SAI Global Corporate Law Bulletin No. 247>

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Bulletin No. 247

Legislation Hotline

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Detailed Contents

1. Recent Corporate Law and Corporate Governance Developments

1.1 UK consultation paper on insolvency and corporate governance

20 March 2018 - The UK Government has released a new consultation paper, Insolvency and Corporate Governance. The consultation paper considers:

Sales of businesses in distress: This section of the consultation paper proposes potential changes to ensure that directors responsible for the sale of an insolvent subsidiary of a corporate group take proper account of the interests of the subsidiary's stakeholders. This proposal seeks to deter reckless sales, which could potentially harm stakeholder interests, in those limited circumstances. Where a large company or business cannot support itself then the directors involved in any sale, including directors of a holding company controlling the sale of shares in a subsidiary, should satisfy themselves that the sale would lead to a better outcome for creditors than putting the company into formal insolvency.

Reversal of value extraction schemes: This section of the paper proposes changes where a company in financial difficulties has been "rescued" by investors who then strip it of its assets to lessen their loss, or protect their profits, and the company eventually become insolvent. These arrangements are often complicated and designed to avoid existing protections for creditors. Government wants all creditors to be treated fairly in an insolvency situation and is seeking views on potential changes to how certain transactions, or a series of transactions entered into before insolvency can be challenged.

Investigation into the actions of directors of dissolved companies: This section explores proposals to extend existing investigative powers into the conduct of directors to cover directors of dissolved companies. Difficulties are caused when companies are dissolved with outstanding debts or allegations of director misconduct, because the Insolvency Service does not currently have the necessary powers to investigate.

Strengthening corporate governance in pre-insolvency situations: This section explores a number of wider corporate governance issues that can be particularly relevant when companies get into financial difficulties and seeks views on whether further action by Government is needed.

- Group structures - this section considers whether steps should be taken to improve governance, accountability and internal controls within complex company group structures;

- Shareholder responsibilities - this section seeks views on whether there may be further opportunities, such as through the Financial Reporting Council's review of the Stewardship Code, to strengthen the role of shareholders in stewarding the companies in which they have investments;
- Payment of dividends - this section seeks views on whether the legal and technical framework within which dividend decisions are made could be improved and made more transparent whilst ensuring that dividend payments should remain for directors to decide, having regard to their legal obligations and guidance;
- Directors' duties and the role of professional advisers - this section asks if directors are commissioning and using professional advice with a proper awareness of their duties as directors and the requirement to apply an independent mind; and
- Protection for company supply chains in the event of insolvency - this section explores whether supply chain and other creditors should be better protected and, if so, how this could be achieved while preserving the primacy of the interests of shareholders.

1.2 Report on global tech IPOs

14 March 2018 - 2017 saw 100 technology IPOs globally, raising US$25.1 billion in total proceeds, according to PwC's Global Technology IPO Review. The totals mark an 85% increase in total IPOs and a 168% jump in proceeds. On a smaller scale, the final three months of 2017 proved to be one of the best quarters in recent memory, totalling 33 global technology IPOs that raised proceeds of $7.9 billion. Five listings during the quarter came from unicorns.

The Asian market continued to dominate, contributing 65% of the total listings for the year. China single-handedly outpaced the United States in total listings for the year (51 versus 24), although China's US$7 billion in total proceeds trailed the US total of US$8.1 billion. US tech IPO listings increased 50% year on year, while total proceeds improved 351% for the year.

Twenty major exchanges were home to global technology IPOs in 2017. Asian exchanges outnumbered the others in terms of listings with 60 IPOs. US exchanges led the way for proceeds, totalling US$10.6 billion during the year. The New York Stock Exchange raised the most, US$8.8 billion, from 15 IPOs, while the Shenzhen Stock Exchange had the highest number of listings, with 26 IPOs. The South Korean stock exchanges had the second position in terms of proceeds, raising US$2.7 billion with just six listings, followed by the Shenzhen Stock Exchange with US$2.4 billion in proceeds. Meanwhile, the Stock Exchange of Hong Kong had its best year in terms of proceeds, raising US$2.1 billion during 2017. Cross-border IPO activity slowed in 2017 as more companies chose to list in their home countries. In 2017, cross-border listings accounted for just 12% of total global tech IPOs.

1.3 Report on codes of conduct, whistleblowing and corporate culture

14 March 2018 - The Australian Council of Superannuation Investors (ACSI) has issued a critical assessment of codes of conduct and whistleblowing systems at many of Australia's largest listed companies. The paper, Codes of Conduct, Whistleblowing and Corporate Culture: An Analysis of ASX200 Companies, which is based on research commissioned by ACSI and led by the Centre for Workplace Leadership at the University of Melbourne, shows that ASX200 companies are failing to address key risk

topics in their codes of conduct. The report also found that many whistleblowing systems lack critical features and do not adequately support or protect users.

The research compares codes of conduct and whistleblowing systems of ASX200 companies against a set of leading practice indicators and identifies key gaps in their coverage and content:

- Coverage of key topics in codes of conduct is weak - 67% failed to cover five of the 13 recommended topics in their code of conduct. The omissions include several well-known business risks, including: fair dealing/product responsibility, data protection and cybercrime, anti-money laundering and counter-terrorism finance. Overall, ASX50 companies had better coverage than the ASX51-200, but there were still significant gaps among their coverage;
- Codes of conduct are not being regularly reviewed - Guidance issued by the New York Stock Exchange (NYSE) recommends that codes of conduct be reviewed after significant corporate compositional changes or two years. The report found that 116 ASX200 codes of conduct (58%) had not been reviewed in last two years or were undated. Fifteen codes of conduct (8%) five years or older;
- "Tone from the top" and usability needs to be improved - Endorsing a code of conduct (via an introduction) is a signal of support by the Chief Executive Officer (CEO) and an essential element in setting the tone from the top. Only 56 ASX200 codes of conduct (28%) include an introduction by the CEO. A key factor in determining whether a code of conduct will be effective is the ease with which it can be read, interpreted and put in to action. The use of case studies, questions and answers (Q&As) and frequently asked questions (FAQs) contributes to readers' understanding of a code of conduct, yet only 34 ASX200 companies (17%) do this;
- Very few codes of conduct demonstrate leading practice - Across the ASX200, only 11 codes of conduct (6%) demonstrated leading practice, as measured by being two years old or less, using examples, Q&As or case studies and setting a tone from the top by having a CEO introduction; and
- Features are missing from many whistleblowing systems - There are a range of essential features that should be included in a whistleblowing policy and implemented to make a whistleblowing system effective. Many ASX200 companies do not disclose if they offer anonymity (91 companies or 45%), 24-hour availability (97 companies or 48%) or a commitment that retaliation is not acceptable (71 companies or 36%). Whistleblowing is the initial source of detection for 39% of frauds and the code of conduct is the document most widely distributed to employees. Yet 38 ASX200 codes of conduct (19%) had no reference to whistleblowing.

1.4 IOSCO report on growing vulnerability of older investors to financial fraud, unsuitable investments and other risks

12 March 2018 - The Board of the International Organization of Securities Commissions (IOSCO) has published a report that examines the growing vulnerability of older investors to financial fraud and other risks, and identifies sound practices for enhancing their protection.

The report, Senior Investor Vulnerability, reveals that seniors are at a higher risk than other investors of losing money to fraud or of being misled by others. It also indicates that the biggest risks to senior investors are unsuitable investments, financial fraud and their diminished cognitive capability which affects their financial decision-making. Complex products, deficient financial literacy, and social isolation pose additional risks to senior investors.

The report explores the views and experiences of IOSCO members regarding senior investor vulnerability. It provides a list and description of sound practices for both regulators and financial services providers and includes a non-exhaustive bibliography of literature that may be helpful to regulators and others.

1.5 Central bank digital currencies could impact payments, monetary policy and financial stability

12 March 2018 - According to a Central bank digital currencies report by the Bank for International Settlements' Committee on Payments and Market Infrastructures and the Markets Committee, central banks must carefully weigh the implications for financial stability and monetary policy of issuing digital currencies to the general public - although the underlying technologies might hold more promise for wholesale payments, clearing and settlements.

The joint report looks at two types of central bank digital currency (CBDC): a wholesale currency limited to select financial institutions, and a general purpose currency accessible to the public. The report analyses the implications of both types in three core central banking areas: payments, monetary policy implementation and financial stability.

The report finds that wholesale CBDCs might be useful for payments but more work is needed to assess the full potential. Although a CBDC would not alter the basic mechanics of monetary policy implementation, its transmission could be affected. A general purpose CBDC could have wide-ranging implications for banks and the financial system. Commercial banks' reliance on customer deposits may become less stable, as deposits could more easily take flight to the central bank in times of stress. Besides consequences for financial stability, effects on the efficiency of financial intermediation need to be carefully considered.

1.6 European Commission promotion of the Capital Markets Union including reducing barriers to cross-border investments

12 March 2018 - The European Commission is taking a major step towards the development of a Capital Markets Union (CMU) by promoting alternative sources of financing and removing barriers to cross-border investments. The European Commission's latest proposals aim to boost the cross-border market for investment funds, promote the EU market for covered bonds as a source of long-term finance and ensure greater certainty for investors in the context of cross-border transactions of securities and claims.

The Commission is proposing common rules, through a Directive and a Regulation, for common bonds.

The proposed Directive:

- provides a common definition of covered bonds, which will represent a consistent reference for prudential regulation purposes;
- defines the structural features of the instrument (dual recourse, quality of the assets backing the covered bond, liquidity and transparency requirements, etc.);
- defines the tasks and responsibilities for the supervision of covered bonds; and
- sets out the rules allowing the use of the "European Covered Bonds" label.

The Regulation amends the Capital Requirements Regulation (CRR) with the aim of strengthening the conditions for granting preferential capital treatment by adding further requirements. The proposal will reduce borrowing costs for the economy at large. The Commission estimates that the potential overall annual savings for EU borrowers would be between €1.5 billion and €1.9 billion.

The European Commission's proposals also aim to remove regulatory barriers that currently hinder the cross-border distribution of investment funds, to make cross-border distribution simpler, quicker and cheaper. Increased competition will give investors more choice and better value, while safeguarding a high level of investor protection.

Additionally, the Commission has adopted a Communication to clarify which country's law applies when determining who owns a security in a cross-border transaction. Enhanced legal certainty will promote cross-border investment, access to cheaper credit and market integration.

1.7 UK FCA publishes discussion paper on transforming culture in financial services

12 March 2018 - The UK Financial Conduct Authority (FCA) has published a discussion paper, Transforming Culture in Financial Services, which presents views from academics and industry thought leaders. The paper is intended to provide a basis for stimulating further debate on transforming culture in the sector. The paper is a set of essays that discuss what a good culture might look like, the role of regulation and regulators, how firms might go beyond incentives, and how to change behaviour for the better.

