2019.

The largest deals in Q2 2020 included National Commercial Bank's US$16 billion acquisition of Samba Financial Group and Liberty Global's US$13 billion acquisition of O2 Holdings.

View the XBMA's review here.

1.3 Monitoring Group publishes its recommendations to strengthen the international audit and ethics standard-setting system

14 July 2020 - The Monitoring Group has published its recommendations on Strengthening the International Audit and Ethics Standard-Setting System.

The Monitoring Group is a group of international financial institutions and regulatory bodies committed to advancing the public interest in areas related to international audit-related standard-setting and audit quality.

The Monitoring Group is responsible for the overall governance of the international audit and ethics standard-setting process and the review of its effectiveness. The set of recommendations fulfils the overall objective that the Monitoring Group set out when the effectiveness review began in 2015 - to strengthen international audit and ethics standard-setting to enhance its responsiveness to the public interest and improve audit quality.

Specifically, the recommendations are designed to achieve the following objectives:

- achieve an independent and inclusive, multi-stakeholder standard-setting system;
- reinforce the consideration of the public interest within the standard-setting process and throughout the full cycle of the standards' development, with enhanced independent oversight and standard-setting guided by the Public Interest Framework; and
- foster the development of timely, high quality standards that respond to an accelerating pace of change.

The recommendations include:

- all levels of the governance and oversight framework be subject to transparent accountability processes, including regular effectiveness reviews and enhanced reporting in the public domain;
- the Public Interest Oversight Board (PIOB) will provide oversight of the standard-setting process to ensure that international audit-related standards are responsive to the public interest, including that they are developed in accordance with the principles of the Public Interest Framework;
- international audit-related standard-setting activities will be undertaken in accordance with the Public Interest Framework; and
- standard-setting activities will be carried out by two expert and objective multi-stakeholder Boards.

Under the recommendations, the Public Interest Oversight Board will continue to have the critical role of providing independent oversight of the public interest responsiveness of audit and ethics standard setting. The Monitoring Group will work with the Public Interest Oversight Board and the standard-setting boards to achieve enhancements in the standard-setting system in the public interest and improvements in audit quality.

1.4 Proposals to modernise the Ontario capital markets

9 July 2020 - The Ontario Capital Markets Modernization Taskforce has published its consultation report, which contains 47 proposals aimed at modernising the regulation of the province's capital markets. The Minister of Finance of Ontario established the Taskforce in February 2020. The Taskforce was mandated to propose changes to improve Ontario's regulatory structure and reduce duplicative regulatory burden, while promoting investor protection and building a level playing field for a competitive economy.

Some of the proposals on which the Taskforce is consulting are as follows.

Improving regulatory structure

Expand the mandate of the Ontario Securities Commission (OSC) to include:

- fostering capital formation and competition in the markets;
- separate regulatory and adjudicative functions at the OSC; and
- strengthen the accountability framework through increased OSC oversight.

Regulation as a competitive advantage

- mandate that securities issued by a reporting issuer using the accredited investor prospectus exemption should be subject to only a seasoning period;
- introduce greater flexibility to permit reporting issuers, and their registered advisors, to gauge interest from institutional investors for participation in a potential prospectus offering prior to filing a preliminary prospectus;
- prohibit short selling in connection with prospectus offerings and private placements; and
- introduce additional Accredited Investor categories.

Ensuring a level playing field

- enact a prohibition on registrants benefiting from tying or bundling of capital market and commercial lending services, and a requirement for an attestation by a senior officer of the appropriate registrant under the applicable disclosure requirements;
- introduce a retail investment fund structure to pursue investment objectives and strategies that involve investments in early stage businesses; and
- improve corporate board diversity.

Proxy system, corporate governance and mergers and acquisitions

- introduce a regulatory framework for proxy advisory firms (PAFs) to: (a) provide issuers with a right to 'rebut' PAF reports, and (b) restrict PAFs from providing consulting services to issuers in respect of which PAFs also provide clients with voting recommendations; decrease the ownership threshold for early warning reporting disclosure from 10% to 5%;
- require TSX-listed issuers to have an annual advisory shareholders' vote on the board's approach to executive compensation;
- require enhanced disclosure of material environmental, social and governance (ESG) information, including forward-looking information, for TSX issuers; and
- amend securities law to provide additional requirements and guidance on the role of independent directors in conflict of interest transactions.

Fostering innovation

- create an Ontario Regulatory Sandbox in order to benefit entrepreneurs and start-ups;
- in the longer-term, consider developing a Canadian Super Sandbox; and
- allow for greater access to capital for start-ups and entrepreneurs.

Modernising enforcement and enhancing investor protection

- improve the OSC's collection of monetary sanctions;
- create a prohibition to effectively deter and prosecute misleading or untrue statements about public companies and attempts to make such statements;
- strengthen investigative tools by empowering OSC Staff to obtain production orders and enhancing compulsion powers;
- establish greater rights for persons or companies directly affected by an OSC investigation or examination;
- broaden the confidentiality exceptions available for disclosing an investigation and examination order or a summons; and
- require that amounts collected by the OSC pursuant to disgorgement orders be deposited into court for distribution to harmed investors in cases where direct financial harm to investors is provable.

1.5 IFAC and IIA statement on audit committees and COVID-19

8 July 2020 - As companies confront the immediate and longer-term implications of COVID-19, the Institute of Internal Auditors (IIA) and the International Federation of Accountants (IFAC) have issued a call for audit committees to ensure objective oversight of corporate activities, including risk management, performance, controls, and key processes.

The IIA and IFAC have developed specific recommendations for companies to more vigorously confront uncertainties that may threaten their integrity, transparency, and accountability.

The IIA and IFAC state that boards of directors and their audit committees must:

- **Stay informed:** maintain a timely and clear understanding of the continuously-evolving operating environment and how it may impact organisational objectives and performance.
- **Communicate and collaborate:** adopt a multi-disciplinary approach to exercising oversight of internal and external audit and reporting through dynamic communication and collaboration.
- **Leverage available expertise:** seek qualified and reliable assurance and advice on management evaluations of, and responses to, the organisation's continuously evolving risks and risk profile.
- **Promote continuous improvement:** encourage innovation and change to address vulnerabilities and to build resilience, strengthening the pursuit of value creation.
- **Think holistically:** adopt a broad perspective of the organisation and its environment across both financial and nonfinancial goals, considering interconnectivity with other organisations, internal and external interdependencies, and the central importance of people.
- **Embrace technology:** optimise the performance of the audit committee through the use of technology and flexible working practices.

The full statement is available on IFAC's website.

1.6 ESG disclosure by US public companies

6 July 2020 - The US Government Accountability Office (GAO) has published a report on disclosure of environmental, social and governance (ESG) information by US public companies. The report is titled Public Companies: Disclosure of Environmental, Social, and Governance Factors and Options to Enhance Them.

The report examines:

- why investors seek ESG disclosures;
- public companies' disclosures of ESG factors; and
- the advantages and disadvantages of ESG disclosure policy options.

Most institutional investors GAO interviewed said they seek information on ESG issues to better understand risks that could affect company financial performance over time. These investors added that they use ESG disclosures to monitor companies' management of ESG risks, to inform their vote at shareholder meetings, or to make share purchase decisions. Most of these institutional investors noted that they seek additional ESG disclosures to address gaps and inconsistencies in companies' disclosures that limit their usefulness.

GAO's review of annual reports, 10-K filings, proxy statements and voluntary sustainability reports for 32 companies identified disclosures across many ESG topics but also found examples of limitations noted by investors. Twenty-three of the 32 companies disclosed on more than half of the 33 topics GAO reviewed, with board accountability and workforce diversity among the most reported topics and human rights the least. Disclosure on an ESG topic may depend on its relevance to a company's business. Most companies provided information related to ESG risks or opportunities that were specific to the company, although some did not include this type of company-specific information.

Additionally, differences in methods and measures companies used to disclose quantitative information may make it difficult to compare across companies. For example, companies differed in their reporting of carbon dioxide emissions.

The report states that policy options to improve the quality and usefulness of ESG disclosures range from legislative or regulatory action requiring or encouraging disclosures, to private-sector approaches, such as using industry-developed frameworks. These options pose important trade-offs. For example, while new regulatory requirements could improve comparability across companies, voluntary approaches can provide flexibility to companies and limit potential costs.

1.7 UK: FRC principles for operational separation of audit practices

6 July 2020 - The United Kingdom (UK) Financial Reporting Council (FRC) has announced its principles for operational separation of the audit practices of the Big Four firms.

The objectives of operational separation are to ensure that audit practices are focused above all on delivery of high-quality audits in the public interest, and do not rely on persistent cross subsidy from the rest of the firm.

Desired outcomes include that:

- audit practice governance prioritises audit quality and protects auditors from influences from the rest of the firm that could divert their focus away from audit quality;
- the total amount of profits distributed to the partners in the audit practice does not persistently exceed the contribution to profits of the audit practice;
- the culture of the audit practice prioritises high-quality audit by encouraging ethical behaviour, openness, teamwork, challenge and professional scepticism/judgment; and
- auditors act in the public interest and work for the benefit of shareholders of audited entities and wider society.

These final principles follow extensive discussions with the audit firms. The FRC is now asking the Big Four firms to agree to operational separation of their audit practices on this basis and to provide a transition timetable to complete implementation by 30 June 2024 at the latest.

An implementation plan should be submitted to FRC by 23 October 2020. The FRC will then agree a transition timetable with each firm. Thereafter the FRC will publish annually an assessment of whether firms are delivering the objectives and outcomes of operational separation.

1.8 Board and executive remuneration report for ASX300 companies

3 July 2020 - Aon and the Governance Institute of Australia have released the results of the 2020 Board and Executive Remuneration Survey, which provides a snapshot of remuneration levels for directors and senior executives of ASX300 companies.

The report found that:

- almost two thirds of ASX300 organisations did not increase board fees in FY19;
- where there was an increase, the median increase for both chair and members was 4%; and
- for senior executives within the ASX300, median salary movement was 2.4%.

Survey snapshot

Board remuneration: A little over a third of the ASX300 provided some increase to board fees. However, in some of the large financial institutions, there were reductions in board fees in response to the negative investor sentiment towards their remuneration programs in addition to strong public disengagement particularly in the wake of some highly publicised corporate scandals and instances of malpractice.

The median increase in main board fees on a same-company basis for organisations which did provide one, being about a third of the total ASX300 sample, was observed to be 4% for both chair and members.

Executive remuneration: The median same-incumbent salary movement for senior executives over a 12-month period was observed to be 2.4%. This represents the movement from FY19 to

FY20, except where annual report disclosures were used to derive executive remuneration information. Median salary increase (fixed remuneration) for CEOs was recorded at a median of 1.8%. For the top ASX-listed organisations, however, the salary increases for CEOs were observed to be even more muted. The median CEO salary increase in the ASX50 was observed to be 0.2% while for the ASX51-100 it was 0.8%.

Board composition: Overall female representation on boards was observed to be 29% in the survey. Industries including Retail, Healthcare and Social Assistance, and Financial and Insurance Services are trending ahead of the overall survey median of 29%. The Metals and Mining industry fares the worst with a median female representation of 20%.

Board workload: The survey shows that at median, the ASX300 had 11 board meetings in FY19. However, the median for the Financial Services and Construction industries was observed to be slightly higher at 13 annual board meetings. For the Financial Services industry, while the median number of audit committee meetings recorded was five, in some of the large financial institutions, this figure was observed to be higher, as high as 19 in one instance. A similar observation was made with the meeting frequency of remuneration committees as well. While the overall median was again recorded at five meetings, remuneration committees of some of the large financial institutions met more frequently - as high as 22 meetings in one instance.

The impact of COVID-19 on salaries outside the ASX300

Many organisations have announced short-term changes to executive and director remuneration to mitigate the impact of COVID-19. Aon have analysed the recent ASX disclosures of 226 organisations, which revealed the following:

- 87% of companies announced they would reduce chair and NED fees by an average of 51%;
- 72% of organisations disclosed a reduction in CEO fixed remuneration by an average of 37%; and
- 85% of these announcements came from organisations outside of the ASX300 which appear to have been impacted more severely. Their pay reductions are also higher than others by approximately 10-15%.

1.9 AFCA receives more than 80,000 complaints in FY19/20, nearly 5,000 of which are COVID-19 related

2 July 2020 - Australians in dispute with their bank, insurer, super fund or financial firm have lodged more than 80,000 complaints in the last 12 months with the Australian Financial Complaints Authority (AFCA) securing $258.6 million in compensation and refunds direct to consumers.

People made 80,546 complaints to AFCA between 1 July 2019 and 30 June 2020. This is a 13.7% increase in monthly complaints compared to the last financial year (FY18/19).

AFCA resolved 78% of cases, with a majority being settled in 60 days or less. 73% of complaints were settled by agreement or in favour of the complainant, with banks being the most complained about financial institution.

Since COVID-19 was declared a pandemic in March, AFCA has received 4,773 complaints relating to COVID-19. Most of these complaints have been about general insurance claims (1,813) with more than 1,500 of these being travel insurance complaints.

The second most common issue for consumers was credit with 1,711 complaints, with almost a quarter of these being about a failure to respond to requests for assistance. There were also 791 COVID-19 complaints about superannuation, a majority of which related to early access of super.

More information about AFCA's operations for the financial year will be made available in AFCA's 2019/20 Annual Review, scheduled for release in the second half of 2020.

See AFCA's FY19/20 12-month snapshot here.

