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Legislation Hotline

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1. Recent Corporate Law and Corporate Governance Developments

1.1 IOSCO consults on guidance to address conflicts of interest in the equity capital raising process

21 February 2018 - The Board of the International Organization of Securities Commissions (IOSCO) is proposing guidance to help its members address conflicts of interest and associated misconduct risks that may arise during the equity capital raising process.

Conflicts of interest and associated conduct risks stemming from the role of intermediaries can threaten the integrity and efficiency of equity capital raising, damage investor confidence and undermine capital markets as an effective vehicle for issuers to raise funding. To help regulators identify and address these issues, IOSCO has issued the consultation report Conflicts of interest and associated conduct risks during the equity capital raising process.

The report describes the key stages of the equity raising process where the role of intermediaries might give rise to conflicts of interest, and it requests public comment on IOSCO's proposed guidance for tackling these issues. The guidance comprises eight measures that are grouped according to the various stages in the capital raising process. Each group of measures addresses the following specific conflicts of interest:

- Guidance to address conflicts of interest and pressure on analysts during the formative, pre-offering phase of a capital raising;
- Guidance to address conflicts of interest during the allocation of securities;
- Guidance to address conflicts of interest in the pricing of securities offerings; and
- Guidance to address conflicts of interest and conduct risks stemming from personal transactions by staff employed within firms managing a securities offering.

IOSCO believes that the Guidance could help enhance the range and quality of timely information made available to investors during equity capital raising, improve the transparency of allocations, and increase the efficiency and integrity of the overall process.

Responses to a survey of IOSCO members indicated that while different jurisdictions share some common characteristics, they tend to have different market practices and different legal and regulatory frameworks governing the equity capital raising process. As a result, the severity of the conflicts of interest and associated misconduct risks, and the harm they can inflict, vary across jurisdictions. Consequently, the guidance is designed to provide IOSCO members with a degree of flexibility over how they implement the measures domestically, to ensure that these measures are appropriate for the legal and regulatory framework and the specific risks arising in each jurisdiction.

1.2 BIS report on implications of fintech developments for banks and bank supervisors

19 February 2018 - The Bank for International Settlements (BIS) has published a new report by the Basel Committee on Banking Supervision (the Committee), Sound Practices: Implications of Fintech Developments for Banks and Bank Supervisors, which assesses how technology-driven innovation in financial services, or "fintech", may affect the banking industry and the activities of supervisors in the near to medium term.

Various future potential scenarios are considered, with their specific risks and opportunities. In addition to the banking industry scenarios, three case studies focus on technology developments (big data, distributed ledger technology and cloud computing) and three on fintech business models (innovative payment services, lending platforms and neo-banks).

Against this backdrop, current observations suggest that although the banking industry has undergone multiple innovations in the past, the rapid adoption of enabling technologies and emergence of new business models pose an increasing challenge to incumbent banks in almost all the banking industry scenarios considered.

The Committee has proposed ten key implications and considerations on the following supervisory issues:

- the overarching need to ensure safety and soundness and high compliance standards without inhibiting beneficial innovation in the banking sector;
- the key risks for banks related to fintech developments, including strategic/profitability risks, operational, cyber- and compliance risks;
- the implications for banks of the use of innovative enabling technologies;
- the implications for banks of the growing use of third parties, via outsourcing and/or partnerships;
- cross-sectoral cooperation between bank supervisors and other relevant authorities;
- international cooperation between bank supervisors;
- adaptation of the supervisory skill set;
- potential opportunities for supervisors to use innovative technologies (suptech);
- relevance of existing regulatory frameworks for new innovative business models; and
- key features of regulatory initiatives set up to facilitate fintech innovation.

1.3 Reform of credit card practices and increasing competition in banking

15 February 2018 - The Treasury Laws Amendment (Banking Measures No. 1) Bill 2017 (Cth) has been passed by parliament. The reforms include:

- requiring affordability assessments to be based on a consumer's ability to repay the credit limit within a reasonable period (from July 2018);

- banning unsolicited offers of credit limit increases (from January 2019); and
- simplifying how credit card interest is calculated, and requiring credit card providers to have online options to cancel cards or to reduce credit limits (from January 2019).

The Bill will also increase competition in the banking sector by allowing small lenders to call themselves banks - a change that is aimed at enticing new lenders and challenger banks to enter the market. This reform paves the way for more than 60 current Australian lenders and credit unions to call themselves banks.

1.4 Establishment of the Australian Financial Complaints Authority

14 February 2018 - Parliament has passed legislation to establish the Australian Financial Complaints Authority (AFCA).

The Minister for Revenue and Financial Services, the Hon Kelly O'Dwyer MP, and Minister for Small and Family Business, the Hon Craig Laundy MP, said significantly more consumers and small businesses will have access to free, fast and binding dispute resolution following the passage of the Treasury Laws Amendment (Putting Consumers First - Establishment of the Australian Financial Complaints Authority) Bill 2017 (Cth).

The Government is also increasing access to redress by widening the range of disputes that AFCA will be able to hear.

- the definition of a small business will be relaxed, so that any business with fewer than 100 staff can access AFCA;
- small business primary production producers - defined in accordance with the Income Tax Assessment Act 1997 No. 38 (Cth) - will have access to compensation of up to $2 million for disputes about credit facilities of up to $5 million;
- the cap on income stream insurance product disputes will be increased from $8,300 to $13,400 per month;
- the cap on uninsured third party motor vehicle claims will increase from $5,000 to $15,000; and
- the separate compensation cap for general insurance broker disputes will be increased from $174,000 to $250,000.

AFCA will start receiving disputes from no later than 1 November 2018.

ASIC has welcomed the establishment of AFCA and in a media release has provided information about the transitional arrangements that will operate until AFCA is operational.

1.5 Strengthening APRA's crisis management powers

14 February 2018 - The Australian Parliament has passed the Financial Sector Legislation Amendment (Crisis Resolution Powers and Other Measures) Bill 2017 (Cth), which provides:

- powers that enable the Australian Prudential Regulation Authority (APRA) to set requirements on resolution

- planning and ensure banks and insurers are better prepared for a crisis; and
- an expanded set of crisis resolution powers that equip APRA to act to facilitate the orderly resolution of a distressed bank or insurer.

1.6 IOSCO consults on proposed policy measures to protect investors of OTC leveraged products

13 February 2018 - IOSCO has issued a consultation report proposing policy measures for its members to consider when addressing the risks arising from the offer and sale of over-the-counter (OTC) leveraged products to retail clients.

The *Report on retail OTC leveraged products* identifies various regulatory approaches aimed at enhancing the protection of retail investors who are offered OTC leveraged products, often on a cross-border basis. The report covers the offer and sale by intermediaries of rolling-spot forex contracts, contracts for differences (CFDs), and binary options. Intermediaries market and sell these products to retail investors in most IOSCO member jurisdictions.

Retail investors use OTC leveraged products to speculate on the short-term price movements in a given financial underlying. The products are traded over the counter, and their pricing, settlement and trading terms are not standardized. Typically, the products are offered through online trading platforms, and often through aggressive or misleading marketing campaigns. Several studies show that a large majority of retail investors in these complex products lose money.

In its report, IOSCO encourages its members to improve the practices of licensed firms that offer OTC leveraged products, in an effort to better inform investors about the features and risks of these products and to more effectively combat illegal cross-border activity in this area. IOSCO proposes the following policy measures in the report and offers guidance to regulators on how to apply each one:

- a licensing requirement for all firms that sell the relevant products to retail investors either domestically or on a cross-border basis;
- leverage limits or minimum margin requirements;
- measures to address the risk of investors losing more than their initial investment;
- measures to enhance the disclosure of costs and charges of the products;
- measures to improve the disclosure of risks of the products, including profit and loss ratios;
- other focused requirements to enhance the quality of pricing and order execution; and
- measures to restrict the sale, distribution and marketing of the products with a view to addressing mis-selling risk.

1.7 UK Financial Conduct Authority and Prudential Regulation Authority publish reports on algorithmic trading

12 February 2018 - The UK Financial Conduct Authority (FCA) has published a report on the supervision of algorithmic trading in wholesale markets, *Algorithmic trading compliance in wholesale markets*. The report summarises the key areas of focus for algorithmic trading and highlights areas of good and bad practice observed within previous cross-firm reviews.

Automated technology brings significant benefits to investors, including increased execution speed and reduced costs. However, it can also amplify certain risks. It is therefore essential that key oversight functions, including compliance and risk management, keep pace with technological advancements. The report focuses on five key areas within algorithmic trading compliance in wholesale markets:

- defining algorithmic trading
- development and testing process
- risk controls
- governance and oversight; and
- market conduct.

The UK Prudential Regulation Authority (PRA) has also published a Consultation Paper on proposed expectations regarding a firm's governance and risk management of algorithmic trading. The PRA publication is a formal consultation on a supervisory statement which sets out expectations for the prudential aspects of risk management and governance of algorithmic trading at PRA regulated firms. The UK's FCA and PRA will continue to work together to ensure coordinated approaches.

1.8 Review into open banking

9 February 2018 - The Australian Government has released the *Report of the Review into Open Banking - Final Report*. The Report makes recommendations on the most appropriate model for implementing open banking in Australia. Open banking will transform the way Australians interact with the banking system by giving consumers the right to safely share their data with other banks, other institutions and innovative FinTechs.

Granting third-party access to a customer's data will allow rival providers to offer competitive deals, products that are tailored to individual needs, and enhanced services that simplify the choices customers face when accessing banking services. It should simplify the process of switching between banks

Open banking will be implemented as part of the Consumer Data Right in Australia, a more general right to data being created across the economy following a recommendation by the Productivity Commission's *Data Availability and Use Inquiry*. On 26 November 2017, the Government announced that the Consumer Data Right will be established sector-by-sector, beginning in the banking, energy and telecommunications sectors.

The Open Banking Report makes 50 recommendations in total. It makes recommendations on: the regulatory framework to support open banking; what data should be shared and with whom; what safeguards are needed to inspire confidence in data sharing; how data should be transferred; and how open banking should be implemented.

1.9 Banking Royal Commission releases first two Background Papers

February 2018 - The Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry has released two Background Papers. The first is titled *Some features of the Australian banking industry: Background Paper 1*.

This background paper provides information about the range of Australian banking industry participants, the relative market share of those participants, the size of the Australian banking industry, the range of products offered and the profitability of the sector.