1.8 Female board appointments to ASX200 companies

8 March 2018 - The percentage of female appointments to ASX 200 boards has spiked in 2018, according to a new report released by the Australian Institute of Company Directors (AICD). Women accounted for 47% of ASX 200 board appointments in the first two months of 2018, up from 36% in 2017.

The AICD's Quarterly Gender Diversity Report, which tracks progress towards the Institute's target of achieving 30% female representation across ASX 200 boards by the end of 2018, also reveals that women now account for 26.7% of ASX 200 directorships. The report shows that the number of ASX 200 companies which have no women around the board table now stands at only five, down from 14 last year. Across the ASX 200, a total of 74 companies have reached or exceeded the 30% target

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1.9 European Commission plan to promote FinTech

8 March 2018 - The European Commission has unveiled an Action Plan on how to harness the opportunities presented by technology-enabled innovation in financial services (FinTech).

As a first step, the Commission is putting forward new rules that will help crowdfunding platforms to grow across the EU's single market. The Action Plan envisages enabling the financial sector to make use of the rapid advances in new technologies, such as blockchain, artificial intelligence and cloud services.

In addition, the Commission is proposing a pan-European label for platforms, so that a platform licensed in one country can operate across the EU.

The Action Plan sets out 19 steps, including the following:

- the Commission will host an EU FinTech Laboratory where European and national authorities will engage with tech providers in a neutral, non-commercial space;
- the Commission has already created an EU Blockchain Observatory and Forum. It will report on the challenges and opportunities of crypto assets later in 2018 and is working on a comprehensive strategy on distributed ledger technology and blockchain addressing all sectors of the economy. A distributed ledger is an information database that is shared across a network. The best-known type of distributed ledger is blockchain;
- the Commission will consult on how best to promote the digitisation of information published by listed companies in Europe, including by using innovative technologies to interconnect national databases. This will give investors far easier access to key information to inform their investment decisions;
- the Commission will run workshops to improve information-sharing when it comes to cybersecurity; and
- the Commission will present a blueprint with best practices on regulatory sandboxes, based on guidance from European Supervisory Authorities. A regulatory sandbox is a framework set up by regulators that allows FinTech startups and other innovators to conduct live experiments in a controlled environment, under a regulator's supervision. Regulatory sandboxes are gaining popularity, mostly in developed financial markets.

1.10 IFIAR releases report on sixth annual survey of audit inspection findings

8 March 2018 - The International Forum of Independent Audit Regulators (IFIAR) has released a report on the results of its sixth annual survey of inspection findings arising from its member regulators' individual inspections of audit firms affiliated with the six largest global audit firm networks. IFIAR collected information about two categories of activities: inspections performed on firm-wide systems of quality control and inspections of individual audit engagements. Forty-two IFIAR members contributed to the 2017 survey.

IFIAR members reported in the 2017 survey that 40% of audit engagements inspected had at least one finding, compared to 42% in the 2016 survey and to 47% in the first survey capturing this percentage (2014 survey).

High rates of findings indicate need for improvement. To that end, IFIAR's Global Audit Quality Working Group (GAQ WG) set a goal in 2015 for the six largest network firms to reduce the number of deficient audits (those with at least one finding) reported in aggregate by members of this Working Group in IFIAR's annual survey by at least 25% - to 29% or less - by 2019.

1.11 IOSCO consults on recommendations to help trading venues manage extreme volatility

7 March 2018 - The International Organization of Securities Commissions (IOSCO) has published a consultation report, Mechanisms Used by Trading Venues to Manage Extreme Volatility and Preserve

Orderly Trading, which explores the measures that trading venues use to address the risks posed by extreme volatility.

Extreme volatility in securities markets can undermine IOSCO's objective of ensuring that markets are fair, efficient and transparent, weaken market integrity and reduce investor confidence. Following recent extreme volatility events, regulatory authorities and trading venues have been reviewing their approaches to managing extreme volatility. Volatility control mechanisms seek to minimize market disruption triggered by events such as erroneous orders, by halting or temporarily constraining trading.

In the report, IOSCO proposes eight recommendations to assist trading venues and regulatory authorities when considering the implementation, operation, and monitoring of volatility control mechanisms.

Specifically, the report recommends that:

- trading venues should have mechanisms to manage extreme volatility and these mechanisms should be appropriately calibrated and monitored;
- regulatory authorities should consider what information they require to effectively monitor the overall volatility control mechanism framework in their jurisdiction, and ensure that trading venues maintain relevant records;
- information about volatility control mechanisms and when they are triggered should be made available to regulatory authorities, market participants and, if appropriate, the public; and
- communication amongst trading venues should be considered where the same or related securities are traded on multiple trading venues in a particular jurisdiction. In addition, where the same or related instruments are traded in different jurisdictions and the mechanism is triggered, communication may be appropriate.

The report also highlights the issues that arise where this information sharing and communication between trading venues occurs across jurisdictions.

1.12 APRA to introduce first prudential standard aimed at addressing growing threat of cyber attacks

7 March 2018 - The Australian Prudential Regulation Authority (APRA) has responded to the growing threat of cyber attacks by proposing its first prudential standard on information security. APRA has released a package of measures, titled "Information Security Management: A new cross-industry prudential standard, for industry consultation". The package is aimed at shoring up the ability of APRA-regulated entities to repel cyber adversaries, or respond swiftly and effectively in the event of a breach.

The proposed new standard, *CPS 234 Information Security*, would require regulated entities to:

- clearly define the information security-related roles and responsibilities of the board, senior management, governing bodies and individuals;
- maintain information security capability commensurate with the size and extent of threats to information assets, and which enables the continued sound operation of the entity;
- implement information security controls to protect its information assets, and undertake systematic testing and assurance regarding the effectiveness of those controls;
- have robust mechanisms in place to detect and respond to information security incidents in a timely manner; and
- notify APRA of material information security incidents.

Key areas where APRA is hoping to lift standards include assurance over the cyber capabilities of third parties such as service providers, and enhancing entities' ability to respond to and recover from cyber incidents.

The consultation package is available on APRA's website.

1.13 FSB publishes Global Shadow Banking Monitoring Report 2017

5 March 2018 - The Financial Stability Board (FSB) has published the Global Shadow Banking Monitoring Report 2017. The Report presents the results of the FSB's seventh annual monitoring exercise to assess global trends and risks from shadow banking activities. The 2017 monitoring exercise covers data up to end-2016 from 29 jurisdictions, which together represent over 80% of global GDP, including, for the first time, Luxembourg. Also for the first time, the Report assesses the involvement of non-bank financial entities in China in credit intermediation that may pose financial stability risks from shadow banking, such as maturity/liquidity mismatches and leverage.

The global monitoring of developments in the shadow banking system is part of the FSB's strategy to transform shadow banking into resilient market-based finance. The monitoring exercise adopts an activity-based approach, focusing on those parts of the non-bank financial sector that perform economic functions which may give rise to financial stability risks from shadow banking.

The main findings from the 2017 monitoring exercise include that:

- the activity-based, narrow measure of shadow banking grew by 7.6% in 2016 to $45.2 trillion for the 29 jurisdictions. This represents 13% of total financial system assets of these jurisdictions. China contributed $7 trillion to the narrow measure (15.5%), and Luxembourg $3.2 trillion (7.2%);
- collective investment vehicles with features that make them susceptible to runs (eg. open-ended fixed income funds, credit hedge funds and money market funds), which represent 72% of the narrow measure, grew by 11% in 2016. The considerable trend growth of these collective investment vehicles - 13% on average over the past five years - has been accompanied by a relatively high degree of investment in credit products and some liquidity and maturity transformation. This highlights the importance of implementing the FSB policy recommendations on structural vulnerabilities from asset management activities published in January 2017;
- the assets of market intermediaries that depend on short-term funding or secured funding of client assets (eg broker-dealers) declined by 3%. These intermediaries accounted for 8% of the narrow measure by end-2016. Reflecting their business models, broker-dealers in some jurisdictions employ significant leverage, although it is lower than the levels prior to the 2007-09 global financial crisis;
- the assets of non-bank financial entities engaged in loan provision that is dependent on short-term funding, such as finance companies, shrank by almost 4% in 2016, to 6% of the narrow measure. In some jurisdictions, finance companies tend to have relatively high leverage and maturity transformation, which increases their susceptibility to roll-over risk during period of market stress; and
- in 2016, the wider "Other Financial Intermediaries" (OFIs) aggregate, which includes all financial institutions that are not central banks, banks, insurance corporations, pension funds, public financial institutions or financial auxiliaries, grew by 8% to US$99 trillion in 21 jurisdictions and the euro area, faster than banks, insurance corporations and pension funds. OFI assets now represent 30% of total financial assets, the highest level since at least 2002.

1.14 Survey of Australian directors on issues affecting trust in their companies

27 February 2018 - The Australian Institute of Company Directors and KPMG have published a report on the results of a survey of almost 600 company directors on issues affecting trust in their companies. Survey respondents represent companies across all sectors with 40.7% coming from private business, 30.8% NFPs, 14% public sector, and 11.2% from listed companies.

The report, Maintaining the Social Licence to Operate: 2018 KPMG-AICD Trust Survey, shows that directors are acutely aware of the need for their companies to maintain trust with stakeholders amid generally declining trust in all institutions. As the "crisis of trust" in institutions continues to dominate global and national headlines, encouraging conversations are being held in Australian boardrooms where trust remains front of mind. Directors overwhelmingly agree that trust is important to their company's sustainability, and boards are increasingly looking to better understand, and respond to, the issues that are affecting their company's trustworthiness.

Specifically, the survey found that:

- almost half of directors reported that their board had to deal with issues that can affect trust in their company over the past year;
- Boards see "clients or customers" and "employees" as the two most critical stakeholders to maintain trust in a company;
- less than half of company directors who responded felt that their board has a proactive approach to building trust with the company's most important stakeholders;
- although company directors feel a greater sense of responsibility to the wider communities they serve, "internal culture and practices" was voted by directors as the most critical issue relating to trust; and
- the factors contributing to trust are more dynamic and interrelated than ever before. There are simply too many issues to address them all with the same level of focus; boards must prioritise and focus on those that are most likely to impact their company and its stakeholders. The results, however, suggest a mixed picture in the extent to which companies have formal processes for escalating trust issues to the board level.

1.15 Financial stability and international regulatory reform

23 February 2018 - The Bank of England has published a working paper on the international regulatory reforms introduced to achieve financial stability following the global financial crisis. In Rethinking Financial Stability, the authors provide an overview of the state of progress of these reforms, and assess whether they have achieved their objectives and where gaps remain. They find that additional insights gained since the start of the reforms paint an ambiguous picture on whether the current level of bank capital should be higher or lower. Additionally, the authors present new evidence that a combination of different regulatory metrics can achieve better outcomes in terms of financial stability than reliance on individual constraints in isolation. They discuss in depth several recurring themes of the regulatory framework, such as the appropriate degree of discretion versus rules, the setting of macroprudential objectives, and the choice of policy instruments. The authors conclude with suggestions for future research and policy, including on models of financial stability, market-based finance, the political

economy of financial regulation, and the contribution of the financial system to the economy and to society.