1.10 Basel Committee finalises AML/CFT guidelines on supervisory cooperation

2 July 2020 - The Basel Committee on Banking Supervision has issued the updated version of its guidelines on Sound management of risks related to money laundering and financing of terrorism, with guides on the interaction and cooperation between prudential and anti-money laundering and combatting the financing of terrorism (AML/CFT) supervisors.

These guidelines are intended to enhance the effectiveness of supervision of banks' money laundering and financing of terrorism risk management, consistent with and complementary to the goals and objectives of the standards issued by the Financial Action Task Force and principles and guidelines published by the Basel Committee.

The revisions set out principles and recommendations for information exchange and cooperation in relation to:

- authorisation related procedures of a bank;
- ongoing supervision; and
- enforcement actions.

Also, possible mechanisms to facilitate such cooperation in the jurisdictional and international contexts are provided.

1.11 FSB statement on the impact of COVID-19 on global benchmark reform

1 July 2020 - The Financial Stability Board (FSB) has discussed the impact of COVID-19 on global benchmark transition. The FSB's Official Sector Steering Group (OSSG) is monitoring the developments and recognises that some aspects of firms' transition plans are likely to be temporarily disrupted or delayed, while others can continue. The FSB maintains its view that financial and non-financial sector firms across all jurisdictions should continue their efforts in making wider use of risk-free rates in order to reduce reliance on Inter-bank Offered Rates where appropriate and in particular to remove remaining dependencies on the London Inter-bank Offered Rate (LIBOR) by the end of 2021.

LIBOR transition remains an essential task that will strengthen the global financial system. COVID-19 has highlighted that the underlying markets LIBOR seeks to measure are no longer sufficiently active. Moreover, these markets are not the main markets that banks rely upon for funding. The increase in the most widely used LIBOR rates in March put upward pressure on the financing cost of those paying LIBOR-based rates. For those borrowers, this offset in large part the reductions in interest rates in those jurisdictions where central banks have lowered interest rates.

Relevant national working groups are co-ordinating changes to intermediate milestones in their benchmark transition programmes, where appropriate, to ensure global coordination. Financial and other firms should continue to ensure that their transition programmes enable them to transition to LIBOR alternatives before end-2021.

LIBOR transition is a G20 priority, and the G20 in its February 2020 communique asked the FSB to identify remaining challenges to benchmark transition by July 2020 and to explore ways to address them. The FSB will publish a report on these issues. FSB members, in collaboration with other standard-setting bodies and international institutions, will continue to monitor developments.

1.12 FSB evaluation finds too-big-to-fail reforms made banks more resilient and resolvable, but gaps need to be addressed

28 June 2020 - The Financial Stability Board (FSB) has published for public consultation an evaluation of too-big-to-fail (TBTF) reforms for systemically important banks. The TBTF reforms were endorsed by the G20 in the aftermath of the 2008 global financial crisis and have been implemented in FSB jurisdictions over the past decade. The evaluation examines the extent to which the reforms are reducing the systemic and moral hazard risks associated with systemically important banks, as well as their broader effects on the financial system.

The key findings of the evaluation are as follows.

TBTF reforms have made banks more resilient and resolvable

- Systemically important banks are better capitalised and have built up significant loss-absorbing capacity. The capital ratios of global systemically important banks have doubled since 2011.
- Many FSB jurisdictions have introduced comprehensive bank resolution regimes and are carrying out resolution planning. This gives authorities a wide range of options for dealing with banks in stress.
- Evidence from market prices and credit ratings suggest that these reforms are seen as credible by market participants.

The benefits of the reforms significantly outweigh the costs

- Material negative side effects of the reforms have not been observed. Other market participants have stepped into areas where large banks have reduced their activities, while market fragmentation has not increased.
- On a conservative estimate of the probability and costs of financial crisis, the reforms have produced net benefits to society.

There are still gaps that need to be addressed

- Resolution of banks is a complex process, and some obstacles to resolvability remain. The FSB continues its work to make sure these are addressed and to encourage full implementation of the resolution reforms.
- Supervisors, firms and markets have much better information than before the implementation of the reforms, but reporting and disclosures could still be improved.

1.13 UK legislation to relieve burden on businesses during the COVID-19 outbreak

26 June 2020 - The UK *Corporate Insolvency and Governance Bill* received royal assent on 25 June 2020 and is now an Act. The measures in this Act will relieve some of the burdens on businesses during COVID-19.

Some of the measures in the Act came into effect immediately on 26 June 2020. Other measures came into effect on 27 June 2020 when the secondary legislation came into force.

The Act:

- introduces temporary measures for annual general meetings (AGMs) and filing requirements for public limited companies (PLCs);
- introduces new corporate restructuring tools to the insolvency regime to give companies the time they need to maximise their chance of survival; and
- temporarily suspends parts of insolvency law to support directors during COVID-19.

Under the secondary legislation, companies will receive an automatic extension for confirmation statements, registrations of charges (mortgage), and event-driven filings, such as a change to a company's directors or people with significant control.

View Corporate Insolvency and Governance Act.

1.14 IOSCO publishes good practices on processes for deference

26 June 2020 - The Board of the International Organization of Securities Commissions (IOSCO) has published a series of eleven Good Practices on Processes for Deference (the Good Practices) to assist regulatory authorities in mitigating the risk of unintended, regulatory-driven market fragmentation and to strengthen international cooperation.

Wholesale securities and derivatives markets are global in nature and many market participants operate on a cross-border basis. As a result, numerous authorities have implemented deference processes that allow them to rely on one another to regulate and supervise these market participants and help reduce potentially duplicative or conflicting regulations.

Over time, the use of deference between regulators has significantly increased, in parallel with enhanced cross-border capital flows. IOSCO's 2019 Report on Market Fragmentation and Cross-

Border Regulation, which was submitted to the G-20, suggested that IOSCO should identify good practices to enhance the processes for deference determinations further.

The aim of the eleven Good Practices identified in the report is to help members in establishing and operating efficient deference processes. They are underpinned by the philosophy that deference processes should be outcomes-based, risk-sensitive, transparent, sufficiently flexible and supported by strong cooperation.

They cover all phases of the deference process and focus on several key issues, including:

- arrangements for ensuring transparency of deference processes, including the scope, steps and criteria;
- the criteria for making an outcomes-based assessment of the assessed authority and/or firm, including the nature of the supervisory and enforcement practices in the assessed jurisdiction;
- important factors such as the nature and degree of risks that entities from another jurisdiction may pose in their markets;
- the level of engagement, cooperation and communication between the assessing authority and the assessed authority and/or firm throughout the process and once deference has been granted; and
- revocation of a deference determination.

IOSCO drew on the experience of the European Commission and members of the Committee on Payments and Market Infrastructures to develop these Good Practices.

1.15 Global coalition issues guidance on how businesses can adopt a long-term value creation agenda

25 June 2020 - In the wake of unprecedented economic disruption due to the COVID-19 pandemic, many companies are rethinking their fundamentals and assessing how their corporate purpose, strategy and business model will drive long-term success.

To support businesses in this uncertain environment, the International Federation of Accountants (IFAC), International Integrated Reporting Council (IIRC), and the Association of International Certified Professional Accountants (the unified voice of the American Institute of CPAs (AICPA) and the Chartered Institute of Management Accountants (CIMA)) have released new guidance for Chief Financial Officers (CFOs) and finance teams to navigate their organisations toward long-term value creation.

The report contains actionable insights for CFOs, finance teams, and other business leaders to sharpen their perspective on value creation beyond the financials, including how to do the following:

- understand the value creation process;
- identify principal opportunities and risks related to the organisation's strategy and business model;
- develop an integrated view of performance and value, incorporating balance sheet, business, and societal perspectives; and
- drive priorities for value creation into decision making and reporting.

The approach outlined in the report helps CFOs and finance teams to think about how to ensure that all relevant information around performance, opportunities, risks, and trade-offs are available to internal decision-makers, investors, and other capital providers.

1.16 CPMI-IOSCO publish a report on CCP auctions

25 June 2020 - The Committee on Payments and Market Infrastructures (CPMI) and the International Organization of Securities Commissions (IOSCO) have published a report entitled Central counterparty default management auctions - Issues for consideration.

The report outlines certain issues that central counterparties (CCPs) should consider regarding default management auctions processes. It also identifies practices that CCPs could consider in the development and improvement of default management auctions to address those issues.

CCPs have become increasingly important in recent years and play an important role in mitigating contagion in the event of a participant default. A CCP's ability to effectively manage the default of its participants is essential to its resilience and can help reduce systemic risk. A default management auction is one of the tools that a CCP may use to transfer a defaulting participant's positions to non-defaulting participant(s), thereby restoring the CCP to a matched book.

The report builds on a discussion paper on CCP default management auctions published in June 2019. The responses to the discussion paper indicated considerable industry consensus on a variety of topics related to default management auctions. However, on a number of additional issues, further work among industry participants towards consensus is necessary for effective auction practices and procedures to be developed.

The report is accompanied by a cover note. CPMI and IOSCO will work with the industry to progress some issues related to CCP default management auctions over the next 24 months. At the end of this timeframe, CPMI and IOSCO intend to take stock of industry progress towards consensus on those issues as well as towards implementation of concrete measures (where relevant) and reconsider whether additional work, potentially including guidance, would be necessary.

1.17 IOSCO consults on AI/ML guidance for market intermediaries and asset managers

25 June 2020 - The IOSCO Board is requesting feedback on proposed guidance to help its members regulate and supervise the use of Artificial Intelligence (AI) and Machine Learning (ML) by market intermediaries and asset managers.

The use of these technologies may benefit firms and investors, such as by increasing execution speed and reducing the cost of investment services. However, it may also create or amplify risks, potentially undermining financial markets efficiency and causing harm to consumers and other market participants.

Consequently, regulators are focusing increasingly on the use and control of AI and ML in financial markets to mitigate the potential risks and prevent consumer harm. In 2019, the IOSCO Board identified AI and ML as an important priority.

The consultation report on The use of artificial intelligence and machine learning by market intermediaries and asset managers proposes six measures to assist IOSCO members in creating appropriate regulatory frameworks to supervise market intermediaries and asset managers that use AI and ML.

The proposed measures seek to ensure that market intermediaries and asset managers have the following features:

- appropriate governance, controls and oversight frameworks over the development, testing, use and performance monitoring of AI and ML;
- ensuring staff have adequate knowledge, skills and experience to implement, oversee, and challenge the outcomes of the AI and ML;
- robust, consistent and clearly defined development and testing processes to enable firms to identify potential issues prior to full deployment of AI and ML; and
- appropriate transparency and disclosures to investors, regulators and other relevant stakeholders.

The proposed guidance reflects the standards of conduct expected of market intermediaries and asset managers using AI and ML. Although the guidance is not binding, IOSCO members are encouraged to consider the proposed measures carefully in the context of their legal and regulatory frameworks.

To prepare the report, IOSCO surveyed and discussed AI and ML with market intermediaries and asset managers. The report analyses how firms use this technology, identifies the risks involved and describes how firms address them. It also includes a chapter on guidance for AI and ML published by supranational organisations, such as the International Monetary Fund and the Financial Stability Board.

1.18 FMSB issues new statement of good practice on algorithmic trading

24 June 2020 - The FICC Markets Standards Board (FMSB) published a new Statement of good practice for FICC market participants on algorithmic trading in FICC markets as a transparency draft for market consultation.

As the use of computer algorithms in FICC (fixed income, currencies and commodities) markets continues to increase, the potential for such trading activities to adversely impact market or firm stability, or result in harm to clients, also rises. Accordingly, algorithmic trading has increasingly been the subject of regulatory scrutiny and intervention.

This Statement of Good Practice draws on the extensive work conducted by regulators to date and seeks to further enhance the integrity and effective functioning of FICC markets by promoting good conduct and governance practices for participants engaged in algorithmic trading across all FICC asset classes and markets, in particular those subject to less stringent regulatory requirements.

It sets out ten Good Practice Statements which cover the governance of, and management of conduct risks associated with, the use of algorithmic trading.

1.19 OECD publishes report on duties and responsibilities of boards in company groups

3 June 2020 - The OECD has published a report on the Duties and Responsibilities of Boards in Company Groups.

The publication provides an overview of the duties and responsibilities of boards in company groups across 45 jurisdictions. The introduction outlines the global landscape of company groups, their economic role and the principal challenges they present with respect to corporate governance polices.

Part I develops a typology of legal and regulatory approaches that jurisdictions have taken to address these challenges.

Part II highlights differences and commonalities across jurisdictions, especially as they relate to the following:

- how directors may take into account group interests; procedures for managing conflicts of interest;
- compensating losses incurred by a group company for the benefit of the group;
- transparency around group purposes and allocation of business opportunities; and
- allocation of responsibility for company policy and oversight between parent and subsidiary boards.

Additional chapters offer case studies of recent and specific approaches to company group governance in Colombia, India, Israel and Korea.

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2. Recent ASIC Developments

2.1 Minor updates to Regulatory Guide 97

24 July 2020 - ASIC has released minor amendments to the fees and cost disclosure regime for issuers of superannuation and managed investment products.

A major update of Regulatory Guide 97 - Disclosing Fees and Costs in PDSs and Periodic Statements (RG 97) and the associated legislative instrument were released in November 2019. ASIC has slightly amended RG 97 and the instrument to adjust the transitional timeframes in response to COVID-19 and to provide greater clarity on the obligations following additional feedback from industry.

Key changes ASIC has amended the transitional arrangements for product disclosure statements (PDSs) in response to COVID-19:

- PDSs given on or after 30 September 2022 must comply with the new requirements;
- issuers can choose to apply the new requirements from 30 September 2020; and
- once an issuer has elected to apply the new requirements, all subsequent PDSs for that financial product must comply with the new requirements.

