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Bulletin No. 278

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Legislation Hotline

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1. Recent Corporate Law and Corporate Governance Developments

1.1 FSB publishes high-level recommendations for regulation, supervision and oversight of "global stablecoin" arrangements

13 October 2020 - The Financial Stability Board (FSB) has published the final version of its high-level recommendations for the regulation, supervision and oversight of "global stablecoin" (GSC) arrangements following an earlier public consultation. The report states that GSC arrangements are expected to adhere to all applicable regulatory standards and to address risks to financial stability before commencing operation, and to adapt to new regulatory requirements as necessary.

So-called "stablecoins" are a specific category of crypto-assets which have the potential to enhance the efficiency of the provision of financial services, but may also generate risks to financial stability, particularly if they are adopted at a significant scale. Stablecoins are an attempt to address the high volatility of "traditional" crypto-assets by tying the stablecoin's value to one or more other assets, such as sovereign currencies. They have the potential to bring efficiencies to payments, and to promote financial inclusion. However, a widely adopted stablecoin with a potential reach and use across multiple jurisdictions (a so-called GSC) could become systemically important in and across one or many jurisdictions, including as a means of making payments.

The emergence of GSCs may challenge the comprehensiveness and effectiveness of existing regulatory and supervisory oversight. The FSB has agreed on 10 high-level recommendations that promote coordinated and effective regulation, supervision and oversight of GSC arrangements to address the financial stability risks posed by GSCs, both at the domestic and international level.

The recommendations call for regulation, supervision and oversight that is proportionate to the risks. Authorities agree on the need to apply supervisory and oversight capabilities and practices under the "same business, same risk, same rules" principle.

The performance of some functions of a GSC arrangement may have important impacts across borders. The recommendations also stress the value of flexible, efficient, inclusive, and multi-sectoral cross-border cooperation, coordination, and information sharing arrangements among authorities.

The FSB has agreed to the following further actions as a key building block of the roadmap to enhance cross-border payments commissioned by the G20:

- completion of international standard-setting work by December 2021;
- establishment or, as necessary, adjustment of cooperation arrangements among authorities by December 2021 (and as needed based on market evolution);
- at a national level, establishment or, as necessary, adjustment of regulatory, supervisory and oversight frameworks consistent with the FSB recommendations and international standards and guidance by July 2022 (and as needed based on market evolution); and
- review of implementation and assessment of the need to refine or adapt international standards by July 2023.

1.2 FSB report highlights increased use of RegTech and SupTech

9 October 2020 - The FSB has published a report on the use of supervisory and regulatory technology by FSB members and regulated institutions. The report finds that technology and innovation are transforming the global financial landscape, presenting opportunities, risks and challenges for regulated institutions and authorities alike.

The opportunities offered by supervisory technology (SupTech) and regulatory technology (RegTech) have been created by the substantial increase in availability and granularity of data, and new infrastructure such as cloud computing and application programming interfaces. These allow large data sets to be collected, stored and analysed more efficiently. Authorities and regulated institutions have both turned to these technologies to help them manage the increased regulatory requirements that were put in place after the 2008 financial crisis.

SupTech and RegTech tools could have important benefits for financial stability. For authorities, the use of SupTech could improve oversight, surveillance and analytical capabilities, and generate real-time indicators of risk to support forward-looking, judgment-based, supervision and policy making. For regulated institutions, the use of RegTech could improve compliance outcomes, enhance risk management capabilities, and generate new insights into the business for improved decision-making. For both authorities and regulated institutions, the efficiency and effectiveness gains, and possible improvement in quality arising from automation of previously manual processes, is a significant consideration.

SupTech is a strategic priority for an increasing number of authorities. Based on a survey of FSB members, the majority of respondents had SupTech, innovation or data strategy in place, with the use of such strategies growing significantly since 2016. Authorities are also vigilant to possible risks that could arise from the use of SupTech and RegTech technologies. Survey responses indicated that the risk reported to be of greatest concern was around resourcing, followed by cyber risk, reputational risk and data quality issues. A particular risk is over-reliance on methods built on historic data, which could lead to incorrect inferences about the future, and the potential for limited transparency of SupTech and RegTech tools. Looking to the future, the potentially catalytic role of data standards and the importance of effective governance frameworks for the use of SupTech and RegTech were also emphasised.

The report includes 28 case studies giving practical examples on how SupTech and RegTech tools are being used.