This paper illustrates the following key points:

- authorised Deposit-taking Institutions (ADIs) collectively hold around 55% of the total assets of Australian financial institutions (as at the September quarter 2017), making up the largest part of the Australian financial system;
- there has been a decline in the number of ADIs operating in Australia, largely as a result of the decrease in the number of credit unions following consolidation activity. Credit unions and building societies have also rebranded themselves as mutual banks, resulting in an increase in the number of domestic banks operating in Australia.
- the major banks hold approximately three-quarters of total assets held by ADIs in Australia;
- ADIs hold $4.6 trillion in assets, around two-and-a-half times the size of Australia's $1.8 trillion nominal economy. Financial and insurance services is the largest contributor to real industry gross value added; and
- banks provide a wide range of products and services to Australian consumers and businesses. In particular, bank lending is a key source of external financing for SMEs and agricultural businesses in Australia.

The second background paper is titled Some Features of the Australian Mortgage Broking Industry: Background Paper 1. This paper illustrates the following key points:

- the mortgage broking industry is a key distribution channel for residential mortgage financing in Australia, settling 55.7% of all residential home loans in the September quarter 2017;
- mortgage aggregators act as intermediaries between mortgage brokers and lenders, by providing brokers with access to lenders on their aggregator's panel;
- residential property investors and residential owner-occupiers are the main customers of mortgage brokers, collectively accounting for over 75% of the customers of mortgage brokers;
- banks still finance the majority of the loans originated through mortgage brokers, although there is a modest increase in the volume of loans financed by non-bank lenders; and
- mortgage brokers and mortgage aggregators do not charge borrowers directly for their services. Instead, they typically receive upfront and trail commissions from the lender.

1.10 Competition in the Australian Financial System - Draft Report

7 February 2018 - The Australian Productivity Commission has released a draft report on *Competition in the Australian Financial System*.

The report finds some notable failings in competitive behaviour evident in markets of home loans and for small and medium enterprise (SME) finance. In home loan finance, the widespread use of published loan benchmarks that do not reflect actual practice, accompanied by the lack of a legal duty of care by mortgage brokers, means consumers can be left unaware of better deals available to them. And regulator impacts on competition are evident, with insufficient attention being paid to opportunities to improve weighting of SME loan risks and lower smaller banks' cost of capital, in a manner practiced by other comparable nations. Some home loans are also not as well risk-weighted as they could be. These failings have the capacity to prevent loans being made, or cost borrowers significant sums.

The Productivity Commission has accordingly recommended that financial regulators collectively place more emphasis on competition, after a sustained period since the Global Financial Crisis emphasising stability. The Commission noted that competition in Australia's financial system is without a champion among the existing regulators - no agency is tasked with overseeing and promoting competition in the financial system.

The Inquiry draft report recognises that both competition and financial stability are important to the Australian financial system, and are an uncomfortable mix at times. The legislators' solution to date has been to specify a need for balance between the two. But balance is not evident - decisions have persistently favoured stability.

The Commission found that competition is weakest in markets for small business credit, lenders' mortgage insurance, consumer credit insurance and pet insurance. Proliferation of products (4000 varieties of home loans, 20 brands of pet insurance underwritten by a single insurer) and information complexity means little ability for consumers to stay abreast of market trends and serve their own best interests when the time comes to negotiate. And once-revolutionary information sources such as mortgage brokers are now part of the establishment, often owned by banks, and with their financial incentives generally aligned against keeping clients informed of opportunities to switch loans.

1.11 APRA releases CBA Prudential Inquiry Progress Report

1 February 2018 - APRA has released the Progress Report by the Panel appointed to conduct a Prudential Inquiry into the Commonwealth Bank of Australia (CBA): *CBA Prudential Inquiry Progress Report*.

In August 2017, APRA established the Prudential Inquiry to examine the frameworks and practices in relation to the governance, culture and accountability within the CBA group, in light of a number of incidents which damaged the reputation and public standing of CBA. The Panel was subsequently appointed in September and the Inquiry began work in October.

The Progress Report provides an update on the status of the Inquiry and outlines the methodology that the Panel has adopted to address the Terms of Reference.

1.12 IOSCO issues recommendations and good practices to improve liquidity risk management for investment funds

1 February 2018 - IOSCO has issued final recommendations that seek to improve liquidity risk management practices of open-ended collective investment schemes (CIS). The final report, *Recommendations for Liquidity Risk Management for Collective Investment Schemes*, sets out IOSCO's recommendations to entities responsible for managing the liquidity of CIS ('responsible entities') to ensure that liquidity is managed to safeguard and protect the interests of investors, including in stressed market conditions. In addition to its recommendations to responsible entities, the final report includes IOSCO's additional guidance to securities regulators to promote good liquidity management practices for CIS.

IOSCO has also simultaneously published a final report that provides practical information, examples and good practices regarding open-ended fund liquidity risk management, to supplement its recommendations. This final report, *Open-ended Fund Liquidity and Risk Management - Good Practices and Issues for Consideration*, is intended to assist regulators, the industry, and investors.

1.13 Survey results show a median pay ratio of 140:1 for US CEOs

1 February 2018 - Equilar, a provider of advice to boards of directors, has conducted an anonymous survey of 356 US public companies to identify the CEO Pay Ratio they plan to report in their 2018 proxy statements. Overall, the survey found that the median was 140:1 among this group of companies.

In 2015, the US Securities and Exchange Commission (SEC) passed a ruling that required public companies to report the ratio of compensation for their CEO in comparison to that of a median employee.

Key findings from the survey included the following:

- the median CEO pay ratio across all 356 submitting companies was 140:1. At the 25th percentile, the ratio was 72:1, and was 246:1 at the 75th percentile. The average was 241:1.
- median employee compensation for all companies in the survey was US$60,000;
- the median CEO pay ratio was larger in direct correlation to company revenue, totalling 47:1 for companies below US$1 billion in revenue and 263:1 for companies above US$15 billion in revenue; and
- companies with the greatest number of employees had the largest ratio (318:1) and the smallest median employee compensation (US$46,000). The smallest companies, with fewer than 2,310 employees, had the lowest ratio (45:1) and highest median pay (US$85,580).

Ratios by industry sector varied much more widely:

- "[c]onsumer discretionary" companies, which include retail and hospitality, had the highest ratio with a median 350:1;
- energy companies had the lowest ratio at 72:1; and
- median employee pay at the 48 consumer discretionary companies that responded to the survey was US$21,840 vs US$107,887 for the 30 energy companies that responded.

1.14 Australian Consumer Law amendments

31 January 2018 - In August 2017, Consumer Affairs Ministers agreed to a package of 14 legislative reforms, proposed by the Consumer Affairs Australia and New Zealand's Australian Consumer Law Review - Final Report, to improve the operation of the Australian Consumer Law (ACL). The Australian Government is now seeking views on the design of the exposure draft legislation and regulations (and accompanying draft explanatory materials).

These exposure drafts include amendments to:

- clarify existing provisions relating to consumer guarantees, voluntary recalls, unsolicited consumer agreements and false billing;
- enhance the regulators' information gathering powers for investigations in relation to product safety and unfair contract terms;
- extend the unconscionable conduct protections to publicly listed companies;
- expand the remedies available to the courts for contraventions of the ACL; and
- improve price transparency.

The exposure drafts and accompanying draft explanatory materials are available on the Treasury website.

1.15 APRA releases planned policy initiatives for 2018

31 January 2018 - APRA has published an Information Paper that outlines its policy initiatives for 2018: *Information Paper: APRA's policy priorities*. APRA has a prudential policy framework that includes legislation, prudential standards and guidance that, taken together, establish expectations for prudential conduct by regulated financial institutions. APRA supervisors rely on the prudential framework as a basis on which to assess prudent practice and, where necessary, enforce compliance with regulatory expectations.

The Paper sets out priorities in relation to banking (ADIs), insurance, superannuation and cross-industry initiatives. These include the following:

- commencing public consultation on changes to prudential requirements for minimum ADI capital, in accordance with the Basel Committee on Banking Supervision's revisions to the risk-based capital framework;
- commencing the more detailed consultation phase on the credit risk capital prudential standards;
- commencing consultation on proposals to implement the Financial System Inquiry's recommendation on a framework for minimum loss-absorbing and recapitalisation capacity;
- finalising requirements for counterparty credit risk;
- meeting with stakeholders and considering submissions on prudential reforms to address problems with strategic and business planning practices within registrable superannuation entities (RSE) licensees' business operations, which would require RSE licensees to undertake regular assessments of outcomes being delivered to members; and
- consulting on proposed prudential requirements for information security risk, and on requirements for operational risk management and revised standards for business continuity and outsourcing.

1.16 Sustainable finance: European Commission report

31 January 2018 - The European Commission's High-Level Expert Group on Sustainable Finance (HLEG) has published its *Final Report*, which sets out strategic recommendations for a financial system that supports sustainable investments.

The report proposes:

- a classification system, or "taxonomy", to provide market clarity on what is "sustainable";
- clarifying the duties of investors when it comes to achieving a more sustainable financial system;
- improving disclosure by financial institutions and companies on how sustainability is factored into their decision-making;
- an EU-wide label for green investment funds;
- making sustainability part of the mandates of the European Supervisory Authorities; and
- a European standard for green bonds.

1.17 US federal securities class action filings reach record high for second straight year

30 January 2018 - The number of US federal securities class action lawsuits filed in 2017 reached a record high for the second straight year, according to *Securities Class Action Filings-2017 Year in Review*, a new report issued by Cornerstone Research and the Stanford Law School Securities Class Action Clearinghouse. The increase was spurred by a sharp increase in lawsuits targeting mergers and acquisitions.

The 412 securities class action filings in 2017 represented a more than 50% increase from the previous record of 271 filings in 2016. It also was more than double the historical average over the previous 20 years and the highest level since the enactment of the *Private Securities Litigation Reform Act of 1995*.

Filings involving M&A transactions increased to 198 and accounted for nearly half of all federal securities class action filings in 2017. This was more than double the number of M&A filings in 2016. In addition, core filings - those excluding M&A claims - rose 15% over the same period. The growth in the number of core filings over the past six years has coincided with activity by three plaintiff law firms, which were typically appointed lead counsel in cases that were smaller than average in size.