There is no change to the transition arrangements for periodic statements.

Minor technical refinements have been made to confirm ASIC's policy positions in relation to:

- the disclosure of buy/sell spreads in periodic statements for collective investment products under Class Order [CO 14/1252];
- disclosure of performance fees;
- the identification and treatment of derivative costs; and
- significant event notice requirements.

ASIC has also clarified some definitions and amended the "Consumer advisory warning" and "Example of annual fees and costs" to correct inconsistencies between the templates in the legislative instrument and RG 97.

To give effect to these amendments ASIC has released:

- RG 97 (updated 24 July 2020);
- ASIC Corporations (Disclosure of Fees and Costs) Instrument 2019/1070; and
- ASIC Corporations (Amendment and Repeal) Instrument 2020/579, which amends ASIC Corporations (Disclosure of Fees and Costs) Instrument 2019/1070.

2.2 Consultation on second product intervention order to stop continuing consumer harm

9 July 2020 - ASIC has released Consultation Paper 330 (CP 330) on the proposed use of its product intervention power to address significant detriment it has identified in the continuing credit industry.

This proposed intervention follows the product intervention order that ASIC made in September 2019, which banned the provision of a class of financial products, namely short-term credit products, unless specified conditions were complied with in relation to fees and charges.

In monitoring the effect of the short-term credit intervention, ASIC has identified another class of financial products, namely continuing credit products, being issued to borrowers.

ASIC is concerned that the continuing credit products are likely to result in significant detriment due to borrowers incurring very high cost, relative to the loan amount. ASIC is also concerned that continuing credit products are being issued to vulnerable clients, including many who are already in financial difficulty.

While ASIC is aware of two firms currently engaging in the concerning conduct, the proposed product intervention order would apply to any business engaging in the concerning conduct.

2.3 ASIC issues no-action position to allow right-of-use lease assets to count in satisfying AFS licensee requirements

7 July 2020 - ASIC has issued a temporary no-action position for Australian financial services (AFS) licensees in relation to potential breaches of the financial resource requirements that arise from recent changes to the accounting treatment of lease assets. The no-action position will apply until further notice.

AFS licensees are required to maintain adequate resources, including financial resources, to provide services under the terms of their licences. ASIC recognises that some AFS licensees may face difficulty in complying with their financial resource requirements because, following changes to the accounting standards for leases, lessees are required to recognise lease liabilities and a right-of-use asset for all leases. While the lease liabilities are taken into account for the purposes of an AFS licensee's financial resource requirements, the right-of-use assets are now generally treated as intangible assets and do not count towards meeting those requirements.

By issuing the temporary no-action position, ASIC will do the following:

- allow licensees to use right-of-use lease assets to count towards their financial resource requirements; and
- not take regulatory action against licensees in relation to past breaches of financial resource requirements, when the breach arises from right-of-use lease assets not being able to be counted towards meeting those requirements.

ASIC plans to consult on proposals to change the financial resource requirements to enable an AFS licensee to include a right-of-use lease asset when calculating whether it meets its financial resource requirements.

Further information is available at No-action position to allow right-of-use lease assets to count in satisfying AFS licensee requirements.

2.4 Focuses for financial reporting under COVID-19 conditions

7 July 2020 - ASIC has provided further information on focus areas for financial reporting in the COVID-19 environment for years ending 30 June 2020 following its guidance via the frequently asked questions already published on the ASIC website.

Focus areas for 30 June 2020

Given the adverse impacts on many entities from the COVID-19 pandemic, directors, preparers and auditors should focus on asset values, provisions, solvency and going concern assessments, events occurring after year end and before completing the financial report, and disclosures in the financial report and Operating and Financial Review (OFR).

Entities may face some uncertainties about future economic and market conditions, and the future impact on their businesses. Assumptions underlying estimates and assessments for financial reporting purposes should be reasonable and supportable. Assumptions should be realistic, and not overly optimistic or pessimistic.

Useful and meaningful disclosures about the business impacts and potential uncertainties will be vital. Uncertainties may lead to a wider range of valid judgments on asset values and other estimates. Disclosures in the financial report about uncertainties, key assumptions and sensitivity analysis will be important to investors.

The OFR should complement the financial report and tell the story of how the entity's businesses are impacted by the COVID-19 pandemic. The underlying drivers of the results and financial position should be explained, as well as risks, management strategies and future prospects.

ASIC surveillances

ASIC will review the full-year financial reports of about 200 larger listed entities and other public interest entities as at 30 June 2020. ASIC's reviews will focus on entities and industries adversely affected by the current conditions. ASIC will also review the adequacy of disclosure by some entities whose businesses have been positively affected.

The reporting process

Appropriate experience and expertise should be applied in the reporting and audit processes, particularly in more difficult and complex areas, such as asset values and other estimates.

Directors and auditors should be given sufficient time to consider reporting issues and to challenge assumptions, estimates and assessments.

Directors should make appropriate enquiries of management to ensure that key processes and internal controls have operated effectively during periods of remote work. Auditors may need to amend their procedures for remote work (for example, virtual stock counts and system walk-throughs) and where there are changes in the design or effective operation of internal controls.

Reporting deadlines

ASIC has extended the deadline for both listed and unlisted entities to lodge financial reports under Chapters 2M and 7 of the Corporations Act 2001 No. 50 (Cth) by one month for certain balance dates up to and including 7 July 2020 balance dates.

Where possible, entities should continue to lodge within the normal statutory deadlines having regard to the information needs of shareholders, creditors and other users of their financial reports, or to meet borrowing covenants or other obligations.

Frequently asked questions

ASIC's frequently asked questions on the impact of COVID-19 on financial reports and audits (see ASIC COVID-19 implications for financial reporting and audit: Frequently asked questions (FAQs)) provide additional information on matters such as the following:

- focus areas and factors to consider;
- disclosures in the financial report and OFR;
- the use of non-IFRS financial information;
- half-year report disclosures;
- director liability;

- loan and receivable provisioning;
- lessor accounting for rent concessions;
- the solvency statement by directors;
- the extensions of time for financial reporting;
- the "no action" position on the timing of AGMs;
- virtual meetings; and
- reporting by auditors.

The FAQs may be updated from time to time in response to emerging issues and changing circumstances.

2.5 ASIC approves temporary COVID-19 changes to the Banking Code

25 June 2020 - ASIC has approved a variation of the *Banking Code of Practice* (the Code).

The variation, as proposed by the Australian Banking Association (ABA), involves the insertion of a Special Note into the Code to allow for special application of specified Code provisions until 1 March 2021. The ABA has proposed the variation due to the extraordinary external environment caused by COVID-19.

The ABA has published the updated version of the Code, including the Special Note.

The updated Code can be found on the ABA's website.

ASIC approved the Code in December 2019, for commencement on 1 March 2020.

View:

- ASIC Corporations (Approval of Variation of March 2020 Banking Code of Practice) Instrument 2020/602
- Explanatory statement

2.6 New regulatory guidance for mortgage brokers

24 June 2020 - ASIC has published regulatory guidance to assist in the application of the new best interests duty for mortgage brokers, which comes into effect in 2021.

The new obligations were legislated by the Parliament in response to Recommendation 1.2 of the Financial Services Royal Commission. From 1 January 2021, mortgage brokers will be required to act in the best interests of consumers and to prioritise consumers' interests when providing credit assistance.

Consistent with this legislation, the guidance is high level and principles-based, but also incorporates practical worked examples. The purpose of the guidance is to explain the obligations introduced by the federal government - it does not prescribe minimum standards of conduct, nor does it impose new or additional obligations.

Regulatory Guide 273 - Mortgage brokers: Best interests duty (RG 273) contains ASIC's views on how mortgage brokers may comply with their best interests obligations at key stages of the credit assistance process. It provides guidance on the effect of the range of credit providers and products brokers can access, recommending packages of credit products, and the types of records that may be kept to demonstrate compliance.

From 1 January 2021, ASIC will closely monitor conduct and outcomes to ensure mortgage brokers are complying effectively with the best interests duty.

Alongside the new guidance, ASIC has also published a report responding to feedback received during the consultation process.

View:

- Regulatory Guide 273 Mortgage brokers: Best interests duty
- Report 662: Response to submissions on CP 327 on mortgage brokers and the best interests duty
- Submissions to CP 327

2.7 Decisions on applications for relief - October 2019 to March 2020

23 June 2020 - ASIC has granted over 600 applications for relief between 1 October 2019 and 31 March 2020.

ASIC's latest report, Report 664 - Overview of decisions on relief applications (October 2019 to March 2020) (REP 664), outlines decisions on relief applications and highlights ASIC's efforts to reduce red-tape and achieve a practical, positive outcome for companies seeking regulatory flexibility, without harming stakeholders.

During the report period, ASIC granted relief from provisions of the Corporations Act 2001 No. 50 (Cth) or the National Consumer Credit Protection Act 2009 No. 134 (Cth) in relation to 619 applications.

The granting of relief, which has a net regulatory benefit, or which facilitates business or cuts red tape, is an important part of ASIC's regulatory function. The reporting of ASIC's decisions on relief applications aims to provide transparency about decision making and to better inform businesses about the circumstances in which ASIC will grant relief.

REP 664 lists publications released by ASIC during the period that may be relevant to prospective applicants for relief.

The report also provides examples where ASIC has exercised, or refused to exercise, its exemption and modification powers under the Corporations Act.

During, and subsequent to, the report period ASIC has provided facilitative individual and class relief to mitigate the impacts on business of the COVID-19 pandemic and the associated containment measures.

REP 664 includes summaries of selected individual relief decisions, publications and legislative instruments which relate to COVID-19. These relief decisions and publications concern disclosure, financial reporting, AGMs and registered office closure.

ASIC will continue to take a facilitative approach, where appropriate, to the provision of individual and class relief to assist business in dealing with the challenges associated with the COVID-19 pandemic and the associated containment measures.

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3. Recent ASX Developments

3.1 Public consultations - CHESS replacement revised implementation timetable

On 30 June 2020, ASX released its consultation paper on the CHESS Replacement Revised Implementation Timetable. The paper sets out key project activities and milestones including system development and testing, user testing, technical accreditation, operational readiness, and operating rule amendments.

The revised timetable has been produced to provide additional time for the ongoing impact of the COVID-19 pandemic on all stakeholders, accommodate functionality changes requested by users, and have a longer period for users to complete their development and readiness activities. The new proposed go-live date is April 2022.

The consultation paper is available on the ASX website.

3.2 ASX COVID-19 measures: Temporary emergency capital raising relief

On 31 March 2020, ASX introduced temporary emergency capital raising measures (by way of class waivers) to help listed entities affected by the COVID-19 pandemic to raise urgently needed capital. These measures were due to expire on 31 July 2020.

On 9 July 2020, ASX announced that it has decided to extend its temporary emergency capital raising measures until 30 November 2020. The decision was made in light of the high and increasing levels of COVID-19 infections in major overseas markets, recent events in Victoria, and the present uncertainty about the nature and level of government economic stimulus in Australia after September 2020.

The media release is available on the ASX website.

3.3 ASX24 - 5 year treasury bond futures contract

On 26 June 2020, ASX announced that it intends to list a 5 Year Treasury Bond Futures contract on the ASX24 market in late Q4 2020, subject to regulatory approval and internal/external readiness.

The contract will provide an additional liquidity point and hedging tool at the 5 year point on the curve, allowing participants to manage their risk exposure in a more efficient and effective manner.

The media release is available on the ASX website.

3.4 Reports

On 6 July 2020, ASX released the ASX Monthly Activity Report for June 2020.

4. Recent Takeovers Panel Developments

4.1 Webster Limited - Panel declines to make declaration

15 July 2020 - The Takeovers Panel has declined to make a declaration of unacceptable circumstances in response to an application dated 28 June 2020 from Winpar Holdings Limited (Winpar) in relation to the affairs of Webster Limited (Webster). The application concerned whether Winpar had validly objected to Henslow Acquisitionco Pty Ltd's (Henslow) proposed compulsory acquisition of Webster's preference shares pursuant to Part 6A.2 of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) (see TP20/38).

The Panel considered (among other things) that, having regard to the underlying policy of the compulsory acquisition provisions in Part 6A.2 of the Corporations Act and the need to have a clear and finite objection period that is able to be assessed by the 90% holder, Henslow proposing to proceed with compulsory acquisition without court approval is not unacceptable. The Panel also considered that Winpar has other avenues available to it, including applying to ASIC for relief or seeking orders from the Court under s. 1322(4) of the Corporations Act to remedy the procedural defect.

The Panel considered that it is not against the public interest to decline to make a declaration of unacceptable circumstances.

On the basis of the above, the Panel decided not to make a declaration of unacceptable circumstances.

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

4.2 Moreton Resources Limited (Administrators Appointed) 02 - Panel declines to conduct proceedings

15 July 2020 - The Takeovers Panel has declined to conduct proceedings on an application dated 10 July 2020 from Alexander Jason Elks in relation to the affairs of Moreton Resources Limited (Administrators Appointed).

The application concerned, among other things, whether certain shareholders of Moreton were associated and had contrived the appointment of administrators to Moreton and certain of its subsidiaries in order to move the assets and interests of Moreton, 'thereby failing to allow a free, transparent and open market to operate' (see TP20/41).

The Panel considered, among other things, that the applicant did not provide the Panel with a sufficient body of material for the Panel to examine whether the administration was a device for any person to gain control of Moreton or subvert the operation of Chapter 6 of the Corporations Act 2001 No. 50 (Cth) or to otherwise justify the Panel making further enquiries, including as to whether an association exists or existed between the relevant shareholders.