1.16 New Banking Royal Commission background papers published

The Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry has published two new background papers:

- Some Features of Car Financing in Australia: Background Paper 3; and
- Everyday Consumer Credit - Overview of Australian Law Regulating Consumer Home Loans, Credit Cards and Car Loans: Background Paper 4.

The Commission has also published a paper prepared by Treasury at the request of the Commission titled Reforms to Consumer Lending that provides an overview of the main reforms to consumer lending since 2007.

1.17 Justice Nettle speech on duties of company directors published

Justice Geoffrey Nettle of the High Court of Australia presented the 2017 Harold Ford Memorial Lecture at Melbourne Law School on the topic "The changing position and duties of company directors". The lecture has been published by the Melbourne University Law Review and is available here.

This is a summary of the lecture:

"In 1974, in the first edition of his Principles of Company Law, Professor Ford was able to say that directors' duties were "not very demanding". This lecture traces how the duties and standards of care demanded of company directors have increased since then. In doing so, it makes reference to the attenuated business judgment rule, comparing the positions in the United Kingdom and, briefly, South Africa. It then considers similarities and differences between the duties imposed on company directors, union officers and public officials. It suggests that, while the regulatory regimes that apply to company directors and union officers are strikingly different, there is little reason in principle why that should be so. For practical reasons, the same cannot be said of the differences between public officials and company directors or union officers. But it remains somewhat paradoxical that, although the actions of public officials may have far more broad-ranging effects on the nation's wellbeing than the actions of any company director or union officer, public officials' duties are much less onerous."

2. Recent ASIC Developments

2.1 New Deputy Chairperson role at ASIC

19 March 2018 - The Australian Government has announced that it intends to create a new Deputy Chairperson role at the Australian Securities and Investments Commission (ASIC). This means there will be two positions of Deputy Chairperson. The Government also announced the reappointment of two Commissioners - Peter Kell for a further one-year period from 6 May 2018 up to and including 5 May

2019 and John Price for a further two-year period from 21 March 2018 up to and including 20 March 2020.

2.2 Report on changes to small business loan contracts by big four banks

15 March 2018 - The Australian Securities and Investments Commission (ASIC) has released a report setting out the details of the changes made by the big four banks to remove unfair terms from their small business loan contracts of up to $1 million.

The report, Unfair contract terms and small business loans (REP 565), provides more detailed guidance to bank and non-bank lenders about compliance with the unfair contract terms laws as they relate to small business.

The report follows the announcement in August 2017 that the big four banks had committed to improving terms of their small business loans following work with ASIC and the Australian Small Business and Family Enterprise Ombudsman (ASBFEO).

The report:

- identifies the types of terms in loan contracts that raise concerns under the law;
- provides details about the specific changes that have been made by the banks to ensure compliance with the law; and
- provides general guidance to lenders with small business borrowers to help them assess whether loan contracts meet the requirements under the unfair contract terms law.

2.3 Market integrity report

15 March 2018 - ASIC has released its latest report on market integrity for the period 1 July to 31 December 2017, Market integrity report: July to December 2017 (REP 569).

Key outcomes during the six-month period include:

- one person jailed;
- four enforceable undertakings;
- $40.8 million in community benefit payments;
- ten infringement notices issued; and
- four people disqualified from providing financial services.

The report examines ASIC's focus on cyber resilience, client money and sell-side research. It also examines some of ASIC's key activities over the last six months in areas such as financial benchmarks, continuous disclosure and binary options.

2.4 Extension of the transition period for superannuation and retirement calculators

13 March 2018 - ASIC has extended to 1 July 2019 the time that providers of retirement and superannuation calculators have to comply with the requirement that generic financial calculators must account for inflation.

If a generic financial calculator makes an estimate of a future return or payment, it must adjust for inflation using an assumed rate of inflation of 2.5% (being the mid-point of the Reserve Bank of Australia's target range for inflation over the cycle). As a result of the extension, this requirement will not apply to retirement and superannuation calculators until 1 July 2019.

ASIC has postponed the commencement of this requirement for superannuation and retirement calculators because there are superannuation reforms that may impact on how superannuation calculators should present and calculate estimates in the future. These reforms have been deferred until 1 July 2019. During this period, ASIC will further review the suitability of the prescribed discount rate for calculators that produce retirement estimates, taking into account the interests and further views of consumers, superannuation and retirement calculator providers, and actuaries.

ASIC will monitor the impact of these reforms to assess the ongoing appropriateness of the requirement to account for inflation.

This extension does not affect other provisions of ASIC's relief for calculators.

2.5 Further extension of exemption for simple credit hardship arrangements

13 March 2018 - ASIC has issued Credit (Amendment) Instrument 2018/114, which amends Class Order 14/41 as it applies to providers of consumer credit and consumer leases.

The newly made instrument extends the exemptions granted under transitional regulations (set out in ss. 69A and 69B of the National Consumer Credit Protection Regulations 2010 No. 44 (Cth)) that relieve credit providers and lessors from the obligation to provide a written response to a hardship notice in certain circumstances.

For industry and consumers, this extends the arrangements for credit hardship that are currently in place. It allows flexibility for both sides in dealing with a simple hardship arrangement.

The exemption was due to expire on 1 March 2018 and now extends until 1 March 2020. This will allow ASIC time to continue to consult with industry and affected stakeholders in relation to the hardship process and the interaction with credit reporting requirements.

2.6 National financial literacy strategy annual highlights report

8 March 2018 - ASIC has released the National Financial Literacy Strategy Annual Highlights Report 2016-17.

The Report paints a national picture of financial literacy programs and initiatives delivered by a wide range of organisations across the government, education, industry and community sectors in support of the National Financial Literacy Strategy, led and coordinated by ASIC. The scale of work continues to grow with over 70 organisations supporting or contributing to initiatives aligned with the National Strategy.

2.7 Remake of "sunsetting" class order about share and interest sale facilities

6 March 2018 - ASIC has remade Class Order [CO 08/10] *Share and interest sale facilities*, which was due to expire on 1 April 2018.

The new instrument, ASIC Corporations (Share and Interest Sale Facilities) Instrument 2018/99, continues to provide issuers of shares and interests who operate certain share and interest sale facilities and related purchase facilities relief from the managed investment, licensing, disclosure and unsolicited offers provisions of the Corporations Act.

ASIC has extended the relief to include a related body corporate of the product issuer that operates a share or purchase facility.

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

The relief was remade following public consultation in Consultation Paper 252 Remaking ASIC class order on share and interest sale facilities: [CO 08/10] (CP 252). ASIC did not receive any submissions in response to this consultation paper.

2.8 Consultation on updated guidance for oversight of the Australian Financial Complaints Authority

5 March 2018 - ASIC has released a draft updated version of Regulatory Guide 139, Oversight of the Australian Financial Complaints Authority (updated RG139) for public consultation.

The Bill to establish Australian Financial Complaints Authority (AFCA) passed on 14 February 2018, and Financial Services Minister Kelly O'Dwyer has announced that AFCA will commence operations no later than 1 November 2018.

There are a number of transitional steps that need to take place before AFCA commences, including that:

- the Minister will authorise AFCA; and
- the AFCA Board will consult on the scheme's terms of reference.

ASIC will finalise this guidance to coincide with AFCA commencement - that is, no later than 1 November 2018.

ASIC states in its announcement that there has already been extensive public consultation on these reforms through the progress of the Review of the financial system external dispute resolution and complaints framework led by Professor Ian Ramsay, as well as the release of a Treasury consultation paper on the establishment of AFCA in November 2017.

ASIC is consulting for a period of five weeks on a limited number of policy issues. This includes whether firms need any transitional relief from external dispute resolution disclosure obligations.

The consultation paper is available on the ASIC website.

2.9 Enforcement report

28 February 2018 - ASIC has released its enforcement outcomes report for the period 1 July 2017 to 31 December 2017: ASIC enforcement outcomes: July to December 2017 (REP 568).

The enforcement outcomes over that six-month period include:

- 63 investigations commenced and 61 investigations completed;
- 54 people or companies removed or restricted from providing financial services or credit, and 28 people disqualified or removed from directing companies;
- 34 infringement notices issued, $21.5 million in civil penalties, and 12 enforceable undertakings; and
- 17 people charged in criminal proceedings, and 232 people charged in summary prosecutions for strict liability offences.

The report presents a number of key outcomes over the last six months, across the areas that ASIC enforces: corporate governance, financial services, market integrity and small business.

This edition of the report also provides a summary of ASIC's work addressing loan fraud. Since becoming the national consumer credit regulator in 2010, ASIC has undertaken over 100 investigations into loan fraud, and removed or restricted 60 people from providing financial services, of which 36 people were banned permanently.

2.10 Corporate finance regulation report

26 February 2018 - ASIC has published its latest report on the regulation of corporate finance issues for the period July to December 2017.

Report 567 ASIC regulation of corporate finance: July to December 2017 (REP 567) provides statistical data, highlights key focus areas, and includes relevant guidance about ASIC's regulation of:

- fundraising transactions;
- mergers and acquisitions;
- corporate governance issues;
- related party transactions; and

- financial reporting.

It details the approach ASIC takes in these areas, including the types of issues that have caused ASIC to intervene and its response to novel issues seen in transactions during the period. The report also provides an overview of ASIC's current policy initiatives.

The report sets out information on ASIC's ongoing engagement with Independent Experts, and an update on the implementation of the industry funding model for ASIC. It also provides information on the new regime for crowd-sourced funding by public companies and highlights ASIC's regulatory initiatives regarding emerging market issuers and ASIC's reflections on the 2017 AGM Season.

3. Recent ASX Developments

3.1 ASX Listing Rules - Guidance Note Updates

On 9 March 2018, ASX released a number of updates to the ASX Listing Rules Guidance Notes. Some of the key amendments were as follows.

In Guidance Note 1, s. 3.8 was updated with further materials on using artificial means to achieve spread and s. 3.19 was updated in relation to ASX's good fame and character requirements.

Guidance Note 12 was updated to reflect a change in policy for back door listings (effective immediately) requiring all directors or proposed directors to provide evidence of their good fame and character, including existing directors who have been elected by shareholders to the board. This update also contains clarification of the accounts that need to be disclosed in an announcement under Annexure A to that Guidance Note.

Guidance Note 8 was updated:

- to provide additional guidance in s. 4.15 relating to ASX's disclosure expectations for material contracts;
- to remove a reference in s. 4.20 to disclosing the impact of material contracts on revenue, costs or profits; and
- to expand guidance in s. 5.10 to address the new insolvent trading safe harbour for directors in s. 588GA of the Corporations Act 2001 No. 50 (Cth), and what should be disclosed when an entity in financial difficulties requests a voluntary suspension to complete a transaction necessary for its survival.