The outcomes of securities class action filings in recent cohorts showed higher dismissal rates than in previous years, and filings in the 2017 cohort of core filings are on pace to have the record-highest rate of dismissal within the first year of filing. The report also finds that M&A cases filed from 2009 to 2016 have been dismissed at a much higher rate than other federal filings.

1.18 Report by BIS Committee on the global financial system assesses structural changes in global banking

24 January 2018 - Bank profitability has fallen from pre-crisis peaks but banks have become more resilient to risks, finds a new report by the Committee on the Global Financial System, a standing committee of the BIS. Over the past decade, banks' balance sheets, cost base, scope of activities and geographic presence have been shaped by the impact of the crisis, as well as the resulting changes in regulation, competition and the macroeconomic landscape.

The report, *Structural changes in banking after the crisis*, outlines common trends but also differences across 21 countries. The banking system data, spanning the years 2000-16, are published alongside the report as a comprehensive reference tool.

The report finds that, since the crisis, banks have significantly strengthened their capital and liquidity buffers, as well as their funding structures, in line with the intended direction of regulatory reforms. A stronger banking sector now generally supports the flow of credit to the real economy, although conditions vary across the globe. Many banks directly affected by the crisis have shifted their businesses away from complex and trading activities and have become more selective in their international activities. In contrast, banks less affected by the crisis, including those in many emerging markets, have expanded internationally.

The decline in bank return-on-equity from historically high pre-crisis rates partly reflects lower leverage and risk-taking, but also sluggish revenues and high costs. Longer-term profitability challenges could also signal overcapacity and the need for further structural adjustment supported by robust bank resolution frameworks.

2. Recent ASIC Developments

2.1 Report on credit rating agencies

15 February 2018 - The Australian Securities and Investments Commission (ASIC) has conducted a market-wide surveillance of credit rating agencies (CRAs) and made a number of recommendations for change. The findings of the surveillance are outlined in REP 566 Surveillance of Credit Rating Agencies.

Under the Corporations Act 2001 No. 50 (Cth), CRAs are required to hold an Australian financial services (AFS) licence and to comply with the conditions of the licence, including requirements to comply with the IOSCO *Code of Conduct Fundamentals for Credit Rating Agencies*. CRAs are also required to provide assistance to ASIC, including in relation to their compliance with the Corporations Act. There are currently six licensed CRAs operating in Australia and they all formed part of the surveillance - A.M Best Asia-Pacific Limited, Australia Ratings Pty Ltd, Equifax Australasia Credit Ratings Pty Limited, Fitch Australia Pty Limited, Moody's Investor Services Pty Limited and S&P Global Ratings Australia Pty Ltd.

In this report, ASIC's main areas of focus were the CRAs' governance arrangements (including relating to conflicts of interest and their corporate structure), transparency and disclosure. The report makes a number of observations about CRAs' activities with some leading to recommendations for change in areas such as board reporting, compliance teams and compliance testing, analytical evaluation of ratings and human resources.

2.2 Report on the 2017 annual general meeting season

29 January 2018 - ASIC has published its overview of the annual general meeting (AGM) season for S&P/ASX 200 (ASX 200) listed companies in 2017. Report 564 *Annual general meeting season 2017* (REP 564) examines the voting outcomes of resolutions considered at AGMs held by ASX 200 companies in 2017 and highlights emerging corporate governance issues and trends arising during the season. It discusses remuneration reports, proxy advisers' recommendations, the extent of shareholder engagement, board diversity and the effectiveness of AGMs, including ASIC's recommendations about good corporate governance practices in these areas.

Among the key points:

- the 2017 AGM season had fewer "strikes" on remuneration reports than the 2016 season;
- proxy advisers continued to actively scrutinise governance practices and attract or generate significant media

and corporate commentary; and
- shareholders advocated for action on specific environmental, social and governance issues, with a particular spotlight on board diversity.

3. Recent ASX Developments

3.1 Delisting of Australian Electricity Base Load Calendar $300 Cap futures contracts

As of 18 January 2018, ASX has temporarily withdrawn the Australian Electricity Base Load Calendar Quarter $300 Cap futures for the Q3 and Q4 2021 expiries and the $300 Cap Calendar Year 2021 strip future expiry from ASX 24. This is due to the Australian Energy Market Commission five minute settlement rule change determined in November 2017.

The Notice is available on the ASX Website.

3.2 Monthly activity report

On 5 February 2018 ASX released the ASX Monthly Activity Report for January 2018.

4. Recent Takeovers Panel Developments

4.1 Panel Publishes Consultation Paper - Revised Guidance Note 17 on Rights Issues

23 February 2018 - The Takeovers Panel has published a Consultation Paper seeking public comment in relation to proposed revisions to Guidance Note 17 on Rights issues. The proposed revisions seek to provide clearer guidance about the Panel's approach to rights issues.

Guidance Note 17 was reissued in a new plain English format on 11 February 2010. Since then shortfall facilities (and bookbuilds for unexercised rights in renounceable rights issues) have become more commonplace. The main proposed changes are to:

- rewrite and move the section in relation to mitigating potential control effects;
- provide more guidance in relation to shortfall facilities; and
- explain that a rights issue will generally not be unacceptable if there is a clear need for funds provided an appropriate dispersion strategy has been put in place.

4.2 Bulletproof Group Limited - Panel declines to make declaration

9 February 2018 - The Takeovers Panel has declined to make a declaration of unacceptable circumstances in response to an application dated 19 January 2018 from Macquarie Cloud Services Pty Ltd. Bulletproof is currently the subject of a conditional off-market takeover bid by the applicant (see TP18/03).

The Panel was satisfied that there was no reasonable prospect it would make a declaration of unacceptable circumstances in relation to the independent expert's report. The Panel considered that the applicant's criticisms of the independent expert's report did not go beyond matters of judgment in respect of which experts might reasonably disagree, and noted that it was open to the applicant to set out its critique in a supplementary bidder's statement.

The Panel conducted proceedings in respect of the applicant's submission that the target's statement did not include all information that holders of Bulletproof shares and their professional advisers would reasonably require to make an informed assessment whether to accept the applicant's takeover bid, however was satisfied with the further information provided by the parties.

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

4.3 Quantum Graphite Limited (subject to Deed of Company Arrangement) - Panel declines to make declaration

17 January 2018 - The Takeovers Panel has declined to make a declaration of unacceptable circumstances in response to an application dated 16 January 2018 from Strategic Energy Resources Limited in relation to Quantum Graphite Limited (subject to Deed of Company Arrangement). The application concerned an issue of shares by Quantum on 29 September 2017 and matters relating to Quantum's annual general meeting held on 18 December 2017 (see TP18/02)).

The Panel had concerns regarding the adequacy of disclosure in the notice of annual general meeting and the failure to lodge a substantial holding notice following the 29 September share issue. There was also material regarding the 29 September share issue that, in other circumstances, may have led the Panel to make further enquiries.

However, on balance the Panel considered making a declaration of unacceptable circumstances was not in the public interest, noting the object of Part 5.3A1 of the Corporations Act 2001 No. 50 (Cth) in addition to the matters in s. 657A(3), the potential prejudice to creditors and shareholders if the Deed of Company Arrangement did not proceed as a result of making a declaration and the potential advantages to creditors and shareholders if the Deed of Company Arrangement is fully implemented and shares of Quantum recommence trading on ASX.

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

4.4 Strategic Minerals Corporation NL - Declaration of unacceptable circumstances

2 February 2018 - The Takeovers Panel has made a declaration of unacceptable circumstances in relation to an application by Ms Veronica Oma in relation to the affairs of Strategic Minerals Corporation NL (see TP18/01).

Strategic Minerals is currently the subject of an on-market takeover bid by QGold Pty Ltd. Mr Christopher Wallin is the directing mind and will of QGold. Mr Wallin is also, and has at all relevant times been, a director of Strategic Minerals.

Strategic Minerals undertook a placement in November 2017. The placee was recommended to Strategic Minerals by Mr Wallin at a time when Mr Wallin was considering whether QGold should make a takeover bid for Strategic Minerals. The Panel was concerned that Mr Wallin was involved in the decision to make the placement and to approach the placee, and that the conduct of the placee in taking the placement and selling soon after the announcement of the takeover bid (disregarding Strategic Minerals' advice to take no action) was not consistent with commercially rational behaviour.

The Panel considered unacceptable circumstances arose from these and other matters, including:

- deficiencies in QGold's bidder's statement
- the sale of the placee's shares contributing to QGold acquiring voting power in Strategic Minerals of at least 75% (being the threshold required under ASX Guidance Note 33 to apply for the delisting of Strategic Minerals), which had the potential to coerce shareholders to accept the takeover bid
- deficiencies in the commissioning and engagement of experts to prepare the technical expert's report and independent expert's report included in Strategic Minerals' target's statement and
- due to errors and deficiencies in the technical expert's report, the target's statement not including all the information required under s. 638 of the Corporations Act 2001 No. 50 (Cth);

On 15 February 2018, the Panel made final orders, which in effect require (among other things):

- the issue and dispatch of a supplementary bidder's statement and a supplementary target's statement (including a revised independent expert's report and a revised technical expert's report);
- QGold to provide persons who sold Strategic Minerals shares following the announcement of the takeover bid with the ability to purchase from QGold the number of shares that they sold;
- that the threshold to seek delisting of Strategic Minerals is increased to take into account the shares sold during the takeover bid by the entity who received shares under a placement in November 2017; and
- the payment of costs to the applicant.

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

5. Recent Research Papers

5.1 Socially Responsible Bidding Firms and Acquisitions Decisions: Australian Evidence

This paper examines the knowledge on acquisition decisions by examining whether a firm's corporate social responsibility (CSR) activities influence the choice and Merger and Acquisition (M&A) performance. These empirical results reveal several new insights. First, the authors find that targets with CSR activities are more likely to be acquired by CSR oriented bidder firms. This finding is consistent with the idea that managers of Australian firms that undertake CSR activities are also likely to acquire a target firm with CSR practices. Secondly, the authors also investigate the acquisition decisions and performance of socially responsible bidding firms. They find that the announcement period abnormal return is positive and significant when CSR-oriented bidding firms announce an acquisition decision in the market. Also, they show that socially responsible firms are more likely to pay a lower bid premium when they pay for acquisitions. Finally, the authors demonstrate that CSR firms make investment decisions consistent with shareholders' wealth maximization objectives, suggesting that CSR-oriented firms are better aligned with the other stakeholders of the firm.