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

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

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5. Recent Research Papers

5.1 The 'safe harbour' reform of directors' insolvent trading liability in Australia: Insolvency professionals' views

Directors of Australian companies are subject to a duty to prevent their company trading whilst it is insolvent. The duty is controversial. Over a period of at least ten years, a series of reforms have been proposed, leading up to the introduction, in 2017, of a safe harbour for directors where directors undertake a restructure of the company outside of external administration. There are important questions relating to the safe harbour reform. To assist in answering these questions, the authors undertook a survey of insolvency professionals. The authors had three main goals in undertaking the survey - to obtain insight into the experience of practitioners with the safe harbour reform, to obtain the views of these practitioners on whether the reform has achieved its objectives, and to obtain their views on whether any changes should be made to the safe harbour provisions in light of the independent review of the reform that the Government is required to commission.

The 'Safe Harbour' Reform of Directors' Insolvent Trading Liability in Australia: Insolvency Professionals' Views

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5.2 The spread of Covid-19 disclosure

Investors rely on corporate disclosure to make informed decisions about the value of companies they invest in. The COVID-19 pandemic provides a unique opportunity to examine disclosure practices of companies relative to peers in real time about a somewhat unprecedented shock that impacted practically every publicly listed company in the U.S. The authors examine how companies respond to such a situation, the choices they make, and how disclosure varies across industries and companies.

The authors ask: What motivates some companies to be forthcoming about what they are experiencing, while others remain silent? Do differences in disclosure reflect different degrees of certitude about how the virus would impact businesses, or differences in management perception of its obligations to shareholders? What insights will companies learn to prepare for future outlier events?

The Spread of Covid-19 Disclosure

5.3 Global economic impact of COVID-19: Evidence from insider trades

The authors examine insider trades around the onset of the COVID-19 pandemic. Insiders purchased shares in record numbers after the stock market decline that began in late February 2020. The authors find that insider purchases were more pronounced for larger firms, value firms, firms with high levels of leverage as well as firms in the finance, energy and consumer nondurable sectors. These results suggest that insiders believe the impact of COVID-19 on global economic activity and the stock prices of their companies to be temporary. The authors also find some evidence of opportunistic insider selling in January and February 2020 prior to the stock market decline, suggesting that some insiders anticipated the decline. Finally, they find similar patterns in insider trading in Canada, Italy, Spain and South Korea, but a more muted response in China. The results indicate that insiders' private information became especially valuable during this period of significant market disruption.

Global Economic Impact of COVID-19: Evidence from Insider Trades

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5.4 What do we know about audit failure so far?

This article presents a comprehensive review of academic research pertaining to audit failure. This literature review is based on auditing-related articles published in leading journals during the 1976 - 2019 period. The authors organise their review around three main groups, namely (a) proxy measures of audit failure, (b) causes of audit failure, and (c) effects of audit failure. They observe that the literature uses a variety of proxies to capture audit failure, such as auditors' going concern opinions (GCOs), material misstatements, auditor communication, financial reporting quality, and perceptions. They find that there are three signals of audit failure: non-issuance of a GCO prior to a business failure, material misstatements in the last audited financial statements, and violation of the code issued by regulators. They find that audit failures reduce clients' market value and the auditor's ability to retain clients. There is also evidence that larger penalties for audit failure result in higher audit fees and overinvestment in audit effort and that increased liability decreases audit failure and reduces auditor shirking. A related objective of this paper is to shed light on audit failure by Big N and non-Big N auditors separately. The authors observe that the audit failure rate is lower for Big N auditors than for non-Big N auditors.

What Do We Know About Audit Failure so Far?

5.5 Conflicts and coherence in the charities sphere: Would a conflict by any other name proscribe the same?

Proscriptions on conflicts of interest have long been a core component of governance regimes. In the charities sphere such proscriptions arise from a number of sources, including general law, statute and governance standards articulated by the regulator. Unfortunately the wording of relevant conflicts duties varies extensively, giving rise to acute incoherence and uncertainty. This article undertakes detailed critical analysis of the myriad of conflicts duties in order to provide certainty and comprehensive guidance. This resolution is relevant beyond the charitable sphere given the multitude of ways in which conflicts proscriptions are expressed in other governance contexts.

Conflicts and Coherence in the Charities Sphere: Would a Conflict By Any Other Name Proscribe the Same?

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6. Recent Corporate Law Decisions

6.1 Ellerston Global ordered to convene shareholder vote on scheme of arrangement to exchange shares for fund units, subject to KYC information

(By Rodd Levy, Herbert Smith Freehills)

In the matter of Ellerston Global Investments Limited [2020] NSWSC 879 (8 July 2020), Supreme Court of New South Wales, Black J

(a) Summary

Ellerston Global Investments' (EGI) proposed restructure by way of scheme of arrangement has proceeded to the next stage after the Supreme Court of New South Wales made orders to convene a shareholder meeting. The restructure aims to appeal to shareholders who seek liquidity at a price closely approximate to the underlying asset value of the company as well as seek to remain within EGI's investment strategy.

To do this, the scheme proposes a one-for-one exchange of EGI shares for units in the Ellerston Global Mid Small Cap Fund (Fund), controlled by EGI's associated entity, Ellerston Capital Limited (ECL). The exchange is subject to EGI shareholders providing Know Your Customer (KYC) information prior to units being issued. Despite the relative complexity of the proposed scheme, Black J was satisfied that it sufficiently protects EGI shareholders from any associated performance risks. In light of the COVID-19 pandemic, the court made orders to convene the shareholder meeting virtually.

(b) Facts

On 17 February 2020, EGI announced it had entered into a Scheme Implementation Deed with ECL in relation to the restructure.

On 26 May 2020, EGI proposed two further amendments to the scheme to:

- require shareholder approval to the related party benefit of an early termination fee under Ch 2E of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act); and
- introduce provisions addressing performance risk of EGI shareholders by providing a mechanism for ECL to acquire future units in the Fund where shareholders failed to comply with KYC requirements (the KYC Amendment).

The KYC Amendment proposed:

- a condition precedent requiring at least 75% of shareholders to handover KYC information by a specified date, with the scheme not proceeding if the threshold was not achieved by that date; and
- that if shareholders failed to provide KYC information by that date, the units would be transferred to an independent custodian, appointed by EGI, to hold them on behalf of those shareholders for a further period. If information is still not provided by end of extension date, the independent custodian can request withdrawal of units and hold the proceeds of withdrawal.

In making the application, counsel for EGI noted there should only be one class of EGI shareholders for voting purposes at the meeting. Variances arose due to a shareholder, Ashok Jacob, being a non-executive director of EGI and a director/shareholder of ECL, and ECL holding a significant number of shares in EGI.

EGI applied to the Court under s. 411 of the Corporations Act for an order to convene a shareholder meeting and consider:

- the Scheme amendments containing the performance risk provisions; and
- whether there should be one class of EGI shareholders for voting purposes.

(c) Decision

Black J ordered EGI convene a shareholder meeting to vote on the scheme. His Honour was satisfied that if the proposed scheme received statutory majority at the meeting, the Court was likely to approve the scheme of arrangement.

In coming to this decision, Black J primarily focused on whether the scheme is adequately explained to those who have a financial interest in it, and if there are any obvious flaws in the scheme that render it inappropriate for consideration, referencing *Re Abacus Funds Management Ltd* [2005] NSWSC 1309 and *Re Villa World* [2019] NSWSC 1207.

His Honour summarised the standard factors the Court will consider in making an order to convene a scheme meeting, including that:

- the proposed scheme fell under the definition of an 'arrangement' contained in s. 411 of the Corporations Act;
- there was proper disclosure to shareholders;
- the scheme is bona fide and properly proposed;
- ASIC had reasonable opportunity to examine the terms of the scheme and appropriately respond within the requisite time frame;
- the procedural requirements in the Supreme Court (Corporations) Rules 1999 No. 703 (NSW) were followed; and
- there is no apparent reason why the scheme should not receive the Court's approval at second instance.

(i) Performance risk provisions

The Court was satisfied the approach addressed the relevant performance risk that the acquirer will not comply with its obligation to pay the scheme consideration to shareholders of the scheme company - namely, to the extent the scheme ensures EGI shares are not acquired by ECL unless it has allocated units to shareholders who have provided KYC information, or to the independent custodian if KYC information has not been provided.

In particular, his Honour noted the correspondence between ASIC and EGI's legal representatives in late May and early June, discussing whether shareholder approval of the early termination fee would have a 'coercive' impact on EGI shareholders, and if EGI could remit cash proceeds of redemption of units to EGI shareholders who had not provided KYC information after the initial period.

EGI contended that shareholder approval of the early termination fee reflected a single integrated proposal of the scheme, and that shareholders who did not believe the benefits of the scheme outweighed the detriment of the Early Termination Fee could vote against the scheme. They further noted ECL and the independent custodian would not pay proceeds of redemption of units without first receiving KYC information, if doing so would constitute an avoidance of their respective obligations under the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 No. 169 (Cth) (the AML/CTF Act).

This argument was accepted by the Court with Black J noting that despite the proposed scheme being a complex commercial arrangement, EGI and ECL's approach was of a satisfactory standard. His Honour held that the restructure appropriately balanced competing considerations of protecting shareholders from any performance risks, against the constraints of the AML/CTF Act and avoiding shareholder hostility. The Court was also satisfied with the nature of the Scheme, the disclosure of terms and verification process and that an independent expert concluded the Scheme was fair, reasonable and in the best interest of EGI shareholders. Therefore, if the scheme received statutory majority at the meeting, his Honour noted it could be reasonably approved by the Court.

(ii) Class issues

With reference to a number of authorities, including *Re Healthscope Ltd* [2019] FCA 542, Black J considered whether the rights of shareholders are so dissimilar it makes it impossible to consult them together with a view to their common interest.

Ultimately, Black J accepted EGI's position that neither Mr Jacob nor ECL should be treated as a different classes of shareholder for voting purposes, but noted EGI would 'tag' the votes of Mr Jacob and ECL so that the impact of their votes could be assessed at the second Court hearing.

(iii) Other considerations

Having regard to the COVID-19 pandemic and restrictions imposed in New South Wales, the Court permitted the meeting to be held virtually. This decision was made with reference to *Re TPG Ltd* [2020] NSWSC 772.

Pursuant to the explanatory booklet, scheme shareholders in foreign jurisdictions will be treated as ineligible foreign shareholders, with their units to be issued to the independent custodian who will subsequently exercise their withdrawal rights. His Honour accepted that this approach is consistent with previous authorities, and that foreign shareholders did not create a separate class for voting purposes. In any event, no shareholders presently fall into this category.

His Honour deemed it unnecessary to consider exclusivity arrangements and the terms of the ECL unit offer. He further noted matters of court approval of the explanatory statement under s. 411(1) of the Corporations Act and whether shareholders registered in the United States can participate in the Scheme are for consideration at the second Court hearing.

6.2 Orders to make the sale of the Virgin companies fly
(By Elaine Stops, DLA Piper)

Strawbridge, in the matter of Virgin Australia Holdings Ltd (administrators appointed) (No 4) [2020] FCA 927 (2 July 2020), Federal Court of Australia, Middleton J

(a) Summary

To assist in the completion of the sale of the Virgin companies to Bain Capital the Plaintiffs sought a number of orders:

- to limit the liability of the Administrators of the Virgin companies;
- to keep certain terms of the sale confidential; and
- to alter the time for the registration of the security interests.

(b) Facts

On 1 July 2020, the Plaintiffs filed an application to the court seeking orders pursuant to s. 447A(1) of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act), regarding the liabilities of the Administrators under s. 443A(1) and the time for registration of security interests under s. 588FM. Section 447A(1) of the Corporations Act empowers the Court to make orders determining how Part 5.3A operates in relations to a particular company - s. 443A(1) indicates that the Administrators of a company are liable for the debts they incur in the performance of their duties as an Administrator, and s. 588FM enables a company or interested party to apply to the Court for an order making a later time for the registration of a security interest so that it does not automatically vest in the company.

The Plaintiffs sought to limit the personal liability of the Administrators regarding any monies advanced, and obligations, if the sale of the Virgin companies (the Companies) to Bain Capital did not complete (the Transaction). The Transaction documents were signed by Bain Capital on 26 June 2020, and agreed that the Administrators' liability should be limited to the assets of the Companies.

The Plaintiffs also sought orders under s. 37AF(1)(b) of the Federal Court of Australia Act 1976 No. 156 (Cth) (the FCA Act) to keep the terms of the Transaction, and other documents in connection with the Transaction confidential and prohibited from public disclosure. Section 37AF(1)(b) of the FCA Act empowers the court to make a suppression order prohibiting the publication of certain information that relates to a proceeding before the Court.

(c) Decision

Middleton J made orders regarding the confidentiality of the Transaction, as requested by the Plaintiffs, on the basis that the Transaction could be prejudiced if the information was released and could cause harm to the parties.

In making his decision regarding the application of ss. 443A and 447A of the Corporations Act, Middleton J referred to the principles he set out in his judgment in *Strawbridge, in the matter of Virgin Australia Holdings Ltd (administrators appointed) (No 2)* [2020] FCA 717. He acknowledged that orders regarding this were commonly sought and made orders limiting the personal liability of the Administrators as per the terms of the Transaction. He justified this on the basis that it was in the best interests of the creditors and the Companies. He further added that unsecured creditors would not be disadvantaged by this order because it would only be limiting the Administrators from personal liability.

Middleton J made further orders regarding the time for the registration of security interests on the basis that this would not cause prejudice to creditors and would be just and equitable. This decision was further supported by Middleton J on the basis that it was necessary to fund the administration period. He made orders altering the time for the registration of the security interest in the collateral to be 24 July 2020, 20 business days after the date that the document that gives rise to the security interests comes into effect.