The Guidance Notes are available on the ASX website.

3.2 Monthly activity report

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

4. Recent Takeovers Panel Developments

4.1 Panel Publishes Consultation Paper: Revisions to Guidance Note 1 on Unacceptable Circumstances

14 March 2018 - The Takeovers Panel has released a Consultation Paper seeking public comment in relation to proposed revisions to Guidance Note 1 on Unacceptable Circumstances.

The proposed revisions give an example of unacceptable circumstances following a last and final statement in relation to a takeover bid (see example 4 of paragraph 32(a) and footnote 39 of Guidance Note 1). The example seeks to provide market participants more certainty by establishing a time frame before which departure from a no increase statement may give rise to unacceptable circumstances.

4.2 Finders Resources Limited - Panel Declines to Conduct Proceedings

13 March 2018 - The Takeovers Panel has declined to conduct proceedings on an application dated 1 March 2018 from Eastern Field Developments Limited in relation to the affairs of Finders Resources Limited.

Finders is currently the subject of an unconditional off-market takeover bid by Eastern Field. The application concerned disclosure in the target's statement (see TP18/17).

The Panel requested and considered further material and relied on the following in reaching its decision:

- Finders submitted that its independent directors believe shareholders could expect from its previous disclosure that Finders' March 2018 quarter copper cathode production would be greater than in the December 2017 quarter (4,100 tonnes) and less than in the June 2017 quarter (6,804 tonnes);
- Finders also submitted that the independent directors maintain their belief that Finders will achieve production at around nameplate capacity of 28,000 tonnes per annum on an annualised basis during the June 2018 quarter and subsequent quarters consistent with their statements in the supplementary target's statement;
- in response to the application (and as requested by Eastern Field), Finders provided updated operational and financial information to the independent expert and technical specialist expert, including actual production levels for January and February 2018;
- the independent expert (as advised by the technical specialist expert) based its review on a more conservative recovery in production following the March 2018 quarter (despite the view of the independent directors noted above);
- having regard to the updated information from Finders and advice from the technical specialist expert, the independent expert confirmed that each change in the key assumptions had an immaterial impact on its valuation analysis (utilising a 10% materiality threshold) and that collectively the changes had a negligible impact on its valuation range and did not alter its opinion that Eastern Field's offer is neither fair nor reasonable; and
- in response to Eastern Field's concerns in relation to working capital, Finders submitted that its independent directors maintain their view regarding Finders' balance sheet position and that no new circumstances have arisen that require additional disclosure at this time.

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

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

5. Recent Research Papers

5.1 Independent Directors in Asia: Theoretical Lessons and Practical Implications

Independent director requirements have spread throughout Asia, generating diverse definitions, enforcement patterns and cadres of directors. Yet the proliferation itself, and some of its features, provide some support for convergence in corporate governance, especially in function rather than form. In particular, seemingly influenced by proposals from Australian reformers in the early 1990s, the definition of independence has departed from US and early UK roots by excluding (variously defined) substantial shareholders, except until recently Singapore. This fits with the historical reality of "lockholders" in Austral-Asian corporate governance, making a key corporate governance concern the tension between large and minority shareholders, rather than the traditional Anglo-American tension between dispersed shareholders and professional managers. Given the looser definition in Singapore, the function of independent directors there has extended to mediating disputes among family blockholders. This may also be found in India, for example, where enforcement has been problematic until recently. The comparative analysis further suggests that significant "legal transplants" are occurring, but with complex features and motivations. Given these patterns, independent directors will probably continue to be the norm in Asian countries, notwithstanding growing academic critiques. It is also likely that the varieties of independent directors found among jurisdictions will not diminish significantly.

Independent Directors in Asia: Theoretical Lessons and Practical Implications

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5.2 Responsibility of Directors of Financial Institutions

This paper examines the governance responsibilities of directors of financial institutions in the United States and worldwide. Part A of the chapter first reviews, as background, the duties generally applicable to directors of firms, including financial institutions. Part B then compares the special responsibilities of directors of financial institutions, including certain responsibilities created in the aftermath of global financial crisis. Finally, Part C enquires more normatively about whether - and if so, how - financial institution governance should be improved to further reduce excessive risk-taking and protect the public against systemic economic harm.o:p>

Responsibility of Directors of Financial Institutions

5.3 Firms and Collective Reputation: The Volkswagen Emission Scandal as a Case Study

This paper uses the 2015 Volkswagen emissions scandal as a natural experiment to provide causal evidence that group reputation externalities matter for firms. The authors' estimates show statistically and economically significant declines in the US sales and stock returns of, as well as public sentiment towards, BMW, Mercedes-Benz, and Smart as a result of the Volkswagen scandal. In particular, the scandal reduced the sales of these non-Volkswagen German manufacturers by approximately 76,000 vehicles over the following year, leading to a loss of approximately US$3.7 billion of revenue. Volkswagen's malfeasance materially harmed the group reputation of "German car engineering" in the United States.

Firms and Collective Reputation: The Volkswagen Emission Scandal as a Case Study

6. Recent Corporate Law Decisions

6.1 Non-solicitor director denied leave to represent company at judicial review application

(Bonnie Johnston, MinterEllison)

Rossi Homes Pty Ltd v Victorian Civil and Administrative Tribunal and Dun and Bradstreet (Australia) Pty Ltd [2018] VSC 95, Supreme Court of Victoria, Derham AsJ, 5 March 2018

(a) Summary

This case concerned an application by a non-solicitor director of a company for leave to represent the company in a judicial review application, pursuant to rl. 1.17(1) of the Supreme Court (General Civil Procedure) Rules 2015 No. 103 (Vic) (the Rules). On the basis of the evidence provided, Derham AsJ considered that the circumstances of the case did not warrant departing from the rule that a company will not be permitted to appear without a legal representative. Factors weighing against the grant of leave included the inherent complexity of a judicial review application, the significant challenges a non-legal representative would face in prosecuting the proceeding and the substantially increased burden that a plaintiff company being legally unrepresented would place on both the court and the defendants.

(b) Facts

Rossi Homes Pty Ltd (the Plaintiff) is a building company. Giuseppe Joe Rossi is the sole shareholder and sole director of the Plaintiff. In late 2016, the Plaintiff had a dispute with one of its suppliers when the Plaintiff failed to pay a number of invoices for work performed by the supplier. In April 2017, the supplier engaged the debt collection services of Dun and Bradstreet (Australia) Pty Ltd (the Second Defendant), to pursue the debt it claimed it was owed by the Plaintiff. The Second Defendant took a number of steps to recover the debt from the Plaintiff, including contacting the Plaintiff regarding payment of the debt and listing the debt as unpaid on a commercial credit report.

The commercial credit report was accessed by third parties, including QBE Insurance (QBE). At that time, QBE was the insurer for the Housing Industry Association Insurance Scheme, who provided home warranty insurance to the Plaintiff. It was alleged by the Plaintiff that this credit report listing ultimately lead to a loss of its mandatory home warranty insurance coverage and, in turn, the suspension of Mr Rossi's registration as a building practitioner (for failure to comply with annual fee and insurance requirements). The Plaintiff also alleged that the credit report was accessed by other suppliers of the Plaintiff which varied their terms of supply to the detriment of the business. Consequently, in June 2017, the Plaintiff brought a claim against the Second Defendant in the Victorian Civil and Administrative Tribunal (VCAT), seeking to recover damages arising from these losses. In November 2017, Member Mahoney found that the Plaintiff was unsuccessful in all claims made against the Second Defendant (see *Rossi Homes Pty Ltd v Dun and Bradstreet (Australia) Pty Ltd (Civil Claims)* [2017] VCAT 1839).

Pursuant to Order 56 of the Rules, the Plaintiff applied for judicial review of VCAT's decision, seeking to quash the decision on a number of grounds, including failure to afford it procedural fairness, allowing the Second Defendant to be legally represented and failing to take into account Mr Rossi's inalienable human right to subsistence. It is against this background that Mr Rossi, as a director of the Plaintiff company, applied to the Supreme Court of Victoria for leave to represent the Plaintiff company in the judicial review application.

(c) Decision

Rule 1.17(1) of the Rules is a restatement of the common law position and provides that a corporation, whether or not a party to proceedings, shall not take any step in a proceeding save by a solicitor. However, rl. 1.17(1) is expressed to be subject to the other provisions of the Rules. This includes rl. 2.04, which enables a court to dispense with compliance with the requirements of the Rules. Consequently, the starting point for the court's consideration of the Plaintiff's application was that a company will not usually be permitted to appear without a legal representative, unless the leave of the court is obtained. The issue for the court was therefore whether to grant leave to Mr Rossi to represent the Plaintiff in a judicial review application.

Extrapolating from the judgment of Forrest J in *Worldwide Enterprises Pty Ltd v Silberman* (2010) 26 VR 595, Derham AsJ commenced his consideration by identifying nine factors relevant to whether the court should exercise its discretion under rl. 2.04 to dispense with the requirement of rl. 1.17(1).

These were:

- the manner in which the case has progressed at the time the application is made;
- the manner in which the case can proceed in the future without a solicitor;
- the complexity of the issues involved in the case;
- whether the lack of disciplinary measures in relation to the person seeking to represent the company will affect the administration of justice;
- whether the case can be conducted in an orderly and responsible fashion without a solicitor;
- any financial considerations which would inhibit a company from obtaining legal representation;
- the stage which the case has reached;
- whether the defendant is likely to expend more funds in defending the claim absent a solicitor acting for the company; and
- what effect, if any, permitting a company to appear without a solicitor will have on court resources and, particularly, the effect upon other litigants.

Taking into account these factors, Derham AsJ rejected the Plaintiff's arguments and considered the decision of *Enviro Pak Pty Ltd v New Horticulture Pty Ltd* [2013] FCA 306 (Enviro Pak) could be distinguished from the circumstances of the current case for the following four reasons.

(i) Financial position of the company

The Plaintiff asserted that it was unable to obtain legal representation due to its limited financial resources. However, unlike in Enviro Pak, the Plaintiff did not provide any substantive evidence:

- establishing that it was in financial difficulty (such as accounting statements);
- of the financial means of Mr Rossi, as the Plaintiff's director, to support the Plaintiff in its claims; and
- of the Plaintiff's efforts to secure pro bono representation.

Even if the court was to accept the Plaintiff's limited evidence that its financial status precluded it from obtaining legal representation, Derham AsJ noted this was only one factor to be balanced against other relevant considerations.

(ii) Conduct of the case to date

Derham AsJ identified that Mr Rossi had demonstrated difficulties in adducing evidence and formulating the Plaintiff's claims in succinct and understandable terms. In addition, Derham AsJ considered that Mr Rossi was not capable of conducting the case in an orderly and responsible fashion due to his continued failure to understand that corporations do not have human rights. Consequently, Mr Rossi had unnecessarily taken up the time of both the court and VCAT with irrelevant legal arguments.