Socially Responsible Bidding Firms and Acquisitions Decisions: Australian Evidence

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5.2 Educate to Innovate: Evidence from STEM Directors and Corporate Innovation

In this paper, the authors present evidence that board directors with educational backgrounds in science, technology, engineering, and mathematics (STEM) play a key role in corporate technological progress. This study focuses on firms' innovative performance, measured by patent-based metrics and research and development expenditures, and employs multiple approaches-including a lead-lag model, a change model, and a two-stage least-squares model-to examine the authors' research hypothesis. The authors find that STEM board directors have significant beneficial effects on corporate innovation activities. Furthermore, the results suggest that independent STEM directors also foster corporate innovation.

[Educate to Innovate: Evidence from STEM Directors and Corporate Innovation]

5.3 Eclipse of the Public Corporation or Eclipse of the Public Markets?

Since reaching a peak in 1997, the number of listed firms in the US has fallen in every year but one. During this same period, public firms have been net purchasers of US$3.6 trillion of equity (in 2015 dollars) rather than net issuers. The propensity to be listed is lower across all firm size groups, but more so among firms with less than 5,000 employees. Relative to other countries, the US now has abnormally few listed firms. Because markets have become unattractive to small firms, existing listed firms are larger and older. The authors argue that the importance of intangible investment has grown but that public markets are not well-suited for young, R&D-intensive companies. Since there is abundant capital available to such firms without going public, they have little incentive to do so until they reach the point in their lifecycle where they focus more on payouts than on raising capital.

[Eclipse of the Public Corporation or Eclipse of the Public Markets?]

5.4 Do Pro-Diversity Policies Improve Corporate Innovation?

Using new product announcements, patents, and patent citations as measures of corporate innovation, the authors find that corporate policies that promote more pro-diversity cultures, specifically treatment of women and minorities, enhance future innovative efficiency. This positive effect is stronger during economic downturns and in firms that are more innovative, value intangibles and human capital more highly, have greater growth options, have higher cash flow, and have stronger governance. Pro-diversity policies also increase firm value via this stimulating effect on innovative efficiency. The results of this study suggest a channel through which workforce diversity may enhance firm value.

[Do Pro-Diversity Policies Improve Corporate Innovation?]

5.5 Judicial Intervention in Directors' Decision-Making Process: Section 172 of the Companies Act 2006 (UK)

Section 172 of the *Companies Act 2006* (UK) (which imposes a duty to promote the success of the company) has been criticised for being unfit for purpose in a post-financial crisis world, given that it is very difficult to hold directors liable under this provision. Although courts should not second-guess board decisions, it does not follow that they should be precluded from intervening in boards' decision-making process through the adoption of a searching standard of review when they assess whether directors have breached s. 172. This article advances and defends a framework - the heightened review - to evaluate board decision-making process under this provision. It is argued that the "heightened review" is beneficial to the company and is supported by case law and policy considerations.

[Judicial Intervention in Directors' Decision-Making Process: Section 172 of the Companies Act 2006]

6. Recent Corporate Law Decisions

6.1 No unfair prejudice in proposed transfer of 98% of company's shares to trustees to implement Deed of Company Arrangement

(Dominique Mayo, Clayton Utz)

In the matter of Paladin Energy Limited (subject to a Deed of Company Arrangement) [2018] NSWSC 11, Supreme Court of New South Wales, Black J, 18 January 2018

(a) Summary

The Court considered an application by the Deed Administrators of Paladin Energy Limited for the transfer of 98% of the shares in the company to trustees as required by the Deed of Company Arrangement, in accordance with s. 444GA of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act).

The Court was satisfied that the proposed transfer did not involve prejudice to shareholders in the company in circumstances where the Court found that the shares in the company did not have residual value on a "going concern" basis, or on a "distressed" going concern basis, or in a liquidation which would likely follow from the failure of the application and the consequential failure of the Deed of Company Arrangement.

(b) Facts

The Plaintiffs, Messrs Woods, White and Dickerson as joint and several deed administrators (the Deed Administrators) of Paladin Energy Ltd (subject to Deed of Company Arrangement) (the Company) sought an order under s. 444GA(1) of the Corporations Act that they jointly and severally have leave to transfer 98% of the fully paid ordinary shares of the Company from its members to the trustees in accordance with the terms of a Deed of Company Arrangement (DOCA).

The order sought by this application was a condition precedent to the implementation of the DOCA.

Two shareholders of the Company, Messrs Burrell and Kalfon, were heard in opposition to the application.

On 3 July 2017, the Deed Administrators were appointed as voluntary administrators of the Company. The convening period for the second meeting of creditors of the Company was twice extended by the Federal Court of Australia and, during that period, the following measures were undertaken:

- consideration of the steps previously taken by the Company to realise its assets and secure a recapitalisation;
- consultation with the Company's management and executive in relation to the earlier sale or recapitalisation proposals and the identity of other parties which may have had an interest in acquiring some, or all, of the Company's assets or recapitalising the Company and may have had the financial capacity to complete the transaction;
- identification of a number of parties which they considered may have had an interest in acquiring the Langer Heinrich mine, or an interest in it; and
- seeking out expressions of interest in submitting a proposal to restructure or recapitalise the Company, or purchase some, or all, of its assets.

None of the above measures were successful.

The second meeting of creditors of the Company was held on 7 December 2017 and the Company's creditors resolved to execute a DOCA.

The Plaintiffs relied on the independent expert report of Mr Jaski of PPB Corporate Finance, which addressed the extent of the assets and debts of the Company and the estimated dividend to unsecured creditors and shareholders of the Company if the Company was placed into liquidation.

Mr Jaski assessed the value of the shares in the Company on two alternative bases.

The first was a "going concern" basis, on the assumption that the Company would continue to operate for the foreseeable future, and would be able to realise its assets and discharge its post-administration liabilities in the normal course of business, which assumption was not supported by the evidence and, thus, the valuation was of little relevance for the purposes of determining the application.

Alternatively, and more relevantly, Mr Jaski assessed the value of shares in the Company on a "distressed" basis, adopting a going concern valuation as a starting point and then discounting that valuation by reference to the Company's current circumstances, including the fact that it did not have sufficient funds available to pursue normal operations into the foreseeable future.

(c) Decision

Black J formed the view that the evidence established that the deficiency in the Company's assets against its debts was such that its equity had no value, on a going concern basis, on a "distressed" going concern basis, or in a liquidation, and a liquidation was the likely outcome if the application were to fail.

His Honour accepted that there appeared to be no present prospect of a capital raising or other injection of funds which might enable the Company to continue to trade or avoid liquidation if the application was not approved and the DOCA could not be effected.

His Honour also accepted that the DOCA represented the best outcome for creditors of the Company and that there would be no return to shareholders on a liquidation. It followed that there was no economic prejudice, or unfair prejudice, to shareholders if the transfer of shares contemplated by the DOCA was to be allowed. His Honour considered that a position by which existing shareholders retained 2% of the equity in the Company was, albeit marginally, more advantageous to shareholders than a liquidation, and there was no evidence to suggest that any other alternative was available.

Whilst Black J heard the various arguments advanced by the two shareholders who opposed the application, his Honour noted that:

- the question which the Court must determine is whether the proposed transfer of shares in the Company is unfairly prejudicial to shareholders, not whether it is possible to hypothesise some other transaction, which does not presently exist, that would have been more favourable to shareholders;
- the issue of notes (contemplated by the DOCA) was conditional upon the terms of the DOCA being met and the execution of the transaction. The position after bondholders have converted their debt to equity would not establish the value of the Company before that note issue occurred;
- s. 444GA draws attention to the prejudice, or unfair prejudice, to shareholders of a transfer of shares where a company is subject to a DOCA, and that will commonly reflect, at least, a degree of previous misfortune, and often a proposal put by creditors to obtain a controlling equity interest in the company on surrender of their debt; and
- it is not open to the Court to consider a "modified version" of the DOCA involving different terms, as submitted, in an application of this kind, where the Court may either grant leave for the relevant transaction if

it is not unfairly prejudicial to shareholders, or decline to do so either because it is unfairly prejudicial to shareholders or because there are discretionary reasons to decline such leave.

Ultimately, his Honour was not satisfied that the transaction was unfairly prejudicial to shareholders, or that any discretionary basis to decline such leave had been established. His Honour considered that it would not be a proper exercise of the Court's statutory power under s. 444GA to refuse to approve the transaction based upon speculation that, if that course were taken, some other proposal which had not yet been articulated might emerge, rather than the Company being placed in liquidation.

6.2 Doubt cast on the legality of certain lender/financial adviser business models targeted at people in difficult financial circumstances

(Yannis Goutzamanis, Solicitor, King & Wood Mallesons)

Australian Securities and Investments Commission v Financial Circle Pty Ltd [2018] FCA 2, Federal Court of Australia, Moshinsky J, 10 January 2018

(a) Summary

The Federal Court of Australia recently delivered a judgment which casts doubt on the legality of certain lender/financial adviser business models targeted at people in difficult financial circumstances. Specifically, the Court held that there was an appreciable risk that the defendant, who had been carrying on such a business model, was in breach of various statutory consumer protection, financial advice and consumer credit obligations.

(b) Facts

This case concerned ASIC's application for a series of interlocutory injunctions to prevent the defendant company (Financial Circle) from carrying on its lender/financial adviser business. ASIC based its application on four alleged breaches of the following statutory provisions:

- s. 12CB of the Australian Securities and Investments Commission Act 2001 No. 51 (Cth) (the ASIC Act), which prohibits unconscionable conduct in connection with financial services;
- ss. 12DA and/or 12DF of the ASIC Act and s. 1041H of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act), which prohibit misleading and deceptive conduct;
- ss. 912A and 961L of the Corporations Act, which set out various obligations for financial services licensees (including the obligation to do all things necessary to ensure that the financial services are provided efficiently, honestly and fairly); and
- s. 29 of the National Consumer Credit Protection Act 2009 No. 134 (Cth) (the National Credit Act), which prohibits the unauthorised provision of credit.