6.3 ASIC's appeal against responsible lending decision fails
(By Kate Hilder and Mark Standen, Minter Ellison)

Australian Securities and Investments Commission v Westpac Banking Corporation [2020] FCAFC 111 (26 June 2020), Federal Court of Australia, Full Court, Middleton, Gleeson and Lee JJ

(a) Summary

On 13 August 2019, Perram J handed down his landmark decision on the boundaries of responsible lending obligations in *Australian Securities and Investments Commission v Westpac Banking Corporation (Liability Trial)* [2019] FCA 1244. The case was brought by the Australian

Securities and Investments Commission (ASIC) as a test case, to provide 'judicial clarification of a cornerstone legal obligation on lenders'.

In dismissing ASIC's case, Perram J held that a lender 'may do what it wants in the assessment process' and is not obliged under the responsible lending provisions of the National Consumer Credit Protection Act 2009 No. 134 (Cth) (the NCCP Act), to take into account a prospective borrower's actual/declared expenses when assessing whether a loan will be unsuitable to consumers. ASIC appealed against the decision and, in December 2019, released responsible lending guidance (RG 209), notwithstanding that the outcome of the appeal was yet to be determined.

On 26 June, the Full Federal Court handed down its decision. In separate judgments Lee and Gleeson JJ dismissed ASIC's appeal with costs. Their Honours held that there is no statutory basis for ASIC's "prescriptive" interpretation of responsible lending obligations.

(b) Facts

The NCCP Act requires lenders to assess whether loans will be unsuitable for consumers.

Broadly, ASIC argued that Perram J erred in failing to find that the manner in which Westpac assessed the unsuitability of 261,987 home loan applications between December 2011 and March 2015 breached these obligations.

ASIC's argument had two parts.

(i) Unsuitability assessment - the proper construction of responsible lending obligations

Broadly, ASIC argued that the method used by Westpac - an automated decision system which used a range of rules, the serviceability rule, the 70% rule and the HEM benchmark - to assess the unsuitability of the loans did not assess the consumer's likely ability to comply with their financial obligations as required under s. 131(2)(a) of the NCCP Act, because each consumer's actual living expenses were not taken into account as (ASIC alleged) was required under the Act.

Section 131(2)(a) of the NCCP Act requires that lenders consider two questions (the s. 131(2)(a) Questions) when assessing whether a loan will be unsuitable:

- is it likely that the consumer will be unable to comply with the consumer's financial obligations under the contract?; and
- is it likely that the consumer will only be able to comply with the consumer's financial obligations under the contract with substantial hardship?

ASIC argued that "upon a proper construction of the provisions of Div 3 of Pt 3-2 of the NCCP Act, the primary judge ought to have held that Westpac did not make an assessment of the s. 131(2)(a) Questions and accordingly did not make the unsuitability assessment required by s. 128 of the Act".

(ii) Interest only loans

For loans with interest only periods, ASIC argued that Perram J erred in concluding that the lender made an assessment of unsuitability within the meaning of s. 131(2)(a) of the NCCP Act because in order to have met this requirement, ASIC considered it necessary for Westpac to have taken into account the higher repayments at the end of the interest-only period (which Westpac did not do).

(c) Decision

(i) Proper construction of the legislation

Gleeson and Lee JJ held separately, that as a matter of statutory construction, there is no obligation for lenders to take into account a prospective borrower's actual living expenses as ASIC contended.

Gleeson J stated:

"The Act cannot be construed to require Westpac to consider the total figure for declared living expenses in each case for the purpose of assessing the consumer's likely ability to meet their financial obligations ...
The language of the Act does not support the degree of prescription contended for by ASIC. Rather, the Act leaves it open to the licensee to decide:
(1) what inquiries it will make under s. 130(1)(a) and (b), provided that those inquiries are reasonable;
(2) what steps it will take to verify the consumer's financial situation under s 130(1)(c), provided that those inquiries are reasonable; and
(3) how it will use the results of its inquiries and verification to make the unsuitability assessment, provided that it in fact assesses whether the contract will be relevantly unsuitable for the particular consumer and noting that the licensee is otherwise motivated by the Act to refrain from entering into an unsuitable contract.

Similarly, Lee J disagreed with ASIC's interpretation of the obligations:

"The difficulty with this argument [ASIC's argument] is that the word 'assessment', as used in ss 128(c) and 129, does not seem to me to incorporate the obligation for which ASIC contends. There is no textual requirement specifying how the assessment is to be undertaken, and indeed ASIC accepted that "it remains open to a licensee to choose how it conducts the assessment required".

Lee J went on to state that:

"There is substance in Westpac's submission that if, as ASIC accepted, what a lender did with the information obtained under s 130 was "legitimately up to the lender", and not all information gathered needed to be used, how does one delineate the information to which Westpac must have regard, from information to which it need not have regard? Nothing in the text allows a licensee in the position of Westpac to know which specific parts of the information obtained must be used in the assessment to avoid incurring a civil penalty. This uncertainty is difficult to reconcile with a mandatory requirement, implied from the text, that in performing an assessment under s 129, Westpac must have specifically used (by "having regard to") the consumer's Declared Living Expenses.
I respectfully agree with the primary judge . that it does not follow that the statutory purpose can only be achieved by taking into account all information collected, regardless of its relevance or materiality to the assessment of unsuitability".

(ii) No error in finding that Westpac did not contravene responsible lending obligations

At first instance, Perram J found that as a question of fact Westpac did take into account customer's actual living expenses through the application of the 70% rule (though there was no statutory requirement for the bank to do so).

Lee J did not "consider the primary judge fell into error in dealing with the Declared Living Expenses issue". Gleeson J also agreed that the primary judge did not err in "concluding that Westpac asked and answered the s 131(2)(a) Questions and, accordingly, the primary judge was correct to conclude that ASIC's case failed".

(iii) The HEM benchmark

Gleeson and Lee JJ did not identify any issue with use of the Household Expenditure Benchmark as part of Westpac's process for assessing unsuitability. Gleeson J accepted Westpac's evidence that its "systems and processes were designed to ensure that a customer would meet their financial obligations to the bank by ensuring that the loan was not unsuitable for the customer and that the customer had the ability to service the loan without suffering substantial hardship".

Gleeson J stated:

"Westpac's ADS sought to answer the s 131(2)(a) Questions most particularly by the Serviceability Rule. The application of the Rule required calculations of the individual consumer's Discounted Monthly Income, Assessed Monthly Repayments and Outgo, and the identification of an HEM benchmark figure applicable to the consumer's circumstances. It is not fairly described as an assessment 'without regard to the circumstances of the individual concerned', and it is plainly directed to the risk of the particular consumer being unable to meet their financial obligations under the proposed credit contract without significant hardship as measured by the HEM benchmark".

Lee J stated:

"This was an unusual case, being a case alleging a serious want of compliance with responsible lending norms, divorced from consideration of any facts about any specific consumers. It was Westpac's job to assess suitability and although not determinative, for my part, it is far from intuitively odd that Westpac would focus on independent, objective data as represented by the HEM Benchmark and use the Declared Living Expenses in the way it did (through the use of the '70% Ratio Rule')".

(iv) Interest-only loans

At first instance, Perram J rejected ASIC's argument that Westpac breached the NCCP Act in the manner in which it answered the s. 131(2)(a) Questions in the case of loans with interest only periods.

His Honour held:

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

Gleeson, Lee and Middleton JJ separately agreed with Perram J's approach.

Editor's note: On 22 July 2020, ASIC announced that it will not seek special leave to appeal the decision of the Full Federal Court to the High Court. ASIC stated:
"While it would have been open to ASIC to seek special leave to appeal to the High Court to obtain a ruling on the construction of the statute, ASIC is mindful of the impact of the additional time required to resolve this matter in the current challenging economic circumstances. ASIC will review its updated regulatory guidance RG 209 (Credit licensing: responsible lending conduct) and will consider what implications the Federal Court decision has for that guidance. Any reform of [the NCCP Act] to clarify further the enforcement of those principles is ultimately a matter for the Federal Government and Parliament."

6.4 Federal Court rules in favour of liquidator seeking summons order

(By Tim Wells and Dana Perez, King & Wood Mallesons)

Pitman v Park (Liquidator), in the matter of BAM Recycling Pty Ltd (in liq) [2020] FCA 887 (25 June 2020), Federal Court of Australia, Derrington J

(a) Summary

The Federal Court of Australia dismissed an application by Mr Pitman (the Applicant) to discharge that part of a summons issued under s. 596B of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) requiring the Applicant to provide documents relating to his personal financial situation. The summons was issued upon request of the liquidator for BAM Recycling Pty Ltd (in liquidation) (the Company) in relation to the Applicant's proposed involvement, as the Company's solicitor, in the Company's liquidation.

In dismissing the application, the Court held that the documents the subject of the summons (including the Applicant's personal financial statements) related to the "examinable affairs" of the Company and therefore enlivened the Court's discretion to issue a summons under s. 596B of the Corporations Act.

In particular, in relation to s. 596D of the Corporations Act, it was held that where a liquidator can show that a possible cause of action might exist against a prospective examinee in relation to the liquidation, then any documents which concern the examinee's ability to meet any judgment obtained by the liquidator (such as personal financial statements) necessarily relate to the examinable affair' of the company.

(b) Facts

The Company carried on the business of trading recycled building materials. Prior to 24 August 2018, the Company was issued a statutory demand for the payment of a debt in the sum of $853,610.77 to the Australian Taxation Office. The statutory demand was unsatisfied, and the Deputy Commissioner of Taxation filed an application in the Federal Court to wind up the Company.

Morgan Conley Solicitors Pty Ltd (Morgan Conley) was engaged to act on behalf of the Company in respect of the winding up application. The Applicant was a director of Morgan Conley at all material times during this period. Morgan Conley received instructions from the Company's accountant, Mr Alistair Bell, in respect of the matter. Mr Bell instructed the Applicant to send him a form of business sale agreement listing the Company as the vendor and Tranz

Holdings Pty Ltd (Tranz) as the purchaser. In accordance with those instructions, the Applicant sent a draft business sale agreement to Mr Bell on 22 August 2018.

A winding up order in respect of the Company was made on 24 August 2018 and a liquidator was appointed. On 21 November 2018, the Applicant (purporting to act for the sole director of the Company) sent an email to the liquidator attaching a number of documents regarding to Company, including a business sale agreement substantially in the form of the draft agreement which the Applicant had sent to Mr Bell on 22 August 2018, but which was dated 28 September 2017 (which pre-dates by more than a year the occasion when the Applicant sent the draft to Mr Bell) and a document purporting to be the balance sheet of the Company as at 30 June 2018.

The liquidator subsequently discovered a discrepancy between the net asset deficiency recorded in the Company's balance sheet that was provided by the Applicant to the liquidator (i.e. -$31,858.01) and a balance sheet for the same period that was derived from the Company's MYOB files (i.e. -$769,088.31). The liquidator then made an application (which was granted by a District Registrar of the Federal Court on 3 March 2020) seeking the summonsing of information about the examinable affairs of the Company. One of the orders made by the District Registrar was that a summons for examination be issued to the Applicant, requiring both his attendance at an examination and that he produce certain documents, including documents relating to his personal financial position.

The Applicant sought a partial discharge of the summons as it related to the obligation to provide his personal financial statements or alternatively, submitted that it was beyond the power of the Court to require the Applicant to produce such documents because there was no factual basis for concluding that any action would (or could on the facts) be commenced against the Applicant. In this respect, the Applicant denied any close involvement with the Company or its liquidation, beyond drafting the business sale agreement and passing on documents received from Mr Bell to the liquidator, albeit with minor amendments.

(c) Decision

The Court held that the documents which were the subject of the summons (including the documents relating to the Applicant's personal financial position) were sufficiently related to the 'examinable affairs' of the Company such that the decision of the Court to grant the summons under s. 596B of the Corporations Act was valid. It was further held that the Court was not limited in its discretion in granting the summons for any reason in this case.

(i) The Court's power to issue a summons

The Court can summon a person under s. 596B of the Corporations Act for examination about a corporation's examinable affairs. It may do so if an eligible applicant applies for the summons and the Court is satisfied that the person to be examined has taken part in the examinable affairs of the corporation and has been, or may have been, guilty of misconduct in relation to the corporation or can give information about the examinable affairs of the corporation. Section 596D(2) provides that a summons may require the person to produce specified documents that are in their possession and relate to the corporation or any of its examinable affairs.

As the liquidator was an eligible applicant under s. 9 of the Corporations Act, the key issue was whether the information to be provided under the summons was about an 'examinable affair' of the Company.

Before engaging in this analysis, the Court noted that its discretion to issue a summons is wide and the matters which it may take into account are unconfined. The exercise of this discretion is, however, conditioned upon the satisfaction of the jurisdictional facts contained in s. 596B of the Corporations Act.

The Applicant challenged the scope of the categories of documents which the summons required him to produce on two alternative grounds:

- primarily, that the documents did not sufficiently relate to the affairs of the Company because he is not a 'potential defendant' from whom documents about his personal finances are required; and
- alternatively, in the circumstances the Court should exercise its discretion not to require him to disclose those documents.

(ii) The Company's examinable affairs

Derrington J addressed the primary ground by first ascertaining the nature of the examinable affairs of the Company. His Honour reasoned that the expression "any of its examinable affairs" is a phrase of wide connotation, and as such includes the issue of whether there exists a good cause of action against the person who is the subject of the summons. Citing support from In the matter of *Newheadspace Pty Ltd (in liq)* [2020] NSWSC 173, Derrington J added that the liquidator need not establish a "plausible claim" against the examinee and must simply show that the intended examination is for the purpose of investigating the "possibility" of a cause of action. Consequently, there is no requirement that the liquidator, after conducting a round of examinations, identify the existence of a cause of action with more certainty and make a subsequent application for the production of documents.