(iii) Future conduct of the claim

Although acknowledging that this was not the correct forum in which to express a considered view of the prospects of the Plaintiff's judicial review application, Derham AsJ found that any potentially arguable ground of review identified in the judicial review application was overwhelmed by irrelevant material. Mr Rossi would therefore face significant difficulties in prosecuting the proceeding himself.

Derham AsJ also considered there was merit in the Second Defendant's point that, in light of the early stage of proceedings:

- the Plaintiff has sufficient time to brief legal representatives; and
- the Second Defendant is likely to incur an additional burden in each of the procedural stages if the Plaintiff were to continue to be legally unrepresented.

(iv) Impact on the court and defendants

In light of Mr Rossi's conduct of the claims to date, Derham AsJ considered that permitting him to continue to represent the Plaintiff posed a real risk to the defendants in having the proceeding dealt with without unnecessary delay and cost. Derham AsJ also noted that the Plaintiff's lack of legal representation was likely to place a greater burden on the court and result in increased costs for the Second Defendant.

For these reasons, Derham AsJ held that the Plaintiff's application for leave to be represented by a non-solicitor director should be refused.

6.2 Treatment of class action members' subordinate claims in voluntary administration

(Sarah Dressler, DLA Piper)

In the matter of SurfStitch Group Limited [2018] NSWSC 164, Supreme Court New South Wales, Brereton J, 22 February 2018

(a) Summary

SurfStitch Group Limited (SurfStitch) was an e-commerce retailer of action sports and youth apparel which operated across multiple jurisdictions through subsidiaries. Prior to the appointment of administrators in August 2017, two shareholder class actions were commenced against SurfStitch relating to alleged misleading and deceptive conduct and breaches of continuous disclosure obligations. Shareholders who could form part of the class actions were subordinate creditors and they were not entitled to vote in the administration without a court order. The administrators of SurfStitch filed an application seeking orders to further extend the convening period for the second meeting of creditors and entitling subordinate claimants to vote at that meeting, in addition to related orders for the admission of those claims for voting purposes. The court made orders that subordinate claimants should be entitled to vote, and that administrators would be justified in rejecting claims not submitted by the time specified in the notice of meeting, but the court did not allow the administrators to value claims of class action group members at a nominal value of $1 for voting at the second creditors' meeting.

(b) Facts

On 11 December 2017, the administrators of SurfStitch sought orders further extending the convening period for the second meeting of creditors under s. 439A of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) and entitling subordinate claimants to vote at that meeting pursuant to s. 600H(1)(b) of the Corporations Act, together with related orders in connection with the giving of notice to certain subordinate claimants as well as the admission for voting purposes of the claims of certain subordinate claimants. Brereton J dealt specifically with the treatment of the subordinate claimants.

Section 600H reduces the requirement for communication with subordinate claimants who are unlikely to have any real stake in the administration. In the present case, the administrators argued it was likely that there will be surplus in the liquidation and, therefore, claimants have a real financial interest in the liquidation and should be entitled to vote at the s. 439A meeting.

By s. 600H(1)(a), subordinate claimants are entitled to receive a copy of any notice, report or statement to creditors only if they ask for a copy. The orders sought to modify the operation of s. 439A(3), s. 439A(4) and s. 439E(7), so the administrators are only required to give notice to shareholders who may be potential group members in the class actions by email or post or fax, and generally by publication in appropriate places.

Pursuant to s. 447A of the Corporations Act, the administrators sought orders to modify the operation of r. 5.6.23 of the Corporations Regulations 2001 No. 193 (Cth) in three ways:

- so that potential subordinate claimants are not entitled to vote unless their claims have been admitted by the administrator, or they have lodged particulars of their claim or a formal proof by the date and time set out in the notice of meeting as the time by which proofs and proxies are to be submitted;
- so that if any resolution is proposed which contemplated a distribution to potential subordinate claimants before all other debts and claims are paid, the Chair is not required to put it to a vote unless and until it has been passed by creditors other than potential subordinate claimants; and
- so that the Chair may admit any group member claimant (including those who have lodged sufficient particulars of their debt or claim or a formal proof) for a just estimate of $1.

(c) Decision

The court agreed that there is likely to be surplus in the liquidation and that the subordinate claimants have a real financial interest in the administration, entitling them to vote at a meeting during the external administration (including the second meeting of creditors).

In relation to *adjustments to accommodate voting,* the court refused the administrators' request to vary the operation of the rules relating to proofs of debt because those rules already acknowledged that proofs and proxies submitted late could already be disregarded. The court instead advised that the administrators would be justified in doing so.

In relation to *resolutions by subordinate claimants,* the court held that it is desirable to make the modification to the extent necessary to ensure that the subordinate claimants cannot, at least without the concurrence of the ordinary creditors, use their numbers to enhance their priority.

The administrators argued that the task of assessing each of the subordinate claims was complex and time consuming and could lead to further disputes with individual claimants. Brereton J rejected the administrators' arguments stating (at [22]): "I do not consider that the circumstances that the claims may be numerous and their valuation complex and time consuming affords sufficient reason for not undertaking the exercise at all." The court refused to make orders under s. 447A requiring a just estimate of $1, stating that it was far from clear that the course proposed would avoid dispute. Brereton J stated it would be a substantial erosion of creditors' rights, which may remove a right of appeal from an administrator's decision on admission of a proof.

Brereton J concluded that the administrators are entitled to take a robust, rough and ready approach to the assessment of claims because claimants may be able to articulate the quantum of their claim. It may be justified to assign only a nominal value to some or all of the subordinate claims for the purposes of voting at the s. 439A meeting, however administrators must first make a genuine attempt to make a "just estimate" of those claims.

This decision acts as a reminder that, no matter how complex or time-consuming it may be to value a subordinate claim, administrators will not be justified in assigning a nominal amount without making an effort to assess value.

6.3 Liquidators' powers to release trust moneys subject to solicitors' lien

(Amber Kennedy, Herbert Smith Freehills)

Re Mamounia Pty Ltd (in liq) (No 3) [2018] VSC 65, Supreme Court of Victoria, Robson J, 20 February 2018

(a) Summary

The liquidators of Mamounia Pty Ltd (in liquidation) (Mamounia) as trustee for the Kurban Family Trust sought directions under s. 511 of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) regarding the distribution of the assets of Mamounia as trustee. Meridian Lawyers (Meridian) and Altus Lawyers (together, the lawyers) provided legal services to Mamounia up to the date of liquidation and were entitled to retain funds in a trust account for Mamounia until payment of their legal costs.

The Court noted that reasonable legal expenses of the solicitors may fall within the principles in *Re Universal Distributing Co Ltd (in liq)* (1933) 48 CLR 171 (*Universal Distributing*), and to the extent that they do not apply, made an order under s. 63 of the Trustee Act 1958 No. 6401 (Vic) (the Trustee Act) to give the liquidators of Mamounia the relevant powers to satisfy the payment and release of the trust moneys. In addition to submissions by the liquidators and the lawyers, the Court was assisted with submissions by the contradictor, Ms C G Rome-Sievers.

(b) Facts

The lawyers provided legal services to Mamounia in its capacity as trustee of a trading trust, being the Kurban Family Trust, prior to the liquidation of Mamounia on 6 June 2016. As at the date of liquidation, Meridian held around $1.5 million and Altus held approximately $232,400 in their respective trust accounts for Mamounia. Except for the sum of around $500,000 retained in Meridian's trust account for Mamounia, the remaining funds were delivered to the liquidators. The lawyers and liquidators agreed that Meridian would retain in its trust account an amount for Altus' legal costs. The liquidators proposed to accept the outstanding amount of the lawyers' fees was approximately $410,950.

Subject to the satisfaction of these outstanding legal fees, the lawyers had a common law possessory lien against this trust property which came into their hands and was retained in Meridian's trust account. This lien was not extinguished by the liquidation of Mamounia.

The liquidators brought an application to the Court when a stalemate arose over these trust moneys, which the solicitors were unable to release on their own part and which the liquidators were unsure if they had the power to release while subject to the lien.

(i) The application

The liquidators applied under s. 511 of the Corporations Act to ask the Court to determine whether they have the power to direct, and are justified in directing, Meridian to withdraw the agreed sums from its trust account, subject to the lien to pay itself and Altus, before paying the balance to Mamounia.

The liquidators submitted that if Mamounia's right of indemnity as trustee of the trust is a personal asset of Mamounia, the liquidators' power to direct payment would arise under s. 477 of the Corporations Act, which gives the liquidators power to compromise or make any arrangement.

Alternatively, if Mamounia's right of indemnity as trustee of the trust is trust property, as bare trustee, Mamounia needs the power to pay the debts of the lawyers conferred on it under s. 63 of the Trustee Act.

In this event, the plaintiff sought orders that pursuant to s. 63 of the Trustee Act, Mamounia and/or the liquidators have conferred on them the power to direct the distribution of the fund in the manner required. Section 63 of the Trustee Act provides that the Court may, by order, confer upon the trustees any necessary power the Court thinks fit, where in the management or administration of any property vested in trustees any release is in the opinion of the Court expedient, but cannot be effected by reason of the absence of any power for that purpose.

(ii) Submissions of the lawyers and contradictor

The lawyers submitted that the property over which the lien was claimed was equivalent to the legal fees in respect of which Mamounia had a right of exoneration.

The lawyers submitted that this proceeding relates to enforcement of a security interest and that three equitable interests in the trust property arose:

- the liquidators' first-ranking equitable lien, and indemnity under the *Universal Distributing* principles, for their costs and expenses reasonably incurred;
- Mamounia's equitable lien which secures its trustee's right of indemnity and/or exoneration, in respect of any expense or liability incurred by it as trustee in the course of administering the trust; and
- the entitlement of objects of the trust to the residual trust property.

The question whether the trustee's right of indemnity and/or exoneration, by reference to which the lien is claimed, is property "of" the company for the purposes of the Corporations Act was said not to arise. The lawyers stated there was no occasion to invoke the priority provisions under the Corporations Act in circumstances where there were no competing creditors that may impinge on the rights of the lawyers as secured creditors. The lawyers submitted that the jurisdictional basis for the liquidators' application is s. 511 of the Corporations Act and/or s. 63 of the Trustee Act (and, if need be, rl. 54.02 of the Supreme Court Rules).

The contradictor concluded that the fact that the fund is a trust asset does not affect the lawyers' right to retain possession of the fund until after their fees are paid and that the solicitors' lien over a trust asset is not subrogated to the trustee's right of exoneration. The contradictor noted the impasse will remain until the owner of the fund exercises a power to pay the legal fees.

(c) Decision

Robson J agreed that payment of the trust moneys to the solicitors required a power to do so. His Honour referred to the *Universal Distributing* principles, stating that the liquidators would be entitled to, and in his opinion justified, in using the trust money to meet some, if not all, the expenses charged and "reasonably incurred in the care, preservation and realisation of the property" on the part of the solicitors.