ASIC alleged that the breaches of these provisions all flowed from Financial Circle's business model, under which:

- Financial Circle would offer loans to persons in difficult financial circumstances;
- these loans were conditional on the borrower also obtaining (and paying for) financial advice from Financial Circle;
- the requirement to obtain (and pay for) this financial advice was not actively disclosed until late in the loan application process; and
- Financial Circle would not only receive revenue from interest payments and fees charged to clients, but also from commissions paid by third party superannuation and insurance providers whenever a client

implemented Financial Circle's advice to change provider (which occurred in almost all cases).

(c) Decision

(i) Relevance of the WRM proceedings

One noteworthy aspect of this decision was the fact that many of Financial Circle's shareholders, directors and key personnel were also involved in a group of companies (the Fuoco Group) that previously operated a similar business model.

The Fuoco Group was ultimately subject to a successful interlocutory injunction application by ASIC in May 2017 (which was also heard before Moshinsky J) in *Australian Securities and Investments Commission v Wealth & Risk Management Pty Ltd* [2017] FCA 477 (the WRM proceedings).

Moshinksy J acknowledged that there were certain similarities between the cash rebate scheme operated by the Fuoco Group in the WRM proceedings and Financial Circle's business model. However, his Honour ultimately held that the question of whether an interlocutory injunction should be granted against Financial Circle could not be resolved solely by reference to the WRM proceedings. Rather, the Court was required to make its own independent assessment of Financial Circle's business model and conduct.

(ii) Unconscionable conduct (s. 12CB ASIC Act)

Moshinsky J held that there was an appreciable risk that Financial Circle was engaging in unconscionable conduct. His Honour based this finding on the following facts:

- Financial Circle specifically targeted a market of persons in difficult financial circumstances who needed small value loans;
- Financial Circle did not initially disclose the fact that the provision of the loan was conditional upon the applicant obtaining (and paying for) financial advice from Financial Circle; and
- in many cases the financial advice fee was greater than the value of the loan (e.g. Moshinsky J set out examples of persons obtaining loans of roughly $3000 but being charged financial advice fees of $5500 which were deducted from their superannuation).

In making this finding Moshinsky J also rejected Financial Circle's argument that the requirement to obtain financial advice (and the cost of the advice) was disclosed prior to the client committing to the arrangement. Moshinsky J stated that whilst this was technically true, the relevant information was not easily discerned from Financial Circle's website (i.e. it was contained in terms and conditions that were difficult to locate) and the client was not actively informed about these matters until the loan application process had reached an advanced stage.

(iii) Misleading and deceptive conduct (ss. 12DA, 12DF ASIC Act; s. 1041H Corporations Act)

Moshinsky J held that there was an appreciable risk that Financial Circle was engaging in misleading and deceptive conduct. His Honour based this finding primarily on the fact that it was not made clear until an advanced stage of the loan application process, that the loan was conditional upon the applicant obtaining (and paying for) financial advice.

(iv) Financial services obligations (ss. 912A, 961L Corporations Act)

Moshinsky J held that there was an appreciable risk that Financial Circle was breaching various financial services obligations contained in Chapter 7 of the Corporations Act. His Honour based this finding on the following facts:

- it could be reasonably inferred that, in many cases, the client would not have been willing to obtain and

implement the advice, and pay the fee, were he or she not in financial difficulty and in need of a loan;
- Financial Circle seemed to be exploiting the client's position of financial difficulty and the client's need for a loan in order to derive lucrative advice fees and commissions. There was therefore an appreciable risk that the financial advice was not being provided "fairly";
- the cost of the financial advice was often substantial relative to the amount of the loan and as a percentage of the client's superannuation balance;
- the advice was generic in nature and almost always recommended switching insurance providers. This raised a serious question as to whether the advice was appropriately tailored to the client's circumstances.

(v) Unauthorised provision of credit (s. 29 National Credit Act)

Moshinsky J held that there was an appreciable risk that Financial Circle was providing credit without proper authorisation. His Honour found that the evidence established that Financial Circle's credit licence only authorised it to engage in credit activities other than as a "credit provider". However, in a number of loan documents, Financial Circle was named as the "lender", and Financial Circle thus appeared to be acting as a credit provider.

6.3 Judicial discretion to reinstate the registration of a company previously deregistered by its directors

(Rebecca Searle, King & Wood Mallesons)

Yeo v Australian Securities and Investments Commission, in the matter of Ji Woo International Education Centre Pty Ltd (deregistered) [2017] FCA 1480, Federal Court of Australia, Gleeson J, 8 December 2017

(a) Summary

The Federal Court of Australia recently delivered a judgment which sheds light on when a court may order ASIC to reinstate the registration of a company which has been deregistered.

The court is granted discretion to make such an order under s. 601AH(2) of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act). This provision outlines certain factors to consider before exercising this discretion, including whether the person applying to the court for the order was aggrieved by deregistration of the company, and whether reinstatement of the company's registration is just.

The company, Ji Woo International Education Centre Pty Ltd (Ji Woo), was deregistered pursuant to s. 601AA of the Corporations Act. The plaintiff sought an order that the defendant, ASIC, reinstate the registration of Ji Woo, asserting that as a shareholder she had not given her required consent to deregistration, and also that she had been deprived of her proportion of the company's value upon deregistration and was therefore aggrieved by deregistration.

The lack of credible evidence in opposition to reinstating Ji Woo's registration was pertinent to Gleeson J's finding that the plaintiff had been aggrieved by deregistration, and that reinstatement of Ji Woo's registration and appointment of a liquidator to investigate potential claims Ji Woo had to certain assets was just.

(b) Facts

Ji Woo was incorporated in 2003. It carried on an educational consulting business, providing referral services for overseas students who wished to study in Australia, and deriving revenue by way of commission from educational institutions to which it referred students. By 2013, Ji Woo traded under the business name "IBN Education".

The plaintiff, Myounghwa Yeo (Ms Yeo) was a former shareholder (holding shares at the time of Ji Woo's deregistration) and a former employee of Ji Woo. Ji Woo's two remaining shareholders were Chi Hoon Choi (Mr Choi), who was also the sole director of Ji Woo at the time of deregistration, and Hye Young Han (Ms Han). Ms Han was the de facto partner of Bo Hyun Lee (Mr Lee). Mr Lee had incorporated Ji Woo and had previously been a director of the company.

On 9 November 2016, on the application of Mr Choi, Ji Woo was deregistered. Section 601AA(2) of the Corporations Act allows a director of a company to apply for deregistration if all members agree to the deregistration, and if the company's assets are worth less than $1,000.

Ms Yeo asserted that she did not consent to deregistration of the company and that Ji Woo had substantial assets in the form of its business, IBN Education. This business had been transferred to a different company, IBN Global Pty Ltd (IBN Global) for no consideration and to the detriment of Ji Woo, and allegedly without Ms Yeo's consent. IBN Global's directors were Mr Choi and Ms Han, and it was owned by Mr Lee, Mr Choi and Ms Han. IBN Global registered the business name IBN Education in December 2013, and started operating from January 2014.

Ms Yeo argued that the business was held on trust by IBN Global for Ji Woo, so Ji Woo's assets were greater than $1,000. Ms Yeo further argued that her interests were harmed when the company was deregistered and she did not receive her proportion of the company's assets.

For these reasons, Ms Yeo contended that Mr Choi should not have applied to deregister Ji Woo. Ms Yeo applied to the court for an order that ASIC reinstate Ji Woo's registration, and an order that the company be wound up and a liquidator be appointed to investigate the circumstances in which Ji Woo's business was transferred to IBN Global for no consideration.

Section 601AH(2) of the Corporations Act allows the court to make an order reinstating a company's registration where:

- an application for reinstatement is made to the court by a person aggrieved by the deregistration (or a former liquidator of the company);
- the court is satisfied that it is just for the company's registration to be reinstated; and
- the court elects to exercise its discretion in making such an order.

ASIC neither consented to nor opposed the order. Mr Choi appeared as an intervener and opposed the order, arguing that Ms Yeo was not aggrieved by the deregistration and that reinstatement would not be just. Mr Choi argued that Ms Yeo relinquished her rights as a shareholder after she was found to have embezzled money from Ji Woo. Because of this it was unclear what rights Ms Yeo could assert, and reinstatement would be premature. Further, Mr Choi contended that because Ms Yeo caused detriment to the company, she could not claim to be aggrieved.

(c) Decision

Gleeson J cited Jagot J's statement from *Deputy Commissioner of Taxation v Australian Securities and Investments Commission; re Civic Finance Pty Limited (Deregistered)* [2010] FCA 1411; (2010) 81 ATR 456 at [14] that it is "often not appropriate in an application for reinstatement to go into factual matters." The court will not second guess the outcome of a prospective winding up or decide whether reinstatement will be futile. Gleeson J therefore did not analyse the factual issues, but focussed on the statutory factors from s. 601AH(2) of the Corporations Act.

(i) Was Ms Yeo a person aggrieved?

Gleeson J noted that the threshold for determining whether a person is aggrieved by deregistration is low and should not be narrowly construed. As long as the claim is not plainly hopeless and bound to fail, it should proceed.

The fact that a person was a shareholder of a company and is now dissatisfied is not in itself sufficient to render them aggrieved. They must have an interest that has been diminished or prejudiced (for example where a right or value or potential value has been extinguished) which distinguishes them from a bystander. Courts should look for damage or injury in a legal sense. This includes where a former shareholder will benefit from reinstatement by sharing in the assets of the company (as discussed in C*allegher v Australian Securities and Investments Commission* [2007] FCA 482, citing *Casali v Crisp* [2001] NSWSC 860).

Ms Yeo alleged that she did not agree to Ji Woo's deregistration, which deprived her of her valuable shareholding in the company (the value being the business IBN Education). Gleeson J held that Ms Yeo had a potential claim to her respective proportion of the value of IBN Education. Whether Ms Yeo consented to the transfer of the business to IBN Global was a factual matter which was not appropriate for Gleeson J to resolve. A liquidator would investigate the transfer of IBN Education to IBN Global, and as Ms Yeo's claim was not plainly hopeless, Gleeson J considered that she was aggrieved by the deregistration.

(ii) Was an order to reinstate the registration of Ji Woo just?

This consideration confers broad discretionary judgment on the court, which should consider the circumstances in which the company was deregistered, the purpose in reinstating registration, whether any person is likely to be prejudiced by reinstatement, and public interest generally (*Re ERB International Pty Ltd (deregistered)* [2014] NSWSC 200). Certain factors may lead a court to determine that reinstatement is not just, including where the applicant has delayed asserting any rights or making a claim and this delay has caused detriment to other parties.