Upon examination of the Applicant's circumstances, Derrington J found that there existed a possibility that the Applicant may be liable as a person who was knowingly concerned in a contravention of the Act in relation to the wrongful disposition of the Company's assets. This is because he was involved in the sale of the Company's business to Tranz after the Company was deemed to be insolvent. Moreover, he had forwarded the liquidator a copy of the business sale agreement that was backdated to a time when the Company was solvent.

Derrington J emphasised that it was not necessary to decide whether the Applicant was in fact knowingly involved in a contravention of the law but rather, the possible existence of a cause of action against the Applicant was held to be an examinable affair of the Company. Therefore, s. 596D(2) of the Corporations Act was enlivened to require the Applicant to provide documents that would evidence his financial worth as a potential defendant.

(iii) The Court's discretion should not be exercised to limit the scope of the documents which are the subject of the summons

In relation to his alternative ground, the Applicant submitted that the Court should exercise its discretion to limit the scope of some of the categories of documents which were the subject of the summons for two reasons:

- first, because there were no temporal limits on the classes of documents to be produced, meaning that the Applicant would have to produce documents dating back many years, which would be oppressive in the circumstances; and
- second, since the documents which were the subject of the summons included information of his financial interests in trusts, he should not be obliged to disclose this information on the basis that such interests would not be available to meet any judgment which the liquidator might secure against him.

Derrington J rejected the first reason, stating that there was no basis for reading the schedule to the summons as requiring documents other than those relating to the identified time period.

In relation to the second reason, the Applicant argued on the basis of *Pleash v Tucker* (2018) 264 FCR 374 that the relevant documents should not be sought by the liquidator as they did not relate to the property of the prospective defendant (the Applicant) because he had no proprietary interests in the trust assets as a beneficiary and had no right to enforce any distribution to him.

In similarly rejecting the Applicant's second argument, his Honour reasoned that the principle in *Pleash* did not apply as the Applicant was a trustee of the assets of those trusts, and not a beneficiary as in the *Pleash* case. Accordingly, as a trustee, the Court found that the Applicant possessed a right of exoneration and an equitable lien over the trust assets, which would be property available to meet the liquidator's claims.

Accordingly, the Court dismissed the application to partially discharge the summons and ordered that a summons should issue to the Applicant substantially in the form attached to the liquidator's submissions to the Court. The Court requested that the parties submit short minutes of order as to the form of the summons to be issued to the Applicant.

6.5 ASIC required to indemnify and fund interim receivers
(By Katrina Sleiman, Corrs Chambers Westgarth)

Australian Securities and Investments Commission v Marco (No 4) [2020] FCA 881 (23 June 2020), Federal Court of Australia, McKerracher J

(a) Summary

In an earlier decision (*Marco (No 3)*), ASIC obtained orders from the Federal Court appointing interim receivers over the assets of the defendants pursuant to s. 1101B(5) of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act).

In this decision, the Federal Court considered how the interim receivers should be funded and indemnified. The Court distinguished between statutorily appointed interim receivers and receivers appointed in the equitable jurisdiction. In the case of interim receivers appointed on application to the Court by ASIC under statute, the Court considered it appropriate for ASIC to provide both funding and an indemnity.

(b) Facts

On 27 May 2020, the Federal Court made orders appointing interim receivers over the assets of the defendants with the power to do 'all things necessary and convenient to be done for or in connection with, or as incidental to, the identification, preservation and securing' of all of the defendants' property for the benefit of potential creditors.

Freezing orders pertaining to the defendants' assets had earlier been made on 1 November 2018 pursuant to s. 1323 of the Corporations Act. However, the parties were unable to reach agreement as to how the freezing orders should be adjusted to accommodate the orders made appointing and empowering the interim receivers' actions.

The first issue was who should provide the receivers with an indemnity. The interim receivers initially sought indemnity under s. 419A of the Act and the defendants voluntarily accepted liability for an indemnity under that provision, which pertains to events, circumstances and agreements which were pre-existing and under the defendants' control. The interim receivers then sought a conventional general indemnity for matters beyond those addressed by s. 419A of the Corporations Act. The defendants contended that if any other indemnity is needed for liability beyond that given under s. 419A, ASIC should give it. ASIC contended that the receivers be provided with an indemnity from the defendants' assets.

Second, ASIC proposed that the interim receivers' costs should be paid out of the defendants' assets, while the defendants contended that ASIC should fund those costs.

Third, the defendants sought a variation to the freezing orders to allow substantial payments in relation to two legal proceedings (the Marco Proceedings). ASIC contended that the interim receivers had the power to assess whether such expenditure ought to be incurred. The defendants contended that as these expenses were incurred before the appointment of the receivers, they should be approved by the Court.

(c) Decision

In the earlier decision of *Marco (No 3)*, the Court determined that the appointment of interim receivers was 'desirable' (the statutory term) for the following four reasons: (i) there was a potentially $200 million shortfall; (ii) there were no material returns to date; (iii) there had been incomplete record keeping giving rise to an uncertainty as to the extent of assets available to satisfy investor entitlements; and (iv) there had been an unsatisfactory use of investor funds in related party transactions.

In considering the indemnity and funding issues, his Honour undertook a detailed analysis of the relevant authorities. Central to his Honour's reasoning on each of the issues was the decision of French J in *Australian Securities and Investments Commission v Carey (No 5)* [2006] FCA 684.

His Honour noted that the observations in *Carey* were relevant to all four matters noted above, in particular that:

- the receivers were appointed on an interim basis for the purpose only of identifying, preserving and securing assets while ASIC's investigations continue;
- s. 1323 (and by parity of reasons s. 1101B(5)) of the Corporations Act are not intended to punish the defendants (*Carey* at [18]);
- the position of a receiver appointed under the Act differs from an appointment under the equitable jurisdiction. The appointment does not give rise to an entitlement to remuneration from the assets, it serves a public regulatory and protection function (*Carey* at [22]); and
- "[w]hile there are serious concerns about the conduct of the defendants, these are based on provisional judgments about the facts. No liability has been ascertained" (*Carey* at [24]).

(i) Should ASIC provide the receivers with an indemnity?

The orders made in *Marco (No 3)* accorded with the decision in *Carey* in that the question of the receivers' indemnity and costs was deferred with leave granted for ASIC to apply at a later time. In *Marco (No 3)* his Honour indicated that any indemnity should be provided by ASIC having regard to the need to mitigate the depletion of the defendants' assets by the appointment of interim receivers.

Central to his Honour's consideration of the indemnity position was the distinction between receivers appointed in the equitable jurisdiction and receivers appointed under statute.

While the conventional position in relation to receivers appointed in the equitable jurisdiction is that they are entitled to have their remuneration and an indemnity borne by the defendants' assets, his Honour noted a clear divergence from this position in the case of interim receivers appointed by the Court at the request of a regulator.

His Honour noted that while the authorities do not suggest that statutorily appointed interim receivers should be denied their remuneration, disbursements or an indemnity, it is not appropriate at least in the first instance that the possibly innocent party whose assets are controlled by the appointment should necessarily be the source of the costs and consequences of doing so.

Here, in the case of an interim appointment under s. 1101B(5) of the Corporations Act, rather than under an equitable appointment, his Honour considered it both valid and appropriate to require ASIC to meet any further indemnity beyond that given by the defendants under s. 419A.

(ii) Who should provide for the fees of, and expenses incurred by, the receivers in connection with their appointment?

The authorities considered by his Honour in relation to the indemnity issue were necessarily also relevant to the question of interim receiver expenses generally.

His Honour determined, on the same principles relevant to the indemnity issue, that all costs associated with the provision of the interim receivers' investigatory reports be paid by ASIC.

(iii) Legal fees of Marco Proceedings

The defendants sought an order that legal fees incurred in the Marco Proceedings up to 27 May 2020 be paid.

However, his Honour noted that the fact that the fees were incurred prior to the appointment of the interim receivers was only one consideration. The more significant was that by the terms of the freezing orders, the defendants were not to incur such a liability without first obtaining Court approval. That said, typically a party whose assets are subject to a freezing order should be entitled to incur reasonable expenses to take legal advice to protect his or her position.

His Honour accepted ASIC's submission that the interim receivers should determine whether the fees should be paid, as they were best placed to make an assessment of the reasonableness of incurring the fees including the quantum.

6.6 Circulating assets - recent decision determines when employee entitlements obtain priority
(By James Marshall, Emanuel Poulos, Michael Sloan, and Richard Fisher, Ashurst)

In the matter of RCR Tomlinson Ltd (administrators appointed) [2020] NSWSC 735 (15 June 2020), Supreme Court of New South Wales, Black J

(a) Summary

In this case, Black J, on an application for directions, was asked to give advice as to whether certain interests, to use a neutral characterisation, were circulating assets. That issue arose by reason of a dispute as to whether those interests came within the operation of s. 561 of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) and would, thereby, be available to employees in priority to the claims of secured creditors.

The judgment also contains an important analysis of what constitutes an 'account' for the purposes of the Personal Property Securities Act 2009 No. 130 (Cth) (the PPS Act).

The decision is authority for the following propositions:

- the relevant time for determining whether an asset is a circulating asset is the date on which administrators were appointed prior to the liquidation;
- rights to receive surplus funds from customers who had a right to call upon performance bonds but may or may not do so and had not done so at the appointment date, were not circulating assets as their nature was too uncertain at that time; and
- claims for work in progress as at the appointment date, even if there had been no claim at that date, were in the nature of circulating assets if there was a right to issue an invoice for that work or nothing further was required to do so than the issue of a certificate that the work had been satisfactorily completed.

Whilst it did not arise for consideration, the reasoning in the case would support an argument that progress payments which are able to be claimed at defined milestones which occur prior to the appointment date in the course of performing a contract are also circulating assets.

(b) Facts

RCR Tomlinson Limited and its related companies ('RCR') provided engineering, construction and maintenance services to customers in Australia. RCR appointed voluntary administrators who were subsequently appointed as its liquidators when RCR entered creditors' voluntary liquidation.

In the course of its business, RCR would arrange for the provision of performance bonds, bank guarantees, or similar instruments, to its customers (the Customer Bonds). The Customer Bonds were issued by various financiers whose claims were secured on a syndicated basis by way of a charge given by the Group. For the purposes of the application for directions, it was accepted that, if a Customer Bond was called and the customer received a payment beyond the amount which it was entitled to receive, it would be under an obligation to remit that surplus to RCR (the Surplus Proceeds).

RCR would also engage sub-contractors to deliver some of the services which it had contracted to provide to its customers. Those subcontractors would provide bonds, bank guarantees, or similar instruments, to RCR in order to secure their obligations to it (the Subcontractor Bonds).

At the time of the appointment of the voluntary administrators (the Appointment Date), calls had not been made on various Customer Bonds which had been provided to counterparties on behalf of RCR or under the Subcontractor Bonds.

Also, at the Appointment Date work under some of the contracts which RCR had with its customers had reached different stages of progress but for which no invoices had been issued (the WIP).

The issues raised by the application for directions, in essence, concerned whether any of (a) the Surplus Proceeds, (b) the WIP or (c) the proceeds from calls under the Subcontractor Bonds where those calls had not been made as at the Appointment Date (the Subcontractor Proceeds) were circulating assets and, therefore, subject to be applied consistently with the requirements of s. 561 of the Corporations Act.

(c) Decision

(i) Threshold Question

A preliminary issue which Black J needed to address was to identify the time at which an assessment is made as to whether an asset or interest is subject to a circulating security interest. In that regard, his Honour concluded (at [25]):

"... it seems to me that it is necessary to determine the question whether property is comprised in or subject to a circulating security for the purposes of s 561 of the Act at the Appointment Date rather than on a continuous basis or at some other unidentified date, adopting the same approach in respect of s 561 of the Act as is adopted in respect of s 433 of the Act".

That is to say, in the case of RCR, the decision as to whether an asset or interest was a circulating asset was to be made as at the Appointment Date.

(ii) Surplus Proceeds

At the Appointment Date, there were a number of Customer Bonds in respect of which no demand had been made. As already noted, it was accepted that, if Surplus Proceeds were received by any customer of RCR, it would be obliged to remit that amount to RCR.

It was held that at the Appointment Date, the interest of RCR to Surplus Proceeds was so uncertain that it could not be characterised as personal property for the purposes of the PPS Act.

As Black J put it (at [70]):

"On balance, it seems to me that .any 'right' to Surplus Proceeds was so contingent that it was "nothing but an expectancy", in the language of Norman [*Norman v Federal Commissioner of Taxation* [1963] HCA 21], and not an existing contractual right and that it did not have the nature of personal property. The uncertainty in that respect was not merely the completion of performance by a [Tomlinson company], but whether a third party, . would call on a Bond, which it may or may not do for its own commercial reasons. This is not a case where a Principal was bound to call on the Bond, still less where it had done so, and the only question was the quantum of the Surplus Proceeds".

If, contrary to his conclusion that the Surplus Proceeds were not personal property, Black J addressed the possibility that they might be a "monetary obligation" and an 'account' for the purposes of ss. 10 and 340 of the PPSA. His Honour concluded that they did not (at [77], [78], and [79]):

"On balance, it seems to me that the Surplus Proceeds cannot properly be characterised as a monetary obligation at the Appointment Date. First, it seems to me that the term "monetary obligation" must retain something of its character in general usage, and a potential claim in respect of the Surplus Proceeds which might or might not arise depending on the actions of a third party, while of a monetary character, had no element of "obligation" about it. If a claim of that character were treated as a "monetary obligation", there would be no principled basis on which to exclude other contingent claims which might or might not arise. .