1.3 Major insolvency reforms

7 October 2020 - The Federal Government has published a draft bill (the Corporations Amendment (Corporate Insolvency Reforms) Bill 2020) and draft explanatory materials which contain the details of proposed major reforms of Australia's insolvency laws. The draft bill and explanatory materials are available on the Treasury website. The publication of these documents follows the announcement, on 24 September 2020, foreshadowing these reforms. In a media release, the Australian Treasurer stated that key elements of the proposed reforms include:

- the introduction of a new debt restructuring process for incorporated businesses with liabilities of less than $1 million, drawing on some key features of the Chapter 11 bankruptcy model in the United States;
- moving from a one-size-fits-all "creditor in possession" model to a more flexible "debtor in possession" model which will allow eligible small businesses to restructure their existing debts while remaining in control of their business;
- a period of 20 business days for the development of a restructuring plan by a small business restructuring practitioner, followed by 15 business days for creditors to vote on the plan. During this time, unsecured and some secured creditors are prohibited from taking actions against the company, a personal guarantee cannot be enforced against a director or one of their relatives, and a protection from ipso facto clauses (that allow creditors to terminate contracts because of an insolvency event) apply (with the same protections applying as during voluntary administration); and
- a new, simplified liquidation pathway for small businesses to allow faster and lower cost liquidation.

These measures will commence on 1 January 2021, subject to the passing of legislation.

Around 76% of companies entering into external administration in 2018-19 had less than $1 million in liabilities. Of these, around 98% are estimated to be businesses with less than 20 full-time equivalent employees.

Further details of the proposed debt restructuring changes

The proposal adopts a "debtor in possession" model. That means that the business can keep trading under the control of its owners, while a debt restructuring plan is developed and voted on by creditors. Business owners will be able to trade in the ordinary course of business when a plan is being developed, prior approval of the small business restructuring practitioner (the practitioner) will be required for trading that is outside the ordinary course of business. The business owners will be required to work with the practitioner to develop and put forward a restructuring plan and to provide information about the business's financial affairs to the practitioner to assist with identifying creditors and to assist creditors in making an informed decision on the restructuring plan.

The practitioner will:

- help determine if a company is eligible;
- support the company to develop a plan and review its financial affairs;
- certify the plan to creditors; and
- manage disbursements once the plan is in place.

A practitioner will not be required to take on personal liability for a company or manage its day-to-day affairs. To support more practitioners being available to work with small business, they will be able to choose to register as a small business restructuring practitioner only. Their practice will be limited to the new simplified restructuring process. Qualifications required to register as a small business restructuring practitioner only will be in line with the streamlined requirements of the role. Registered liquidators will also be able to manage the new process.

If more than 50% of creditors by value endorse the plan, it is approved and binds all unsecured creditors. Creditors vote as one class. Secured creditors are bound by the plan only to the extent their debt exceeds the realisable value of their security interest. To support the integrity of the process, related-party creditors are not entitled to vote. If the plan is approved, the business continues and the practitioner administers the plan by making distributions to creditors according to the terms of the plan. If voted down, the process ends, and the company owners may opt to go into voluntary administration or to use the simplified proposed liquidation pathway.

Safeguards will be included to prevent the process from being used to facilitate corporate misconduct such as illegal phoenix activity. They include a prohibition on related creditors voting on a restructuring plan, a bar on the same company or directors using the process more than once within a prescribed period (proposed at seven years), and the provision of a power for the practitioner to stop the process where misconduct is identified.

The business must pay any employee entitlements which are due and payable before a plan can be put to creditors.

Key mechanisms will be included as part of the restructuring process to ensure that creditor interests are represented and protected. Importantly:

- the role of the practitioner, who will administer the process, remains independent. The practitioner will have important obligations they must fulfil on behalf of creditors (such as certifying the plan);
- key creditor rights will be preserved. For example, there are no changes to the rights of secured creditors, and similar types of debts are treated consistently; and
- creditors retain the right to vote on the debtor company's proposed plan and the plan must achieve the requisite majority to be binding.

The proposed simplified liquidation pathway

The process would be accessible to incorporated businesses with liabilities of less than $1 million (the same threshold that would apply to the new restructuring process).