In this case, Gleeson J held that reinstatement would allow for the appointment of a liquidator to investigate possible claims by Ji Woo against IBN Global. Further, there was no evidence of any likely prejudice resulting from reinstatement, and public policy favoured reinstatement to enable the proposed investigation. Conversely, Gleeson J considered that Ms Yeo's possible consent to the transfer of business to IBN Global would render reinstatement unjust. On the balance of these considerations, Gleeson J was of the opinion that reinstatement was just, notwithstanding the uncertainty regarding Ms Yeo's consent to the transfer of IBN Education.

(iii) Should the Federal Court exercise its discretion on the current facts?

Gleeson J considered that where positive findings are made on the first two matters, then in the ordinary course an order for reinstatement will be made, and discretion was exercised.

In exercising discretion, Gleeson J noted that Mr Choi's evidence, and evidence in support of his claims, was not credible. Claims were not verified by documentation, and much evidence was conflicting. Evidence regarding Ms Yeo's alleged embezzlement and subsequent relinquishing of her shareholding was unclear and unsubstantiated. Serious discrepancies in the evidence led Gleeson J to conclude that the evidence brought in opposition to reinstatement of Ji Woo's reinstatement included detailed fabrications. Gleeson J rejected Mr Choi's claims.

Gleeson J also considered the relevance of concurrent criminal proceedings against Ms Yeo in Korea. Whilst he allowed the hearing to be re-opened to admit this evidence and accepted that the evidence was relevant to an assessment of Ms Yeo's credibility, he held that Ms Yeo's custodial sentence resulting from the criminal proceedings did not weigh against reinstatement of the company. This is because any investigation following reinstatement would not focus on Ms Yeo's credibility.

(iv) Order for winding up

Section 461(1)(k) allows a court to make an order for the winding up of a company if the court is of the opinion that it is just and equitable that the company be wound up.

Gleeson J held that because reinstatement was just, and because Mr Choi deregistered the company without Ms Yeo's consent, winding up was just and equitable.

(v) Costs

Mr Choi's intervention substantially complicated the matter, and he presented and relied on evidence which Gleeson J disbelieved. Therefore Mr Choi was ordered to pay the costs of the proceeding.

6.4 Remunerating invalidly appointed liquidators and administrators

(Rebecca Roach and Connor Davies, Ashurst)

Kreab Gavin Anderson (Australia) Ltd, in the matter of Kreab Gavin Anderson (Australia) Ltd (No 3) [2017] FCA 1473, Federal Court of Australia, Yates J, 8 December 2017

(a) Summary

Reasonable remuneration may be payable to invalidly-appointed administrators and liquidators where:

- the work performed has conferred an incontrovertible benefit on the company; and
- it would be unconscionable for the company to retain the benefit of the work without paying reasonable remuneration.

(b) Facts

Simon John Thorn and Bradley John Tonks (the Applicants) served in a number of roles for Kreab Gavin Anderson (Australia) Ltd (the Plaintiff), namely as:

- administrators from 6 December 2016 to 21 February 2017;
- liquidators from 18 January 2017 to 21 February 2017; and
- provisional liquidators from 21 February 2017 to 24 March 2017.

During their service, the Applicants endeavoured to sell the Plaintiff's business as a going concern and to promote a management buyout. Both endeavours were unsuccessful. The Applicants continued to trade the Plaintiff's business until 23 December 2016, at which time it was decided that any future trading would be unprofitable. Additionally, the Applicants carried out investigations into the Plaintiff's affairs and provided a report of those investigations to its creditors.

At a meeting of the Plaintiff's creditors on 18 January 2017, the Applicants' remuneration as administrators was approved in the sum of $72,722.50 for the period to 31 December 2016, with provision for up to $40,000 additional future remuneration. As liquidators, their remuneration until liquidation was approved up to $50,000. The total remuneration approved by the creditors exceeded the $111,780 claimed by the Applicants in respect of those roles.

In an earlier decision, the Court had held that the appointments of the Applicants as administrators and liquidators were invalid. Their appointments as provisional liquidators were not in issue. Notwithstanding that two of their appointments were invalid, the Applicants applied to the Court for remuneration from the Plaintiff in respect of all three roles.

(c) Decision

The Court surveyed a number of English and Australian cases in respect of whether - and in what circumstances - an invalidly appointed administrator or liquidator can claim remuneration for work performed. His Honour found no uniform application of principle in the cases, but suggested the balance of authority lay with Young J's decision in

Monks v Poynice Pty Ltd (1987) 8 NSWLR 662 (Monks), which set out that remuneration should be paid for services provided by an invalidly appointed company officer (including a receiver under a charge) where:

> .the service conferred an incontrovertible benefit on the defendant and it would be unconscionable to keep the benefit of the service without paying a reasonable sum therefor.

The Court elected to apply the principle in Monks to the Applicants' case.

The Court was satisfied that, from 6 December 2016 until 21 February 2017, the Applicants proceeded on the basis that they had been validly appointed as administrators and then as liquidators. The Court declared that the Applicants were entitled to reasonable remuneration for the work carried out by them, including by their partners and staff, whilst purporting to act in those roles. The Applicants' entitlement to remuneration was established because:

- the work that they performed conferred an incontrovertible benefit on the Plaintiff; and
- it would be unconscionable for the Plaintiff to retain the benefit of the work without paying their reasonable remuneration.

The Court ordered that the amount of remuneration in respect of the Applicants' work as administrators and liquidators be determined by the New South Wales District Registrar of the Court (the District Registrar). The Court additionally ordered that the Applicants' remuneration as provisional liquidators be determined by the District Registrar pursuant to r. 16.1(1) of the Federal Court (Corporations) Rules 2000 1999 No. 359 (Cth).

6.5 Arranger of new issue owes duty of care to investors

(Anna Delgado, Abradat Kamalpour, James Coiley and Tim Morris, Ashurst)

Golden Belt 1 Sukuk Company BSC(c) v BNP Paribas [2017] EWHC 3182 (Comm), England and Wales High Court of Justice (Commercial Court), Males J, 7 December 2017

(a) Summary

A ground-breaking judgment of the England and Wales High Court has established that a duty of care is owed to investors by a bank which has assisted a borrower to arrange a publicly listed capital market issue. Although the case concerned an Islamic financing transaction, widely known as a sukuk, the terms of the judgment suggest that this duty of care exists in the vast majority of new issues of securities where English law is relevant.

This judgment raises many questions for banks and other parties actively involved in arranging new issues of securities. A number of current market practices may be revisited as a result of this judgment and there may now be a period during which new practices evolve in response to its implications.

This case concerned a new issue of sukuk certificates to raise money for a company registered in Saudi Arabia. It was effected by an extensive suite of transaction documents (the Transaction Documents) most of which were expressed to be governed by English law. However, one of them, a Promissory Note issued by the Saudi company, was expressed to be governed by the laws of Saudi Arabia.

Following a default in payments under the certificates it became apparent that the Promissory Note had not been properly executed. Subsequently some certificate holders brought an action against the bank described as the Arranger of the issue on the basis that the Arranger owed the holders a duty to exercise reasonable care and skill to ensure that the Transaction Documents were properly executed and that the holders had suffered a foreseeable loss as a result of the Arranger's failure to fulfil that duty.

(b) Facts

(i) The Offering Circular

The issue was marketed on the basis of an Offering Circular in conventional form for this type of transaction, including typical responsibility statements. On the front cover of the Offering Circular various banks were identified as Lead Managers or Joint Lead Managers and one of them was identified as Arranger and Sole Bookrunner. The inside front cover of the Offering Circular contained a relatively standard disclaimer to the effect that the Lead Managers, one of which was the Arranger and Sole Bookrunner, made no representation or warranty and accepted no responsibility as to the accuracy or completeness of the information in the Offering Circular.

(ii) The role of arranger

The front cover of the Offering Circular described the Arranger as the "Arranger and Sole Bookrunner" but its responsibilities in this capacity were not further defined. Expert evidence to the court agreed that:

- although a sukuk has to be structured in order to comply with Shari'ah law, this makes no real difference to the role of an arranging bank which will be essentially the same as in the case of a conventional Eurobond issue;
- there is no fixed list of tasks or responsibilities associated with a title such as "Arranger" or "Bookrunner"; and
- nevertheless some tasks will be common to all such transactions and one of these is to ensure that the transaction documents are properly executed.

(iii) Duty of care

In this type of transaction there is no express provision by which an Arranger assumes a duty of care to any investors. To the extent that the transaction documents address this issue at all it is to seek to disclaim liabilities to the investors on the part of the Arranger. Indeed counsel for the Arranger argued that the parties had carefully constructed an elaborate contractual scheme which described in detail the rights and obligations of the various parties and therefore the court should not impose upon this scheme any additional duties.

However, the circumstances in which, in the absence of an express provision, a duty of care will be found to exist in English law are well established and are often summarised as the threefold test: whether loss to the claimant was a reasonably foreseeable consequence of what the defendant did or failed to do; whether the relationship between the parties was one of sufficient proximity; and whether in all the circumstances it is fair, just and reasonable to impose a duty of care on the defendant towards the claimant.

(iv) Duty of care in relation to the Promissory Note

The court considered, amongst other things, whether the Arranger owed investors a duty of care to arrange for proper execution of the Promissory Note.

On the first limb of the threefold test the judge had no difficulty in concluding that loss to certificate holders was a reasonably foreseeable consequence of the Arranger failing to ensure proper execution of the Promissory Note. In this structure the Promissory Note had one purpose only. That was to provide certificate holders with a simple and relatively straightforward claim against the obligor in the event of a default under the certificates.

On the question of proximity, it was the Arranger which ensured that it was prominently described as such on the front of the Offering Circular as it wanted the market as a whole, including prospective investors, to understand the prominent role which it had played in bringing the issue to market. Any prospective investor would understand (as the Arranger wanted investors to understand) that the Arranger had been responsible for the preparation of the

Offering Circular and the preparation and execution of the Transaction Documents. Prospective investors would know that the Arranger had its own interests, both financial and reputational, in ensuring that these responsibilities had been properly discharged.

On the final limb, the judge found that to impose a duty to ensure proper execution would not require an arranging bank to do anything which it would not do in any event, it would not in any way undermine the contractual structure and it would be consistent with the Offering Circular, including the usual disclaimers.