[Second, the] Surplus Proceeds do not satisfy any of the requirements . for a 'monetary obligation', since they were not an existing legal obligation (at the Appointment Date) on a Principal (which had not then called on the Bonds or received their proceeds) to pay an identifiable monetary sum to the company on an ascertainable date or at all, and a Principal did not then have (and, absent a call on the Bonds, would never have) an existing liability to make the payment.

Third, the concept of 'account' in s 10 of the [PPS Act] seems to me to have at least its core meaning in common with that of 'account receivable' in s 16 of the [*Personal Property Securities Act 1999* (NZ)], as recognised in the academic commentary to which I have referred above. The Surplus Proceeds are so contingent in character that they would not properly fall within that concept or any expansion of it that can reasonably be drawn from the use of a simpler term 'account'. Fourth, the phrase 'whether or not that obligation has been earned by performance' in the definition of 'account' in s 10 of the [PPS Act] does not extend the operation of that concept to the Surplus Proceeds, since the right to Surplus Proceeds depended on whether the Principal decided to call upon the Bonds for its own reasons, not on any future performance by [RCR]".

(iii) WIP

The application for directions sought advice in respect of a number of categories or permutations of WIP as follows:

- "WIP Permutation 1: The production of the goods or the rendering of services had been completed by the Appointment Date and all that remained to give rise to a right to payment . was for an associated invoice or demand or request for payment . to be issued .
- Permutation 2: The production of the goods or the rendering of services had been completed by the Appointment Date, but . certification or approval was required before an Invoice could be issued ...
- Permutation 3: The production of goods or rendering of services had commenced before the Appointment Date but was only completed after the Appointment Date and no right to payment . until after the Appointment Date.
- Permutation 4: At the Appointment Date a contract for the production of goods or the rendering of services was on foot, but [RCR] had not yet commenced producing the goods or rendering the services.
- Permutation 5: At the Appointment Date there was a head or umbrella contract in place, but no order for the production of goods or for the rendering of services had been placed with [RCR]".

The parties did not argue that each category or permutation of WIP was not personal property. It was disputed, however, as to whether each of them was an account or monetary obligation.

In relation to those various categories or permutations, Black J concluded as follows:

- Permutation 1: "It seems to me that the amounts falling within WIP Permutation 1 were 'monetary obligations' and an 'account' within ss. 10 and 340(5)(a) of the [PPS Act] and therefore a 'circulating asset' within s. 340 of the [PPS Act] to which s. 561 of the [Corporations Act] can apply. First, the extension of the concept of 'account' to amounts still to be earned by performance suggests that it would at least include amounts that had been earned by performance that were yet to be invoiced. Second . the amounts that were still to be invoiced were governed by the contracts and any dispute as to the amount invoiced could be determined on that basis".

- Permutation 2: "It seems to me that the position here is the same as for WIP Permutation 1, since any dispute as to certification and the amount invoiced could be determined under the contract. On that basis, these amounts also constituted an account under s 10 and 340(5)(a) of the [PPS Act], a circulating asset under s 340 of the [PPS Act] and fall within the scope of s 561 of the [Corporations Act]".
- Permutation 3: "WIP Permutation 3 arises where the production of goods or rendering of services had commenced before the Appointment Date but was only completed after the Appointment Date and no right to payment arose until after the Appointment Date . I accept, that ., if there is no contractual basis for an appointment of WIP, then there is no monetary obligation in respect of any amount in this category as at the Appointment Date. . [Moreover] on the assumed facts, there was no such obligation [to make a payment for the then completed work] at the Appointment Date, conditional or otherwise, because the contract did not provide a right for payment for incomplete work. There was, instead, only a possibility at the Appointment Date that an obligation might arise at a future date, if and only if the relevant work was completed. That was not, in my view, a 'monetary obligation' at the Appointment Date".
- Permutations 4 and 5: His Honour did not consider that a direction in respect of these permutations was necessary.

(iv) Subcontractor Proceeds

In relation to the Subcontractor Proceeds, Black J concluded at [107]:

"In my view, a potential claim in respect of the Subcontractor Proceeds which might or might not arise, while of a monetary character, would not fall within the general usage of the term 'monetary obligation' or the term account in ss 10 and 340(5)(a) of the [PPS Act], because it had no element of obligation about it at the Appointment Date".

6.7 Application by administrators to adjourn hearing of winding up application
(By Lucinda Sergiacomi, MinterEllison)

Re FineTea Pty Ltd [2020] VSC 357 (15 June 2020), Supreme Court of Victoria, Delany J.

(a) Summary

The administrators appointed to the defendant, *Re FineTea Pty Ltd*, sought the following orders at the interlocutory process:

- the winding up application filed 9 April 2020 be adjourned to 15 July 2020;
- pursuant to ss. 440A and 447A(1) of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) and r. 90-15 of the Insolvency Practice Schedule (Corporations) at Schedule 2, the administrators' personal liability under ss. 443A(1)(c) and 443B(2) of the Corporations Act be varied such that they will not be liable for relevant rent and outgoings for the period from 16 June 2020 to 15 July 2020; and
- pursuant to Order 54 of the Supreme Court (General Civil Procedure) Rules 2015 No. 103 (Vic) (the Rules) and s. 63 of the Trustee Act 1958 No. 6401 (Vic), that the assets of the FineTea Trust be sold and the proceeds of sale be retained by the company in partial satisfaction of its right of indemnity against those assets.

Delaney J outlined the considerations relevant in determining if the administrator had proven there was a 'sufficient possibility' that the adjournment of the winding up is in the interests of the creditors.

The Court held that the winding up application should be adjourned to 15 July 2020 on the following basis:

- the clear benefit to the creditors of a sale that includes an assignment of the lease, a prospect not available on a winding up;
- the potential for an application in the meantime by the administrators relying upon s. 442C(2)(c) of the Corporations Act if consent to assignment is not obtained by agreement; and
- the need for the Court to consider, if required, the arguments advanced as to estoppel, unconscionable conduct and relief against forfeiture and s. 77(1) of the Retail Leases Act 2003 No. 4 (Vic).

The Court determined to direct the administrators to adjourn the meeting of creditors to 17 July 2020 and that orders should be made under s. 447A of the Corporations Act to vary the liability of administrators under the lease by excusing the administrators from personal liability, until 15 July 2020.

(b) Facts

The defendant, Finetea Pty Ltd, operates a business and had leased the premises for many years. The plaintiff and petitioning creditor, Winchelada Pty Ltd, entered into a loan agreement with the company in the amount of $2 million in 2016, to be used to develop the company. The business ceased operating on 19 March 2020 as a consequence of government restrictions in response to the COVID-19 pandemic.

On 8 May 2020 administrators to the company were appointed. On 25 May 2020, the administrators made an agreement for rental with the landlord to pay $8,000 toward rent and outgoings due under the lease, so they may retain occupancy.

On 4 June 2020, the landlord served a notice under s. 146 of the Property Law Act 1958 No. 6344 (Vic) (the Property Law Act) asserting that the lease had been terminated by reason of the appointment of the administrators on 8 May 2020. The leasehold interest in the premises is a significant part of the business seeking to be sold by administrators.

(c) Decision

(i) Can the business be sold with an assignment of the lease?

The Court found that without remedying the breach, subject to s. 146 of the Property Law Act, the tenant has no right to assign the lease regardless of the qualities of the proposed assignee. Further, as the administrator is already appointed the breach is not capable of being remedied.

Delaney J then discussed s. 442C of the Corporations Act. It was determined that due to the correspondence and submissions of the landlord, indicating that the landlord will not consent to dispose of the property, s. 442C(2)(b) did not apply to this case.

The court then considered s. 442C(2)(c) of the Corporations Act, and in particular, the criteria identified by *O'Bryan J in Re Holdco Pty Ltd (admins apptd)* 2020 FCA 666 at [44]-[49] was cited, and are summarised as follows:

- s. 442C operates to limit the powers of an administrator to dispose of the property of a company in administration in specified circumstances;
- the section gives the Court power to authorise an administrator to dispose of the property, which includes significant intrusion on third party security interests and property rights;
- the Court's power to grant the lease is subject to the condition that the Court must be satisfied that arrangements have been made to adequately protect the interests of the secured party, owner or lessor; and
- if the Court is satisfied that the interests of the secured party will be protected, the discretion of the court under s. 442C(2)(c) is otherwise unconstrained.

Delaney J determined that though the case does not present an occasion to consider s. 442C(2)(c) of the Corporations Act, these observations show that there can be utility in granting the adjournment sought as the landlord cannot be compelled to consent to an assignment.

The Court considered that the power to compel an assignment is available only while the company in administration is valuable - which in this case was due to the significance of the lease to this business. Delaney J found there to be a very strong imperative in favour of adjourning the winding up application so that the administrators can pursue the sale process and if required, apply to court under s. 442C(2)(c) of the Corporations Act.

The Court then considered whether relief against forfeiture is available in the present circumstances, where the event of default relied upon under the lease is incapable of being cured. The reasoning of Bereton J in *Re Hi-Fi Sydney Pty Ltd (admin apptd)* [2015] NSWSC 1312 [26]-[36] regarding when to determine to grant relief against forfeiture, when the breach relied upon was the appointment of an administrator, was found to be relevant.

Delaney J discussed the role of forfeiture as relief against unconscionable conduct, the allegations of unconscionable conduct in the present case and the administrators' submission that an estoppel by conduct arises again the landlord. However, his Honour noted that these contentions could not be resolved in an adjournment application. Importantly, the presence of the issues was found to support the Court adjourning the winding up application.

(ii) What is in the interest of the creditors?

The Court considered the administrators' report to creditors regarding the business' historic annual turnover. That the business had no employees and was currently not trading was also considered and was not found to indicate a lower value of the business, when contrasted with the evidence indicating the business was long-established and well known as a business trading from the leased premises.

Delaney J determined after assessing the administrators' report that pursuant to s. 440A(2) of the Corporations Act there was more than a "sufficient possibility" that the adjournment sought was in the best interests of the creditors. If s. 440A(2) was not applicable, the discretion conferred under s. 447A(1) would have been used.

(iii) Relief from the rent obligation

The Court cited the principles governing the granting of an application to make orders varying the personal liability of administrators under s. 447A of the Corporations Act outlined in *Re Griffin Coal Mining Company Pty Ltd (admins apptd)* [2010] FCA 1469.

The Court was satisfied that the orders should be made under s. 447A of the Corporations Act having regard to the following circumstances:

- the evidence that there were insufficient funds to enable the rent and outgoings to be paid (distinguishing *Re CBCH Group Pty Ltd (admins apptd) (No 2)* [2020] FCA 472);
- the modest amount of rent forgone in the context of the agreement of the administrators to pay $8,000 rent during the time the business was not trading;
- the short period in respect of which the variation from personal liability is sought and its purposes of facilitating a sale of the business for the benefit of the creditors; and
- the landlord's ability to claim the rent for this period as an unsecured creditor.

6.8 COVID-19 delays and compliance with s. 459G of the Corporations Act
(By Brett Cook and Zack George, Clayton Utz)

CPR Solutions Mackay Pty Ltd v Zammit Earthmoving Pty Ltd [2020] QSC 165 (11 June 2020), Supreme Court of Queensland, Crow J

(a) Summary

The applicant filed an application to set aside the respondent's statutory demand. At the time of filing, the registry stamped the application and placed it on the court file. Due to COVID-19 restrictions, the registry was unable to provide a return date, seal the application or issue a copy of it to the applicant. In an attempt to comply with the requirements of s. 459G of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act), the applicant served on the respondent an unstamped copy of the application. The issue for the Court was whether service of the unstamped application constituted valid service under s. 459G.

Crow J found that service was invalid. As the stamps were the only indication that the application had been filed, the unstamped copy was not a "copy of the application" under s. 459G of the Corporations Act. The court also found that COVID-19 related legislation did not empower the Court to alter the requirements of s. 459G.

(b) Facts

On 26 February 2020, Zammit Earthmoving Pty Ltd (Zammit) served a creditor's statutory demand on CPR Solutions Mackay Pty Ltd (CPR), pursuant to s. 459E of the Corporations Act. Twenty days later (on 17 March 2020), CPR filed in the Mackay District Registry (the Registry) an application to set aside the statutory demand, as well as a supporting affidavit, pursuant to ss. 459G and 459H(1) of the Corporations Act.

The usual practice of the Registry was to provide a sealed copy of the filed application, including a file number and return date, on the same day as filing. On this occasion, due to COVID-19 restrictions, that practice was not followed. A sealed copy of the application, with the return date for the hearing of the application, was not made available by the Registry until 6 April 2020.

As a result of the delay by the Registry and the imminent expiry of the 21-day statutory period, on 18 March 2020, CPR's solicitor emailed an unstamped copy of the application, the affidavit and the filing receipt to Zammit's solicitor. The copy of the application which was served did not show the file number given by the court, bear the seal of the court or a return date, or show a filing date for the application. Zammit's solicitors refused to accept that formal service had been effected until they received a sealed copy of the application with the file number and the return date allocated.

The issue in dispute was whether the service of the application on 18 March 2020 constituted valid service under s. 459G of the Corporations Act. Specifically, the issue was whether the copy of the application served on that date came within the meaning of "a copy of an application" under s. 459G(3)(b).