In the event these principles do not apply to meet the liabilities incurred by Mamounia to the lawyers, Robson J made orders under s. 63 of the Trustee Act to grant the liquidators the necessary powers to pay trust moneys to the lawyers.

Robson J held that the funds retained were trust assets and not the property of Mamounia, noting that this meant that the power to release the trust funds could not be conferred on the liquidators under s. 477 of the Corporations Act.

(i) Legal principles

A solicitor has a common law possessory lien over all property of the client in their possession in respect of the taxable costs which the client is liable for. The lien is a right in rem, exercisable upon the possessed property and requires no intervention from the Court. The lien is passive and is not enforceable by action but affords a defence to an action for recovery of the goods by a person who, but for the lien, would be entitled to immediate possession. The solicitor's right to possession over property provided by a client is no greater than that of the client

Mamounia had an equitable lien under s. 36(2) of the Trustee Act and under cl. 24 of the trust deed, which secures its right of indemnity and/or exoneration for any expense or liability incurred by it as trustee in the course of administering the trust. Mamounia's right of indemnity as trustee takes priority over any rights or objects of the beneficiaries.

When the lawyers provided legal services to Mamounia as trustee of the trust, Mamounia became personally indebted to the lawyers for the payment of the legal fees as trustee. The lawyers had a lien against the trust property that came into their hands, which the beneficiaries could not demand return of. As the liquidation of Mamounia did not extinguish the liens, the lawyers were legally entitled to retain possession of the trust property in the fund, and the liquidators did not think they had the power to release the trust moneys to pay the lawyers' fees, and thus recover the balance of trust moneys being held by the lawyers.

Insofar as the *Universal Distributing* principles do not justify the payment by the liquidators of Mamounia of trust money to the lawyers in satisfaction of their claims, the liquidators of Mamounia, as bare trustee, do not have power to use the trust funds. To resolve this issue, Robson J ordered under s. 63 of the Trustee Act that the liquidators of Mamounia be given power to apply and release Mamounia's interest as trustee, in the funds held by the lawyers, in order to satisfy the lien of the lawyers.

6.4 Application for extension of time to file claim to void insolvent transaction granted

(Jonathan Bisset, Ashurst)

Marsden (liquidator) v CVS Lane PV Pty Limited, in the matter of Pentridge Village Pty Limited (in liq) (receiver and manager appointed) (controller appointed) [2018] FCA 102, Federal Court of Australia, Gleeson J, 16 February 2018

(a) Summary

Mr Marsden (the Liquidator), the liquidator of Pentridge Village Pty Limited (Pentridge), successfully applied for an order to extend the time limit under s. 588FF(3) of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act), obtaining an extension of time to investigate whether to initiate claims in respect of a series of potentially insolvent transactions. Most notably, the Court granted the extension because the Liquidator's delay was sufficiently explained by a lack of funding.

Separately, the Liquidator unsuccessfully sought to have CVS Lane PV Mezz Pty Ltd (CVS Mezz), reinstated pursuant to s. 601AH(2) of the Corporations Act, which permits a party aggrieved by the deregistration of a company to apply for its reinstatement. The Court held that it was too premature to reinstate CVS Mezz in order to permit the Liquidator to make a claim against it prior to the Liquidator actually filing such claim.

(b) Facts

(i) Financing arrangements

Pentridge undertook to redevelop a parcel of land situated on the old site of the Pentridge prison, initially financed by a loan from Capital Finance Australia Limited (the CFAL Loan).

Between May and November 2012, the directors of Pentridge arranged to refinance the CFAL Loan through a series of transactions and formed Daimleigh Capital Pty Ltd (Daimleigh) as a special purpose vehicle to obtain funds for this purpose.

Daimleigh initially obtained funds from the first and second defendants, CVS Lane PV Pty Ltd (CVS) and CVS Mezz (together the CVS Parties), on terms under which Pentridge guaranteed the loans and granted security over all of its property.

CVS also entered into a Call Option Deed under which CVS was granted a call option over the shares in Daimleigh and the units in the corresponding trust. The option could be exercised for $1 per share and per unit and could only be exercised if, at the end of a specified "grace period", the "Outstanding Amount" under the loan facilities had not been re-paid in full.

Daimleigh later entered into separate loan facilities with each of Global Consulting Services Pty Ltd (GCS) and Gresham Property Investments Limited (Gresham), the third defendant. Both loans included guarantees and security from Pentridge. The rights of the funders against the Pentridge secured properties were governed by an inter-creditor deed providing priority first to CVS, second to CVS Mezz, third to Gresham, fourth to GCS, and fifth to Daimleigh.

(ii) Standstill and option cancellation fees

From February 2014, Daimleigh and Pentridge entered into a series of "standstill" agreements, under which the CVS Parties and Gresham agreed not to enforce their rights under the loan facilities and securities in exchange for standstill fees to be paid by Daimleigh. The standstill fees formed part of the secured money under the facilities, and were therefore covered by Pentridge's guarantee and security.

In June 2014, the CVS Parties, Daimleigh and Pentridge (amongst others) entered into a Side Deed to the Call Option Deed which involved CVS agreeing not to exercise its call option in exchange for a fee.

(iii) Potential claims

The Liquidator considered that Pentridge was insolvent from at least November 2013 and that the alleged agreements by Pentridge to capitalise the standstill fees and option cancellation fees to the debts of Daimleigh, securing them against the assets of Pentridge, may be voidable pursuant to s. 588FE(2) of the Corporations Act. The Liquidator claimed that the standstill fees increased the debts owed by Daimleigh to the funders (and secured against the assets of Pentridge) by a total of $800,000, while the call option fee increased the debts by $850,000.

(iv) Timeline of key events in the administration of Pentridge

17 July 2014: receivers and managers were appointed to Pentridge.

20 August 2014: Andrew Beck and Paul Stewart (two former partners of the Liquidator) are appointed joint and several liquidators of Pentridge.

1 April 2015: receivers and managers sold the Pentridge security properties, repaying the CVS Parties in full other than the option cancellation fee.

27 May 2015: CVS Mezz is deregistered.

15 April 2016: Mr Marsden appointed liquidator of Pentridge following resignation of Mr Stewart on 1 January 2016 and Mr Beck on 13 April 2016.

April to November 2016: the Liquidator sought to obtain an understanding of the financial affairs of Pentridge, including the external administration to date, and investigated and pursued potential claims against the Construction Forestry Mining and Energy Union and CFAL.

September 2016: Gresham contacted the Liquidator regarding potential claims in relation to the option cancellation fee.

December 2016 to February 2017: the Liquidator sought advice in relation to the potential claims and began to arrange a funding agreement with Gresham.

May 2017: GCS contacted the Liquidator regarding potential claims against Gresham with respect to the standstill fees.

19 July 2017: both Gresham and GCS have agreed to fund potential claims.

20 July 2017: the Liquidator sought an extension of time to conduct investigations in order to determine whether to initiate the claims.

(c) Decision

Ordinarily, pursuant to s. 588FF(3) of the Corporations Act, an application to void a transaction of a company under s. 588FE can only be made between the relation-back day (here, the date that receivers and managers were appointed - 22 July 2014) and the later of 3 years after the relation-back day and 12 months after the first appointment of a liquidator. This would have required the Liquidator to file the claims before 22 July 2017. However, the Court exercised its discretion under s. 588F(3)(b) to grant an extension after considering three key criteria, citing *Walker and Moloney v CBA Corporate Services Pty Ltd (in liq)* [2012] FCA 328 (*Walker*) at [43].

(i) The Liquidator's explanation for the delay

The Liquidator gave three key reasons for the delay: insufficient funds available to conduct the necessary enquiries, the complexity of the liquidation, and the inadequacy of the books and records provided to the liquidators. Note that the Liquidator was required to explain the delay over the entire period of the liquidation, and not merely from when he personally took over from the previous liquidators.

The CVS parties contended that the liquidator could have done more to investigate the potential claims prior to obtaining funding, and that the Liquidator failed to explain why he had not sought and obtained funding for the proposed investigations sooner. However, the Court ultimately accepted that the lack of funding was a sufficient explanation of the delay. The complexity of the liquidation and inadequacy of books and records were obstacles faced by the liquidators in conducting unfunded investigations, however the real obstacle to progress was the lack of funding. Importantly, there was nothing to indicate that funding could have been obtained earlier had the Liquidator taken proactive steps to seek funding, the Liquidator was not required to demonstrate that he had taken any such steps, and the Liquidator acted promptly upon obtaining funding.

(ii) The merits of the foreshadowed proceeding

On the issue of merits, the Court considered "whether such proceedings would be so devoid of prospects that it would be unfair, by granting an extension, to expose the other party to the continuing prospect of suit" (at [60] quoting *Walker* at [44]). The Court did not undertake a complete review of the merits of the prospective claims, but rather was satisfied that they had sufficient merit to warrant investigation.

(iii) The likely prejudice to be suffered if the extension of time is granted

The CVS Parties did not point to any specific prejudice arising from the extension of time.

Finally, the Court denied the application to reinstate CVS Mezz in order to obtain relevant documents and potentially initiate proceedings against CVS Mezz, noting that documents belonging to CVS Mezz could be sought by enquiring with ASIC, and that CVS Mezz could be reinstated when and if a claim is actually initiated against it.

6.5 No duty of care owed by UK parent company for environmental damage caused by Nigerian subsidiary

(Corrina Virtanen, King & Wood Mallesons)

HRH Emere Godwin Bebe Okpabi v Royal Dutch Shell Plc [2018] EWCA Civ 191, England and Wales Court of Appeal, Civil Division, Chancellor Vos, Sales and Simon LJJ, 14 February 2018

(a) Summary

The England and Wales Court of Appeal has affirmed the decision of a single judge of the High Court that there was no arguable case that United Kingdom parent company Royal Dutch Shell Plc ("RDS") owed a duty of care to those affected by environmental damage and contamination, caused by spills from oil pipelines operated by its Nigerian subsidiary Shell Petroleum Development Company of Nigeria Ltd (SPDC). The appeal was dismissed on the basis that the claimants had failed to demonstrate that they had any reasonable prospects of success in establishing that RDS owed them a duty of care. Therefore the Court did not have jurisdiction to deal with the matter.

(b) Facts

The claimants in this case are Nigerian citizens that own or occupy land adjacent to oil pipelines operated by SPDC where serious and ongoing environmental damage and pollution has been caused by oil spills. The oil spills have been caused by alleged negligent management of the oil pipelines and associated infrastructure.

The claimants brought a claim in negligence against RDS, on the basis that as parent company, RDS owed a duty to those affected by the operations of SPDC, its Nigerian subsidiary. This is because RDS had assumed responsibility for and had taken control of, pipeline integrity, security and remediation in Nigeria.