(v) Disclaimers

In this context, it is important to note that the usual disclaimers of responsibility for the contents of the Offering Circular should not be conflated with disclaimers of responsibility for ensuring proper execution of the Transaction Documents. It is one thing for an arranging bank to disclaim responsibility for what it is told by its client (the disclosure in the Offering Circular). It is quite another for an arranging bank to disclaim responsibility for the proper performance of its own functions (such as taking reasonable care to ensure proper execution of the Transaction Documents). There was no suggestion in any of the disclaimers in the Offering Circular for this issue that the Arranger sought to disclaim any responsibility of this latter type.

The judge accepted that it is open to an arranging bank to include an express disclaimer negativing any responsibility to ensure that an important document for the protection of investors is properly executed. However, his opinion was clearly that a bank which wanted to disclaim such responsibility would need to do so in clear terms with all the negative implications for the success or otherwise of the issue that such a disclaimer might involve.

(vi) Primary market vs secondary market

It is also important to note in the context of this duty of care that the judge found there is no difference between immediate purchasers of certificates in the primary market and those who purchased subsequently in the secondary market after issue. Indeed the claimants in this case were secondary market purchasers. It was clearly in the contemplation of all parties including the Arranger that a secondary market in the certificates would develop and that was one of the Arranger's stated intentions. Also the Offering Circular was provided not only to prospective subscribers at the time of issue but was made available to prospective subsequent purchasers of certificates in the secondary market.

(c) Decision

This is the first time in English law that a duty of care has been found to be owed to investors by a bank which has assisted a borrower to arrange a publicly listed securities issue. While this case involved a sukuk structure in which an underlying Promissory Note played a key role, it has nevertheless established an important principle with potentially much wider application. There is also much interesting commentary in the judgment on other aspects of the transaction documentation. This includes the arranging bank's responsibility for the contents of an offering circular and the extent to which it may disclaim that responsibility, and common practices for execution of transaction documents in an international context.

In the light of this judgment arranging banks (and others) will likely wish to revisit the scope of the disclaimers which they typically seek to include in offering documents to describe more precisely the extent of the responsibilities which they are prepared to accept and the things for which they are not prepared to accept responsibility. This may have consequential effects on the description of risk factors in the offering documents.

Where a new issue is arranged and managed by a syndicate, the syndicate members may wish to describe in some detail their respective roles and responsibilities with related disclaimers tailored accordingly. There may also be less enthusiasm amongst potential syndicate members to be named as such in offering documents if they do not in practice intend to play an active role in the new issue process. The more complex the structure of the new issue the more the implications of this judgment are likely to come into focus.

6.6 Removal of director pursuant to shareholders agreement declared invalid

(David Hertzberg, Corrs Chambers Westgarth)

Shearwood (Trustee), in the matter of Allied Resources Partners Pty Ltd v Allied Resources Partners Pty Ltd [2017] FCA 1451, Federal Court of Australia, Markovic J, 6 December 2017

(a) Summary

The plaintiff was purportedly removed as a director of the first defendant company, Allied Resource Partners Pty Ltd (Allied), pursuant to a mechanism in the Allied Shareholders Agreement.

The Federal Court of Australia declared that the purported removal was beyond power, invalid and ineffectual. The Court also declared that the purported appointment of the second defendant, Mr Raftopulos, as a director of Allied pursuant to the Shareholders Agreement and/or the Allied Constitution was beyond power, invalid and ineffectual.

After finding that the removal and appointment were beyond power, invalid and ineffectual, Markovic J considered that s. 1322 of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act), which deals with procedural irregularities, had no application in this case.

(b) Facts

At the time of the purported removal of the plaintiff as a director, Allied had two directors: the plaintiff and Mr Daniel Peters. The plaintiff was also a substantial shareholder of Allied.

In May 2017, Mr Peters sent a "Default Notice" to the company secretary of Allied. It stated that Mr Peters had been made aware of breaches of and non-compliance with the provisions of the Shareholders Agreement by the plaintiff. These alleged breaches and non-compliances related to the distribution of confidential information by the plaintiff, and the plaintiff purporting to act on behalf of Allied without the requisite approvals.

The Default Notice was sent pursuant to cl 15 of the Shareholders Agreement, which was titled "Events of Default". It provided, relevantly, that if a Default Notice was served "each Director, including themselves, appointed by the Defaulting Shareholder is automatically removed".

In June 2017 Mr Peters, acting in reliance upon the Default Notice and cl. 15 of the Shareholders Agreement, took steps to remove the plaintiff as a director of Allied, and immediately took steps to appoint Mr Raftopulos as a director of Allied.

The Allied Constitution provided a mechanism for the appointment of directors if the number of directors in office was not sufficient to constitute a quorum at a meeting of directors. Mr Raftopulos was purportedly appointed as a director of Allied pursuant to that mechanism.

The plaintiff wrote to Allied, disputing that he had breached any provision of the Shareholders Agreement or the Constitution, and disputing that he had been validly terminated as a director of Allied. However, for the purposes of the Federal Court proceedings the plaintiff did not dispute the validity of the Default Notice.

There was no shareholder vote in respect of the removal of the plaintiff or the appointment of Mr Raftopulos.

(c) Decision

(i) How was the plaintiff appointed as a director?

As cl 15 of the Shareholders Agreement provided for the automatic removal of a director appointed by a Defaulting Shareholder, an important issue in the proceedings was whether the plaintiff was appointed as a director:

- by a Defaulting Shareholder, that is, appointed by himself;
- by operation of s. 120(1) of the Corporations Act, read with s. 117(2); or
- by operation of the Constitution and the Shareholders Agreement, which specified that the plaintiff would be an initial director of Allied.

Section 117 deals with the registration of a company by lodgement of an application with ASIC. Section 117(2) specifies what must be stated in the application, including the names of those persons who consent to becoming a director of the company. Section 120(1) provides, relevantly, that a person becomes a director of a company on registration if the person is specified in the application with their consent as a proposed director of the company.

Markovic J held that the plaintiff was appointed as a director of Allied upon its registration by force of s. 120(1) of the Corporations Act, read with s. 117(2). Thus, he was not appointed by operation of the Constitution and the Shareholders Agreement. Those documents merely reflected what had occurred by force of ss. 117 and 120. Nor was he appointed by himself, as contended by Allied. Accordingly, her Honour said that the plaintiff was not appointed by a Defaulting Shareholder.

(ii) Was the plaintiff effectively removed as a director?

Markovic J found that, because the plaintiff was not appointed by a Defaulting Shareholder, cl 15 was not engaged and could not operate to automatically remove him as a director. Accordingly, her Honour held that the plaintiff remained a director of Allied notwithstanding the service of the Default Notice.

Allied also contended that, because the Shareholders Agreement provided that the initial term of a directorship would be three years, the plaintiff's terms as a director came to an end on 2 June 2014, three years after his appointment, and from that time forwards he was either a de facto or shadow director. It said that he ceased to be a de facto or shadow director in May 2017 because the other members of the board at that time were no longer accustomed to act in accordance with his directions or no longer permitted him to act as a director. Markovic J rejected this argument. Her Honour held that the terms of the Shareholder Agreement did not serve to remove a director after the initial three year term; something more was required to remove the plaintiff as a director, and that did not occur in this case.

(iii) Was the second defendant validly appointed as a director?

It followed that, because the number of directors of Allied had at no stage been insufficient to constitute a quorum, the provision of the Constitution relied upon to appoint Mr Raftopulos was not engaged. Accordingly, Markovic J found that the purported appointment was beyond power, invalid and ineffectual.

(iv) Did s. 1322 of the Corporations Act operate to validate the removal of the plaintiff as a director?

Section 1322 of the Corporations Act deals with procedural irregularities. Section 1322(2) provides:

> A proceeding under this Act is not invalidated because of any procedural irregularity unless the Court is of the opinion that the irregularity has caused or may cause substantial injustice that cannot be remedied by any order of the Court and by order declares the proceeding to be invalid.

Section 1322(4) also confers a broad discretion on the Court to make certain orders, including, under s. 1322(4)(a), orders declaring that an act purporting to have been done is not invalid by reason of any contravention of a provision of the Corporations Act or of the constitution of a corporation.

Markovic J said that s. 1322(2) did not apply to the purported removal of the plaintiff as a director. Her Honour observed that, while the removal of a director is a "proceeding", it was not "under" the Corporations Act in this case. Rather, the purported removal was effected by operation of cl 15 of the Shareholders Agreement.

Her Honour was also of the view that the removal of the plaintiff as a director was not a "procedural irregularity" that would attract the protection of s. 1322(2).

Her Honour also refused to make an order under s. 1322(4)(a). Her Honour considered that the purported act was invalid by reason of contravention of the Shareholders Agreement, not by reason of contravention of the Corporations Act or the Allied Constitution, and so there was no relevant contravention to which s. 1322(4)(a) could attach. Her Honour was also not satisfied that it was just and equitable that an order be made pursuant to s. 1322(4)(a), and that no substantial injustice would be caused to any person, as required by s. 1322(6)(a) and (c) respectively. In this regard, her Honour noted that the plaintiff was removed as a director in circumstances where there was no power to do so. Had a different procedure been used, there may have been a different result. Accordingly, her Honour held that s. 1322 had no application in this case.

6.7 Application to inspect company books where there is suspected breach of directors' duties

(Nikki Dalla Valle, Herbert Smith Freehills)

In the matter of Sirrah Pty Ltd [2017] NSWSC 1683, Supreme Court of New South Wales, Black J, 5 December 2017

(a) Summary

Mr Gregory Harris and Ms Monica Brown (the Plaintiffs), as Executors of the Estate of their late mother Ms Aileen Harris, sought an order under s. 247A of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) authorising them, or their solicitor on their behalf, to inspect books and records of the Defendant, Sirrah Pty Ltd (Sirrah) within 38 categories of documents.

The Court found that the Plaintiff's application was in good faith and for a proper purpose and granted the inspection of company books for the majority of the categories. Black J also limited the scope of some categories and denied the inspection of some categories of documents for reasons detailed below.

(b) Facts

Sirrah was a company incorporated in 1963 and conducted a nursing home in Westmead, New South Wales. Ms Aileen Harris and Mr Robert Harris were originally shareholders in Sirrah and in 2002 Mr Robert Harris resigned as the company director and secretary at which point his son, Mr William Harris, was appointed as director and secretary of Sirrah.