(c) Decision

Crow J's reasoning proceeded in three stages. First, his Honour considered the principles concerning the validity of service under s. 459G of the Corporations Act. Secondly, his Honour considered whether COVID-19 related legislation enabled the requirements of s. 459G to be modified. Finally, his Honour applied the principles to the facts.

(i) Principles concerning s. 459G

Following a review of several key authorities, Crow J observed that the words "a copy of" in s. 459G(3)(b) of the Corporations Act did not mean an "exact replica" (quoting *Craneford Nominees Pty Ltd v VGC Co-operative Limited* [2012] SASC 74). Instead, they meant that the copy must not fail to "reflect the original application in a matter of substance" (quoting *LJAW Enterprises Pty Ltd v RJK Enterprises Pty Ltd* [2004] QSC 134).

His Honour also observed that whether there had been valid service of a copy of an application under s. 459G of the Corporations Act depended on a "close application of the applicable State's court rules". As Queensland's court rules require originating applications to specify a return date, his Honour found that, on an orthodox application of the authorities, unless a copy of an application to set aside a statutory demand included a return date, service of that copy would be invalid for the purposes of s. 459G.

That was the position even if the applicant is not at fault and the inability to serve a copy of the application arises from a delay in the court registry in processing and filing the application and the supporting affidavit.

(ii) COVID-19 legislation

Next, Crow J considered whether the COVID-19 Emergency Response Act 2020 No. 13 (Qld) (the COVID Act) could assist in overcoming any defects in service under s. 459G of the Corporations Act. Crow J interpreted s. 15 of the COVID Act as empowering the Court to modify or extend time periods under Queensland Acts (such as the Uniform Civil Procedure Rules 1999 No. 111 (Qld)). However, his Honour considered that s. 15 did not empower a Court to modify or extend a period under s. 459G. This is because the COVID Act, being a State Act, could not empower the Court to modify a Commonwealth Act. Accordingly, Crow J considered that the COVID Act could not assist in overcoming any defects in service under s. 459G.

(iii) Application

In applying the relevant principles to the facts, his Honour commenced by considering the significance of the lack of a return date on the unstamped copy that was served. While, on an orthodox application of the authorities, a return date would have been required, his Honour considered that what properly constitutes a "copy of the application" depends "upon a comparison of the text of the application that was in fact filed . and the document served . purporting to be a copy of that application".

As the application in fact filed did not contain a return date, the unstamped copy that was served did not contain one either. His Honour observed that the only features of the copy on the file that indicated it had been filed were the date and receipt stamps. As the unstamped copy that was served lacked the date and receipt stamps, it was not a sufficient copy for the purposes of s. 459G of the Corporations Act. As service had not been effected in accordance with s. 459G, this produced the "harsh" outcome that the court did not have jurisdiction to entertain the application and the application was dismissed.

6.9 Appointment of special purpose liquidators in the matter of Commonwealth of Australia v Phoenix Institute
(By Jake Hamilton, King & Wood Mallesons)

Commonwealth of Australia (Department of Education, Skills and Employment) v Phoenix Institute of Australia Pty Ltd (in liq) [2020] FCA 937 (4 June 2020), Federal Court of Australia, Markovic J

(a) Summary

On 4 June 2020, Markovic J in the Federal Court of Australia granted an application by the Department of Education, Skills and Employment (the Department) to appoint special purpose liquidators to its debtor, Phoenix Institute of Australia (Phoenix). Her Honour found that this appointment was necessary to allow for investigations into the affairs of Phoenix and its directors with a view to benefitting the interests of creditors. Approval was also granted for the special purpose liquidators to enter into an agreement with the Department, pursuant to which the Department would fund these investigations.

The proceedings raised the following issues:

- whether special purpose liquidators should be appointed pursuant to the Court's power to make orders in relation to the external administration of a company, under s. 90-15 of the Insolvency Practice Schedule (Corporations) (the IPSC) in Schedule 2 to the Corporations Act 2001 No. 50 (Cth) (the Corporations Act);
- whether approval for the special purpose liquidators to enter the funding agreement should be granted under s. 477(2B) of the Corporations Act; and
- whether a confidentiality order should be made in respect of the funding agreement under s. 37AF of the Federal Court of Australia Act 1976 No. 156 (Cth) (the Federal Court Act).

(b) Facts

Phoenix was a vocational education and training (VET) provider which offered diploma courses in business, leadership and management, early childhood education and care, and community services. Phoenix was part of the VET FEE-HELP scheme, under which the Commonwealth government would provide loans to eligible students and pay those students' tuition fees directly to the VET provider. Participation in this scheme required the educational facility to be approved as a registered training organisation by the Australian Skills Quality Authority.

In September 2015, an audit revealed that Phoenix had been non-compliant with several VET quality and accountability requirements. Phoenix's approval as a VET provider and registered training organisation was revoked. On 21 March 2016, Phoenix was placed into voluntary administration.

In March 2020, at a meeting of creditors, it was resolved that Phoenix would be put into liquidation, with the administrators to be appointed as liquidators. The Department, one of Phoenix's creditors, took issue with this decision, as they believed that there should have been investigations into the affairs of Phoenix regarding possible falsification of accounts and wrongful conduct by its directors, which was unlikely to occur if the company were put into liquidation.

The administrators had not undertaken these investigations during the period of administration because of insufficient funding. The Department therefore offered to fund the investigations, on the condition that special purpose liquidators of the Department's choice were appointed to complete the task. The Department applied to the Court for appointment of the special purpose liquidators, as well as for leave of the Court for the special purpose liquidators to enter into a funding agreement. Confidentiality orders were also sought in respect of this funding agreement.

(c) Decision

Markovic J ultimately made all orders sought by the Department.

(i) Appointment of special purpose liquidators

Section 90-15 of the IPSC provides that the Court may make such orders as it thinks fit in relation to the external administration of a company, either on its own initiative or on an application under s. 90-20 of the IPSC.

After reviewing the relevant case law, her Honour determined that the Court's use of this power to appoint an additional liquidator is appropriate where:

- there are matters that require investigation with a view to possible recovery for creditors;
- the current liquidators have insufficient funding to pursue such investigations;
- a creditor is prepared to fund the investigations on the condition that another liquidator is appointed; and
- the appointment would be just and beneficial to the winding up and creditors.

Markovic J found that there were matters that required investigation. In particular, non-compliances by Phoenix in relation to student enrolments reported to the Department had potential to raise issues regarding the amount of payments Phoenix was entitled to receive, the conduct of its directors, and insolvent trading. These matters had not been investigated by the current liquidators due to funding and time constraints and would not be investigated without the funding offered by the Department.

In these circumstances, her Honour found that the appointment of special purpose liquidators would be just and beneficial. Any monies recovered through the investigations would benefit the creditors, and if the investigations did not result in any further recovery, the Department would bear the financial burden. Accordingly, an order for the appointment of the special purpose liquidators was made.

(ii) Approval of entry into the funding agreement

The Department sought to have the special purpose liquidators enter into an agreement in relation to the funding of the investigations. However, as a term of this agreement could end more than three months after being entered into, this required approval of the Court pursuant to s. 477(2B) of the Corporations Act. The Department therefore made an application for such approval.

Markovic J found that there was no issue with this application being made by the Department instead of the additional liquidators themselves. The additional liquidators had consented to enter into the funding agreement and had filed an affidavit in support of the Department's application.

Her Honour determined that it was appropriate for the funding agreement to be entered into. The agreement would allow for the investigations to occur which, as discussed above, would be in the interests of creditors. If the agreement were not entered into, the investigations would be unlikely to proceed. Additionally, the special purpose liquidators had given undertakings to the Court that they would not recover their fees and expenses other than in accordance with the terms of the funding agreement. Accordingly, her Honour granted the leave sought by the Department.

(iii) Granting of confidentiality orders

Finally, the Department sought an order that the funding agreement be kept confidential, pursuant to s. 37AF of the Federal Court Act.

Markovic J allowed the order on the ground that it was necessary to prevent prejudice to the proper administration of justice.

Her Honour gave the following reasons:

- the funding agreement contained a clause requiring its terms to be kept confidential;
- the funding agreement was a commercially sensitive document that was the product of confidential negotiations; and
- disclosure of the funding agreement would reveal the amount of resources available to the special purpose liquidators and the investigations proposed to be undertaken.

6.10 The liability of joint venturers to account for breach of fiduciary duty
(By John Slater, Herbert Smith Freehills)

Jin Niu Investments Pty Ltd v Wang (No 2) [2020] NSWSC 649 (29 May 2020), Supreme Court of New South Wales, Henry J

(a) Summary

This decision involved proceedings brought against two joint venturers for breach of their fiduciary and directors' duties in relation to a range of unauthorised dealings with property of the joint venture. In summary, the two defendant joint venturers:

- used funds advanced by the third joint venturer to make unauthorised payments to themselves; and
- caused joint venture property to be held by or registered in the name of unauthorised corporate and trust entities, resulting in the dilution of the third joint venturer's interest.

Henry J held that while the funds advanced by the third joint venturer were not subject to a *Quistclose* trust, a resulting trust arose over the investments they were used to purchase. This meant that by seeking to retain the proceeds from these investments for personal gain, the two joint venturers acted in breach of trust as well as their fiduciary obligations and statutory duties as directors. The decision illustrates the principle that a fiduciary relationship between joint venturers can arise from the reliance placed by one party on another, separately to the obligations owed under the vehicle used to carry out the joint venture.

(b) Facts

The third plaintiff (Mr Wang) formed a joint venture company, the first plaintiff (JN Investments) with the first and second defendants (Ms Wang and Ms Li, respectively) to invest in Australian assets, with each of the joint venturers appointed as directors.

The terms of the Joint Venture relevantly included:

- Mr Wang, an overseas-based non-English speaker, would raise funding for investments while Ms Wang and Ms Li would be responsible for day to management, reporting regularly to Mr Wang;
- Ms Wang would hold a 90% interest in JN Investments and Ms Wang and Ms Li each a 5% interest; and
- the joint venturers would receive reimbursements for expenses and a third each of the net profits, but no fees or salaries.

Between February 2017 and late 2017, Ms Wang and Ms Li engaged in the following dealings:

- a property was purchased in Sydney for $3 million (the Hyde Apartment) using funds advanced by the second plaintiff, a company controlled by Mr Wang (Henan). Ms Wang and Ms Li were registered as the owners on Ms Wang's advice that laws restricted it from being held in JN Investments' or Mr Wang's name. On its sale, most of the proceeds were transferred to Ms Wang and Ms Li, contrary to the agreement of the joint venturers;
- Ms Wang and Ms Li created and issued interests in three corporate and trust entities without Mr Wang's knowledge (JN Agribusiness, JN Property and JN Property Trust);
- a farm (Blueberry Farm) was purchased using funds obtained through a loan secured by the Hyde Apartment, which was occupied by JN Agribusiness. Mr Wang advanced funds to JN Investments to discharge this loan that were instead transferred to Ms Wang and Ms Li in what was recorded as a loan; and
- a 35% interest in a property development (Lane Cove Property) was purchased using funds held by JN Investments and advanced by Henan. JN Property was registered as the owner without Mr Wang's consent. Later, Ms Wang and Ms Li caused the JN Property Trust to issue units to two corporate entities in respect of which Ms Wang and Ms Li were the sole directors and shareholders.

(c) Decision

(i) Did the joint venture give rise to fiduciary obligations?

Although the agreement between the parties was informal and made orally, Henry J found it constituted a binding joint venture. Further, Mr Wang's vulnerability, together with the trust he reposed in Ms Wang and Ms Li, were held to give rise to a fiduciary relationship in addition to the obligations owed between the joint venturers as directors of JN Investments.

(ii) Breach of trust

Henry J rejected the argument that a *Quistclose* trust arose over the funds advanced by Henan for the purchase of the Hyde Apartment and the interest in the Lane Cove Property, finding that these funds were provided by Mr Wang for working capital and not to be held for a specific purpose on trust.

Instead, his Honour found that a resulting trust arose over these funds, meaning:

- Ms Wang and Ms Li retained the funds from the sale of the Hyde Apartment in breach of trust; and
- JN Property held its interest in the Lane Cove Property in a resulting trust in favour of JN Investments.

(iii) Cash payments

Henry J found that the payments Ms Wang and Ms Li caused to be paid to themselves were made without JN Investments or Mr Wang's authority or consent. Accordingly, both were held to have used their position as directors improperly and dishonestly for personal gain in breach of their fiduciary obligations and statutory duties as directors.

Further, it was found that Ms Wang and Ms Li knowingly assisted each other's breach of fiduciary duty on the basis of evidence that both were complicit in dishonestly characterising the payments as loans and consulting fees. Consequently, both were held liable as constructive trustees for their own and each other's shares of the payments.

(iv) Unauthorised creation of business entities and dilution

Ms Wang and Ms Li's creation of corporate and trust entities to hold the joint venture investments and allocation of equity in such entities between the joint venturers in proportions contrary to the agreed 90/5/5 split was also held to be in breach of their fiduciary duties.

Accordingly, Henry J declared:

- the shares in these entities held by Ms Wang and Ms Li in excess of the agreed 90/5/5 split were to be held on trust for Mr Wang; and
- the two entities controlled by Ms Wang and Ms Li which had received units in the JN Property Trust were liable to account to JN Investments as constructive trustees.

(v) Rent free use of Blueberry Farms

The plaintiffs' claim that Ms Wang and Ms Li breached their fiduciary obligations by allowing JN Agribusiness to occupy Blueberry Farms did not succeed. Whilst Henry J acknowledged this transaction was undertaken without consent, his Honour was not convinced that JN Agribusiness' occupation gave rise to a conflict of interest or that the two defendant joint venturers stood to gain personally from it.