RDS argued that the Court had no jurisdiction to hear the claim, or if the Court did have jurisdiction, it should not exercise it. In order to establish jurisdiction, the claimants were required to demonstrate that their claim had real prospects of success. The claimants were required to demonstrate a properly arguable case that RDS owed them a duty of care on the basis of assumption of responsibility or control over SPDC's oil pipeline operations.

Consistent with the principles in *Chandler v Cape Plc* [2012] EWCA Civ 525, where it was held that the parent company was responsible for the health and safety of a subsidiary's employees, the claimants pleaded that RDS owed a duty of care on the basis of its:

- control and direction of the management of SPDC's environmental compliance and operation of its infrastructure;
- knowledge of the environmental damage caused by SPDC;
- superior expertise, knowledge and resources concerning environmental protection; and
- knowledge that SPDC would rely on that superior expertise, knowledge and resources.

(c) Decision

(i) Decision at first instance

At first instance, Fraser J held that RDS did not owe the claimants a duty of care, as on the evidence before the Court the claimants had failed to establish the second and third elements of the following three-staged test:

1. that damages were foreseeable;
2. there was a relationship of proximity between RDS and the claimants; and
3. it would be fair, just and reasonable to impose a duty of care on RDS.

Fraser J concluded that there was no evidence of any appreciable level of oversight or control. The claimants appealed the decision on the grounds that Fraser J wrongly excluded and ignored certain evidence which in fact showed a high level of control of, and assumption of, responsibility for SPDC's activities by RDS.

(ii) Decision of the majority of the Court of Appeal

A majority of the Court of Appeal (Sales LJ dissenting) agreed that Fraser J had erred in the way that he had approached the evidence before him and therefore saw it appropriate to reconsider the decision.

Accepting that foreseeability of damages had been established, Simon LJ and Chancellor Vos in separate judgments, considered the issues of proximity and whether it was fair, just and reasonable to impose a duty of care on RDS.

In order to demonstrate that RDS assumed responsibility for and control over SPDC's operations, the claimants relied on five main factors, namely RDS's:

- imposition of mandatory policies, standards and manuals, which applied to SPDC;
- imposition of mandatory design and engineering practices;
- imposition of a system of supervision and oversight in relation to compliance with RDS policies and standards;
- imposition of financial control over SPDC; and
- high level direction and oversight of SPDC's operations.

In relation to each of these factors, the claimants pointed to numerous supporting documents, including the Shell Control Framework, the Shell Health, Safety, Security, Environment and Social Performance Framework, Shell Sustainability Reports, Oil Spill Emergency Response and Design and Engineering Practices, as well as oral evidence of former Shell employees as to the structure of the Shell group of companies (the Shell Group). The claimants also highlighted that Nigeria was considered to be one of the highest risk countries in the Shell Group portfolio and that it required particular attention and monitoring from RDS.

Whilst Simon LJ and the Chancellor accepted that the evidence demonstrated that the Shell Group was organised along business and function lines, as well as by legal entities, which assisted the claimants' case, there were fundamental issues with the evidence that could not be overcome. In particular:

- the mandatory policies, standards and manuals relied upon formed part of a centralised system, consistent with industry practice, which applied in a standardised way across the Shell Group;
- RDS did not itself enforce the mandatory policies, standards and manuals but rather left SPDC to operate the system of supervision and oversight;
- the Shell Control Framework document constituted high level guidance that was made available to RDS's subsidiaries, but did not indicate control;
- RDS's high level concern about proper controls in relation to the risks and security of SPDC's operations in Nigeria did not amount to control; and
- where extracts from the documents tendered as evidence were published for the purposes of informing shareholders and regulators, they must be read in their proper context.

Therefore, none of the factors identified or the material relied upon, alone or cumulatively, demonstrated a sufficient degree of control over SPDC's operations to establish proximity. Further, all of the claimants' arguments as to whether it was fair, just and reasonable to impose a duty of care, including the importance of multi-national parent companies conducting themselves consistently with international standards, were found to be unpersuasive and were dismissed.

Although taking a different approach to the evidence than Fraser J, both Simon LJ and the Chancellor ultimately reached the same conclusion, that the claim had no real prospects of success and the Court had no jurisdiction to hear the case.

(ii) Decision of Lord Justice Sales

Sales LJ dissented and held that the claimants did in fact have a good arguable case that RDS owed them a duty of care, which RDS had relevantly breached.

Sales LJ considered that as RDS was acutely aware of the heightened risk in Nigeria, it could be inferred that they may wish to exercise direct control over SPDC if it were ineffectively managing oil spills. Sales LJ also observed that on the evidence it was arguable that the management structure of the Shell Group was intended to enable central management to provide expertise and exert control over the operations of subsidiaries operating in each business line. None of these factors were said to be contradicted by RDS's evidence.

On Sales LJ's assessment of the evidence, it was shown that the claimants had a good and arguable case that RDS owed them a duty of care, which ought to be tried.

6.6 Should leave to proceed be granted for multiple class actions against an externally administered company?

(Matthew Edwards, Clayton Utz)

In the matter of DSHE Holdings Ltd (receivers and managers appointed) (in liq) [2018] NSWSC 82, Supreme Court of New South Wales, Black J, 9 February 2018

(a) Summary

This case concerned an application by Mr and Mrs Mastoris for leave pursuant to s. 500 of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) to commence representative proceedings against DSHE Holdings Pty Ltd (Receivers and Managers Appointed) (In Liquidation) (DSH). DSH was the ultimate holding company of the Dick Smith Group and Mr and Mrs Mastoris sought to bring claims relating to a prospectus of DSH alleging breaches of the ASX continuous disclosure rules and misleading or deceptive conduct (Mastoris Proceedings).

The application was opposed by Mr and Mrs Findlay who were the lead plaintiffs in separate representative proceedings that had already been commenced in the same Court relating to the affairs of DSH (the Findlay Proceedings).

There was likely to be insurance cover for the claims. It was argued that, should leave be granted in the Mastoris Proceedings, it would result in further erosion of the insurance cover in circumstances where there was "no good reason" that the claimants in the Mastoris Proceedings could not join with the claimants in the Findlay Proceedings.

In deciding to grant leave to proceed, Black J considered that denying leave would create an undesirable incentive to be the first to commence a class action and shut out competing actions. He did not wish to impede upon a claimant's ability to choose their own lawyers and funders and considered that the issue could be addressed by well-established case management practices.

(b) Facts

In January 2016 DSH and nine of its subsidiaries were placed into voluntary administration and, ultimately, entered into liquidation. Unsecured creditors were likely to face a significant shortfall in their debt and, as a result, it was not expected that shareholders of DSH would receive any return in the liquidation.

There was likely to be insurance available pursuant to a D&O Policy. A number of proceedings had been commenced in order to access those insurance funds, including:

- proceedings by the Receivers and Managers;
- proceedings by two secured creditors; and
- the Findlay Proceedings.

By this application Mr and Mrs Mastoris sought leave to commence further representative proceedings against DSH. The Mastoris Proceedings differed to the Findlay Proceedings in that it advanced a prospectus claim and advanced misleading and deceptive conduct claims for a wider period.

Evidence was given that 796 group members had signed funding agreements in the Findlay Proceedings. The individual defendants had already filed Defences in the Findlay Proceedings and case management orders had been made requiring DSH to file its defence and for the delivery of the lay and expert evidence of Mr and Mrs Findlay. That being the case, the solicitors for Mr and Mrs Mastoris indicated that their clients would be ready to serve their evidence on the dates required by the case management orders in the Findlay Proceedings, reducing any delay if the matters were to be heard together.

(c) Decision

Section 500(2) of the Corporations Act provides that, after the passage of a resolution for voluntary winding up, no action or other civil proceeding is to be proceeded with or commenced against a company except with the leave of the Court and subject to such terms as the Court imposes. The purpose of this section is to prevent the assets of a company being dissipated by unnecessary litigation.

A party applying for leave is required to show:

- why it should not be left to prove its debt in the winding up; and
- that the claim has a solid foundation and gives rise to a serious question to be tried.

Black J was satisfied that the Mastoris Proceedings had a solid foundation and that it gave rise to a serious dispute. He was also of the view that there were good reasons to depart from the usual proof of debt process given the likely complexities surrounding the case and the fact that a judgment would be necessary to access DSH's insurance coverage.

Counsel in the Findlay Proceedings did not oppose the grant of leave to the Mastoris Proceedings so far as their respective claims did not overlap. Instead, Counsel requested that Black J use his discretion to refuse leave to the extent the Mastoris Proceedings duplicated claims made in the Findlay Proceedings. In that respect it was argued that if the Mastoris Proceedings were allowed to continue it would cause unnecessary expense and that there was "no good reason" for leave to be granted with respect to those aspects of the claim.

His Honour accepted that the additional costs likely to be incurred in the defence of the Mastoris Proceedings would erode the relevant insurance cover. However, given the presence of the proceedings by the Receivers and secured parties, it was his view that additional defence costs would likely result in any event.

Counsel for Mr and Mrs Findlay argued that the participants in the Mastoris Proceedings could join the Findlay Proceedings. However, his Honour considered that this gave too little weight to a number of matters, including:

- a participant's preference to choose their own legal representatives;
- a participant's ability to enter into a different form of funding agreement; or

- a participant's ability to advance a wider case (and/or the need to split their case across multiple proceedings).

Black J noted that it would be a surprising result if the commencement of the Findlay Proceedings was to shut out the possibility of alternative claims brought by individual shareholders. Such a result would be inconsistent with the opt out regime adopted by the Courts and would create an undesirable incentive to be the first to commence a class action.

It was noted that there was scope for the Mastoris and Findlay Proceedings to be heard together and his Honour drew attention to the Court's ability to case manage parallel representative proceedings. While accepting that such a step may create additional costs, his Honour could not conclude that the increase in cost outweighed the interests of the participants in the Mastoris Proceedings. As a result, his Honour made orders granting leave for the commencement of the Mastoris Proceedings in accordance with s. 500 of the Corporations Act.

6.7 Court orders winding up of a managed investment scheme on just and equitable grounds in circumstances of a variety of contraventions of the Corporations Act

(Grant Mason, Corrs Chambers Westgarth)

Australian Securities and Investments Commission v Realestate Equity Investment Trust [2018] FCA 50, Federal Court of Australia, Murphy J, 6 February 2018

(a) Summary

The plaintiff regulator, Australian Securities and Investments Commission (ASIC) conducted investigations of an entity, Lotus Securities Pty Ltd (in liquidation) (Lotus). Those investigations revealed concerns in relation to the operation of the defendant managed investment scheme, Realestate Equity Investment Trust (REIT or the Scheme). Prior to its winding up, Lotus had been the responsible entity of REIT. ASIC's investigations disclosed multiple contraventions of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) by Lotus and the Scheme. ASIC applied to the Court to have the Scheme wound up on the ground that it was just and equitable to do so and obtained orders to that effect despite opposition from some of REIT's unit holders.