In 2003, 341 new shares in Sirrah (equating to 47.2% of the issued capital in Sirrah) were issued to Harris Health Care Pty Ltd (Harris Health Care), a company associated with Mr William Harris (the 2003 transaction). Shares in Sirrah were also issued to each of Ms Aileen Harris and Mr Robert Harris as part of the 2003 transaction. In 2009 Ms Aileen Harris transferred a further 50 shares to Harris Health Care which appeared to be associated with her entry into a deed with Mr William Harris and Harris Health Care in which he gave up claims under her will (2009 transaction). Ms Aileen Harris also transferred 50 shares to each of her sons and daughters except Mr William Harris and one other daughter who did not wish to receive the shares.

Ms Aileen Harris died on 25 March 2016 and the Plaintiffs were granted probate of her will.

(i) Legal principle

Section 247A(1) of the Corporations Act permits the court, on the application of a member of a company to make an order authorising the applicant to inspect books of the company. The Court can make such an order where it is satisfied that the applicant is acting in good faith and that the inspection is for a proper purpose.

Section 247A(3)-(4) permits a person who is granted leave to bring derivative proceedings under s. 237 or who applies for leave under that section to apply to the court for an order authorising them, or another person on their behalf, to inspect books of the company. The court is able to make such an order only if it is satisfied (a) that the applicant is acting in good faith, and (b) that the inspection of those books is to be made for a purpose connected with the application for leave under s. 237, or for a purpose connected with bringing or intervening in proceedings pursuant to leave granted under that section.

The onus is on the plaintiff to demonstrate that they are acting in good faith and that the inspection is for a proper purpose and it is at the Court's ultimate discretion whether to order inspection.

(ii) Application for inspection

Subsequent to the inspection of documents sought under this application, the Plaintiffs intend to bring an application to challenge the 2003 transaction and 2009 transaction and ultimately have the shareholding in Sirrah of Harris Health Care cancelled in order to properly administer their mother's estate. As such, the Plaintiffs seek access to company information in order to "understand the historical commercial operations, business and current status of Sirrah's activities". The Plaintiffs also allege a breach of fiduciary duty by the persons responsible for the approval of the transactions.

In this application, the Plaintiffs identified five areas of concern including:

- that Harris Health Care gave nominal consideration for the 2003 transaction;
- that the 2003 transaction was not authorised by Sirrah's articles of association and therefore invalid and ineffectual because Mr William Harris did not satisfy a shareholding qualification to be director of Sirrah and could not vote as a director on the transactions;
- that the 2003 transaction was not done for a proper and beneficial purpose to raise capital or funding for Sirrah and that there appeared to be no consideration for the shares other than a nominal amount of $0.01 per share;
- that the transfer of 50 shares in Sirrah from Ms Aileen Harris to Harris Health Care was for nominal consideration in 2009, not for a proper purpose and not done in circumstances where Ms Aileen Harris was in a position to make proper decisions; and
- in relation to the sale of the nursing home business.

There were also a number of related party loans between Sirrah and Harris Health Care, as well as management contracts between those parties, in relation to which the Plaintiffs seek to uncover information. The Plaintiffs submitted that the application is one of good faith and for a proper purpose and that their suspicions about a breach of duty are reasonable.

(c) Decision

(i) Whether the application was in good faith and for a proper purpose

In his decision, Black J explained that the requirements for "good faith" and "proper purpose" are not confined by reference to a particular cause of action or legal wrongdoing and he gave a number of examples where inspection of books may be required including investigating financial irregularities or a suspected breach of duty where the Plaintiff can reasonably take the view that its investment in the company is at risk.

Black J found that the Plaintiffs' first three concerns in relation to the 2003 transaction were arguable on technical grounds, but he did not find it appropriate that he determine the underlying merits of the challenge.

Black J did not accept the fourth basis for the Plaintiffs' claim as there was no evidentiary basis to suggest Ms Aileen Harris lacked capacity to decide whether to undertake the 2009 transaction. However, the court mentioned that little turns upon this decision because the documents sought were also relevant to the 2003 transaction claims. His Honour rejected the Defendant's claim that the 2009 transfer did not relate to the affairs of the company as he considered the transfer of a company's shares to be a matter that relates to the company.

In relation to the Plaintiffs' fifth concern, Black J rejected the Defendant's submission that the Plaintiffs' desire to obtain information about the company's past and current business is not a sufficient reason to justify an order for inspection. His Honour made this finding with the consideration that the Plaintiffs were a substantial shareholder in a proprietary company and because there were issues in respect of substantial related party transactions.

It was decided that the majority of the application for inspection was in good faith and for a proper purpose and, as such, orders for inspection of a number of documents were granted.

(ii) Categories of documents for which inspection orders were granted

Black J ordered inspection to be granted for a number of categories including:

- records setting out employees receiving employee entitlements;
- details of reimbursements of entitlements to employees of Sirrah to Harris Health Care in FY 2014;
- up to date management accounts of Sirrah; and
- details of all contracts and related party transactions between Sirrah and Harris Health Care, William Harris, Matthew Harris and Maryanne Harris.

His Honour's reasoning for disclosure of the documents in most cases was that the documents were relevant to produce information about the related party transactions, and understand Sirrah's business affairs and the basic corporate governance of the company.

A number of applications were rejected by the Court where the category was either too wide or where the category of document was unclear. For example, the record of all dividends or drawings from Sirrah was said to be "both uncertain and potentially so wide to be oppressive". Additionally, the category of employment contracts relating to "these transactions" was seen to be unclear.

In summary, the Plaintiffs were successful in obtaining orders for inspection of a narrower range of documents than originally sought for the reasons set out above.

6.8 Receiver with an equitable lien over the shares has no standing to apply for a winding up order

(Sophie Qu, MinterEllison)

Lean v Banning Holdings Pty Ltd [2017] WASC 353, Supreme Court of Western Australia, Smith AJ, 20 November 2017

(a) Summary

This case concerned an application for a winding up order pursuant to s. 461(1) of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act). The key issue was whether or not the plaintiff, as a court-appointed receiver, was entitled to bring the application as a "contributory" of the company within the meaning of s. 9 of the Corporations Act. After construing the Corporations Act as a whole and clarifying the meaning of "contributory", Smith AJ dismissed the proceeding on the basis that the plaintiff did not have standing by merely holding a proprietary equitable lien over the shares in respect of his remuneration and expenses.

(b) Facts

On 21 November 2008, the plaintiff Mr Lean was appointed receiver of Professional Services of Australia Pty Ltd (PSA) for a limited purpose of appropriating and realising property to satisfy a judgment debt owed to Computer Accounting and Tax Pty Ltd (CAT). The judgment debt was owed by PSA together with the second debtor Mr Banning and the only property of substantial value at the time of judgment was one share in the defendant company Banning Holdings Pty Ltd (BH) held by Mr Banning. However, Mr Banning died shortly after the delivery of the judgment and the share in BH was transferred to Mr Lean by the executor of the estate of Mr Banning.

Subsequently, Mr Lean entered into a contract of sale between Mr Lean and the directors and shareholders of CAT to sell the BH share. The transfer did not occur as the directors of BH refused to register the executed transfer and the directors and shareholders of CAT commenced proceedings for the enforcement of the share transfer. Before proceeding to trial, in October 2009, the judgment debt owed to CAT was deemed to have been paid as a result of a Court of Appeal decision reducing damages on a claim of statutory compensation by $680,000 and due to the fact that substantial components of the debt had already been paid at that time. Mr Lean was discharged as receiver on 10 November 2010 and a consequential order was made in favour of him to preserve a lien over the BH share for his costs and remuneration.

On 2 December 2010, the proceedings instituted by the directors and shareholders of CAT to enforce the sale of the share was granted a permanent stay. As a result, Mr Lean's lien over the share he holds can only be realised upon a winding up of BH. It is against this background that Mr Lean brought the application to wind up BH.

(c) Decision

Section 462 of the Corporations Act sets out a list of persons and bodies entitled to bring applications under s. 461(1), which includes the company, a creditor of the company, a contributory, the liquidator of the company, ASIC or APRA. The issue for the court to consider in the current case was whether or not Mr Lean was a contributory of BH.

Under s. 9 of the Corporations Act, a contributory of a company is defined to mean a person liable as a member or past member to contribute to the property of the company if it is wound up and a holder of fully paid shares in the company. Relying on the decision in *Yara Australia Pty Ltd v Oswal [No 2]* [2013] WASCA 187 (Yara), Mr Lean's counsel argued that the holder of a share is the person or entity entered on the register of members. The fact that the legal owner of the share is acting in another capacity, for example as a trustee, should not affect its holder status. Further, it was submitted that Mr Lean's equitable lien over the BH share would entitle him to the distribution of any surplus assets that would be paid to subscribers of which he was one. Accordingly, as a registered owner of the share in BH, Mr Lean was a contributory of BH for the purpose of s. 9 and had standing to bring the wind up application.

These arguments were rejected by Smith AJ on the basis that the principles in Yara were discussed in the context of a trust. It did not apply to Mr Lean's circumstances as he was not holding the share as a trustee and he held the share as property in the possession of the court prior to being discharged as a court-appointed receiver. Smith AJ emphasised the importance of construing the meaning of words in the context of the language in the legislation as a whole. After reading the definition of "contributory" in conjunction with other provisions in the Corporations Act that relate to contributors on the winding up of a company (such as s. 478, s. 480, s. 515 and s. 516), it was considered to be clear that, apart from being entitled to any surplus upon distribution, a contributory must also be liable to contribute to the property of the company on winding up. Relevantly:

- s. 515 provides that a member or past member is liable to contribute to the company's property to an amount sufficient to pay the company's debts and liabilities and the costs, charges and expenses of the winding up and to adjust the rights of the contributories among themselves; and
- s. 516 provides that a member need not contribute more than the amount (if any) unpaid on the shares in respect of which the member is liable as a present or past member.

For these reasons, Smith AJ noted that Mr Lean could not be called into account to contribute the amount paid on the share he holds by having only an equitable lien over the share and therefore, he was not liable to contribute to the property of BH. The application for an order to wind up BH was ultimately rejected for lack of standing.

7. Contributions

If you would like to contribute an article or news item to the Bulletin, please email it to: law-cclsr@unimelb.edu.au.