(b) Facts

In 2010, REIT acquired approximately 63 hectares of real property in Lara, Victoria, within the Geelong City Council region (the Lara Property). On 25 August 2010, by way of a product disclosure statement (PDS), REIT invited members of the public to acquire units in the Scheme. Under the Scheme it was proposed that unit holders would acquire the right to purchase a sub-divided parcel of the Lara Property within 5 years of the commencement of the Scheme. At the time of the PDS the Lara Property was zoned for farming use and would need to be re-zoned in order to be used for residential purposes.

Initially, Perpetual Nominees Limited (Perpetual) was the Custodian of the Scheme, and in that capacity Perpetual opened bank accounts for the Scheme and became the registered owner of the Lara Property.

Around October 2010, Lion Advantage became the Scheme's responsible entity until, in August 2012, its Australian Financial Services Licence (AFSL) was cancelled by ASIC, subject to being permitted to transfer the control of the Scheme to another responsible entity or to wind up the Scheme. On 18 June 2014, Lotus obtained an AFSL, at which time it became the Scheme's responsible entity.

On 20 September 2016, ASIC cancelled Lotus' AFSL due to failures by Lotus to comply with the Corporations Act.

ASIC applied to the Court for orders winding up the Scheme and related orders. REIT opposed those orders and relied on affidavits from five unit holders which cited concerns by those unit holders that they would obtain a lower return from the Scheme if orders were made to wind it up. REIT also sought an adjournment of the application to wind up REIT on the basis that it wished to be allowed time to locate and appoint an alternate responsible entity.

(c) Decision

Murphy J declined the adjournment application citing, among others, the following concerns:

- uncontested evidence from ASIC that provided a real basis for his Honour to consider that the Scheme had been operated in substantial non-compliance with the Act, that unit holders' monies had not been properly accounted for and that those monies may have been misused;
- the proposed new responsible entity, Starin Ltd, did not have an appropriate AFSL and had not applied to ASIC for a variation of the terms of its existing AFSL that would allow it to act as the responsible entity;
- a memorandum of understanding had been signed but did not provide certainty that Starin would actually become responsible entity of the Scheme, because Starin's appointment was conditional upon legal and due diligence requirements being finalised, which enquiries were to be conducted at the expense of funds from the Scheme thereby reducing returns potentially available to unit holders;
- any enquiries conducted by Starin were likely to lead it to the conclusion that the Scheme had substantially failed to comply with its obligations under the Act, meaning that Starin was unlikely to accept the role as responsible entity;
- the likely insolvency of the Scheme, meaning that an adjournment would only be appropriate in exceptional circumstances; and
- the public interest in ensuring that managed investment schemes are conducted in accordance with the Act and the relevant PDS.

Murphy J was satisfied that there was a basis to order that the Scheme be wound up on the ground that it was just and equitable to do so. In reaching that conclusion, his Honour relied on the following factors:

- the Scheme was insolvent, in the broad sense of that word as it applied to managed investment schemes, because the Scheme was unable to pay its debts as and when they fell due. For example, Perpetual had ceased providing custodian services on the basis that fees owed to it had not been paid. However, the extent of the insolvency was not clear as financial statements had not been filed since 2012;
- Lotus, the responsible entity of the Scheme was insolvent;
- the Scheme was without a responsible entity and, despite attempts to locate an alternate responsible entity, no willing and proper responsible entity had been found;
- the purpose of the Scheme had failed because no steps had been taken to rezone the Lara Property and the Scheme was intended to result in a return to unit holders within five years. The hearing took place more than 7 years after the Scheme had commenced;
- REIT and Lotus had breached the Act on a number of separate occasions;
- the Scheme's books and records were incomplete;
- some of the unit holders' funds were unaccounted for and there were concerns as to the use of some of the unit holders' funds;

- the Scheme did not have a valid PDS, in circumstances where the PDS had been withdrawn in December 2012, at ASIC's request, and had never been re-issued;
- the PDS that had been relied on, prior to being withdrawn, was misleading in material ways; and
- the unit holders were unable to redeem their investments even though more than five years had passed since those units had been acquired.

Having considered those issues collectively, his Honour had no difficulty concluding that the affairs and management of the Scheme were "being conducted in a manner that [was] prejudicial to unit holders' interests, and that unit holders' funds [were] at risk". His Honour further observed that ASIC had "a justifiable lack [of] confidence that the Scheme and its management will comply with their obligations under the Act".

As well as ordering that the Scheme be wound up on the basis that it was "plainly just and equitable" to do so, Murphy J ordered that receivers be appointed to the Scheme's assets so that those assets could be sold in a practical manner, as Lotus was already in liquidation. His Honour ordered that the receivers would have all the usual powers but limited their powers of investigation to restrict the Scheme's limited available funds being further depleted.

6.8 Corporate group and director fined $7.8 million for "egregious" breaches of Future of Financial Advice obligations

(James Campbell, King & Wood Mallesons)

Australian Securities and Investments Commission v Wealth & Risk Management Pty Ltd (No 2) [2018] FCA 59, Federal Court of Australia, Moshinsky J, 5 February 2018

(a) Summary

In this case, the Federal Court held that a corporate group and its common director had committed "egregious" breaches of the Future of Financial Advice (FoFA) obligations under the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) and the Australian Securities and Investments Commission Act 2001 No. 51 (Cth) (the ASIC Act) and imposed pecuniary penalties totalling $7.8 million.

Wealth & Risk Management Pty Ltd (WRM) and two related companies, Jeca Holdings Pty Ltd (JECA) and Yes FP Pty Ltd (Yes FP), were found to have committed numerous breaches of the FoFA obligations, including the "best interest obligations" under Part 7.7A, Division 2 of the Corporations Act. A director of those companies was also found to have been an accessory to some of those contraventions.

The contraventions related to a "cash rebate scheme" operated by the defendants, under which cash payments were made to clients on condition that they pay for, and implement, financial advice from WRM related to superannuation and insurance products. Moshinsky J found that the scheme deliberately targeted and exploited financially disadvantaged and vulnerable people.

In addition to the pecuniary penalties, Moshinsky J made declarations and granted injunctions restraining each of the corporate defendants from carrying on a financial services business for 18 years and their director for 10 years.

(b) Facts

(i) The parties

WRM, as the holder of an Australian Financial Services Licence (AFSL), was authorised to provide advice to retail clients about life insurance and superannuation products. JECA (trading as Yes FS) was the marketing arm of the WRM business and had at no time held an AFSL or been authorised under such a licence. Yes FP was a corporate authorised representative of WRM, who employed most of WRM's authorised representatives (ARs) to provide advice on life insurance and superannuation products. Mr Fuoco was a director and the sole shareholder of each of the corporate defendants.

(ii) The cash rebate scheme

The contraventions arose from a business scheme conducted by the corporate defendants which involved offering and giving cash payments to clients in connection with the provision of financial advice (the "cash rebate scheme"). The cash rebate scheme operated from December 2015 to May 2017, when the Federal Court made interlocutory injunctions against the corporate defendants restraining them from operating the scheme.

Under the cash rebate scheme, JECA attracted prospective clients through the Yes FS website and online advertising. Its marketing specifically targeted people with a poor credit history who were seeking credit, fast cash or debt management advice, using statements such as "FAST PRE QUALIFICATION: CASH FROM $2,000 - $20,000" and "NO CREDIT CHECK REQUIRED.Receive $1000 to $2000 emergency funding directly into your account". However, in order to obtain access to a cash payment, the applicant would generally be required to comply with the following conditions of eligibility:

- receive and implement financial advice from WRM, the fee for the advice being charged to the applicant's superannuation fund typically in the range of 2-20% of their superannuation balance;
- replace their existing superannuation fund provider with another, typically a retail fund, recommended by an AR;
- purchase or switch life, total and permanent disability and/or income protection insurance policies (typically all three) on the advice of an AR; and
- agree to annual insurance premiums being charged against their superannuation, typically a substantial portion of the employer's annual contribution to the fund (and in some instances more).

At no time, though, did JECA's advertising disclose these conditions of eligibility for a cash payment, nor did it provide credit or debt management advice even where such advice was sought by clients in their application forms. A prospective client who wished to apply for a cash payment was instead referred to an AR, who would obtain the various insurance quotes referred to above.

As well as receiving the advice fee and ongoing commissions, WRM received an up-front commission from the insurance provider on the insurance purchased by the applicant. Pursuant to a referral agreement between WRM and JECA, WRM paid the up-front commission to JECA who then made a cash payment to the applicant.

(c) Decision

(i) Breaches of FoFA obligations

Moshinsky J held that the defendants' operation of the cash rebate scheme gave rise to numerous significant breaches of the FoFA obligations under the Corporations Act and the ASIC Act.

These included that:o:p>

- WRM had breached s. 961L of the Corporations Act, requiring a financial services licensee to take reasonable steps to ensure that its representatives comply with the "best interests obligations" under Part 7.7A, Division 2 of the Corporations Act. By administering the cash rebate scheme, the ARs had variously failed to act in the best interests of clients (s. 961B), provide advice appropriate to the client (s. 961G), warn clients that relevant information was incomplete or inaccurate (s. 961H) and give priority to the client's interests in the event of a conflict (s. 961J);

- in connection with the above, WRM had breached ss. 912A(1)(a) and 912A(1)(ca) of the Corporations Act, by failing to take reasonable steps to ensure that its representatives comply with the financial services laws and to ensure that financial services covered by its licence were provided efficiently, honestly and fairly;
- JECA had breached s. 1041H of the Corporations Act and ss. 12DA and 12DB(1)(f) of the ASIC Act, by engaging in conduct that was misleading and deceptive in connection with its provision of financial services. By making the statements published on its website and in its online advertising, JECA falsely represented that it provided fast credit and personal loans and that it was licensed to do so; and
- by deploying unfair tactics specifically targeting clients who, because of their urgent need for cash, were in a very weak bargaining position, WRM, JECA and Yes FP had breached s. 12CB of the ASIC Act, by engaging in unconscionable conduct in connection with the supply or possible supply of financial services to a person.

Moshinsky J found that Mr Fuoco was knowingly concerned in some of these contraventions, as the "mastermind and architect" of the cash rebate scheme.

(ii) Relief

Moshinsky J considered that the targeting and exploitation of financially disadvantaged and vulnerable people made the cash rebate scheme "a particularly egregious example of the kind of conduct that the statutory provisions are designed not merely to prevent, but to dissuade and sanction in the strongest terms".

His Honour ordered that the corporate defendants pay pecuniary penalties totalling $7,150,000 for their contraventions and that Mr Fuoco pay $650,000 for his accessorial involvement. The defendants were ordered to pay ASIC's costs.

His Honour further made declarations and granted injunctions restraining the corporate defendants from carrying on a financial services business for 18 years and Mr Fuoco for 10 years.

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.

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