The simplified liquidation process will retain the general framework of the existing liquidation process, with modifications to reduce time and cost. As currently occurs, the small business can appoint a liquidator who will take control of the company and realise the company's remaining assets for distribution to creditors. The liquidator will also still investigate and report to creditors about the company's affairs and inquire into the failure of the company. Time and cost savings will be achieved through reduced investigative requirements, requirements to call meetings, and reporting functions. Key modifications include:

- reduced circumstances in which a liquidator can seek to claw back an unfair preference payment from a creditor that is not related to the company;
- only requiring the liquidator to report to Australian Securities and Investments Commission (ASIC) (under s. 533) on potential misconduct where there are reasonable grounds to believe that misconduct has occurred;
- removing requirements to call creditor meetings and the ability to form committees of inspection;
- simplifying the dividend process (where creditors receive a return proportionate to their debt) and the proof of debt process (where creditors provide information as to the debt they are owed, which is assessed and accepted or rejected by the liquidator); and
- maximising technology neutrality in voting and other communications.

The rights of secured creditors and the statutory rules as to the payment of priority creditors such as employees will not be modified.

1.4 UK: FCA bans the sale of crypto-derivatives to retail consumers

6 October 2020 - The United Kingdom (UK) Financial Conduct Authority (FCA) has published final rules banning the sale of derivatives and exchange traded notes (ETNs) that reference certain types of crypto assets to retail consumers.

The FCA considers these products to be ill-suited for retail consumers due to the harm they pose. According to the FCA, these products cannot be reliably valued by retail consumers because of the:

- inherent nature of the underlying assets, which means they have no reliable basis for valuation;
- prevalence of market abuse and financial crime in the secondary market (eg. cyber theft);
- extreme volatility in crypto asset price movements;
- inadequate understanding of crypto assets by retail consumers; and
- lack of legitimate investment need for retail consumers to invest in these products.

These features mean retail consumers might suffer harm from sudden and unexpected losses if they invest in these products.

Unregulated transferable crypto assets are tokens that are not "specified investments" or e-money, and can be traded, which includes well-known tokens such as Bitcoin, Ether or Ripple. Specified investments are types of investment which are specified in legislation. Firms that carry out particular types of regulated activity in relation to those investments must be authorised by the FCA.

To address these harms, the FCA has made rules banning the sale, marketing and distribution to all retail consumers of any derivatives (i.e. contract for difference, options and futures) and ETNs that reference unregulated transferable crypto assets by firms acting in, or from, the UK.

The FCA estimates that retail consumers will save around £53m from the ban on these products.

The ban will come into effect on 6 January 2021.

View PS20/10: Prohibiting the sale to retail clients of investment products that reference cryptoassets.

1.5 IFRS Foundation Trustees consult on global approach to sustainability reporting

30 September 2020 - The Trustees of the International Financial Reporting Standards (IFRS) Foundation have published a Consultation Paper to assess demand for global sustainability standards and, if demand is strong, assess whether and to what extent the Foundation might contribute to the development of such standards.

The IFRS Foundation was established to develop a single set of globally accepted accounting standards. It is the organisation behind IFRS Standards - financial reporting standards required for use by more than 140 jurisdictions. The Trustees are responsible for the strategic direction and governance of the Foundation as well as for oversight of the International Accounting Standards Board, which sets IFRS Standards.

Amid heightened focus on environmental, social and governance (ESG) matters, developments in sustainability reporting and increased calls for standardisation of such reporting, the Trustees are now seeking stakeholder input on the need for global sustainability standards and gauging support for the Foundation to play a role in the development of such standards.

The Consultation Paper sets out possible ways the Foundation might contribute to the development of global sustainability standards by broadening its current remit beyond the development of financial reporting standards and using its experience in international standard-setting, its well-established and supported standard-setting processes and its governance structure.

One possible option outlined in the paper is for the IFRS Foundation to establish a new sustainability standards board. The new board could operate alongside the International Accounting Standards Board under the same three-tier governance structure, build on existing developments and collaborate with other bodies and initiatives in sustainability, focusing initially on climate-related matters.

The Consultation Paper sets out critical success factors for the creation of a new board, including the following:

- achieving sufficient support from public authorities and market participants;
- working with regional initiatives to achieve global consistency and reduce complexity in the reporting landscape;
- achieving the appropriate level of funding; and
- ensuring the current mission of the IFRS Foundation is not compromised.

1.6 Consumer credit reforms

25 September 2020 - The Federal Government has announced significant reforms to the regulation of consumer credit. Key elements of the reforms include:

- removing responsible lending obligations from the National Consumer Credit Protection Act 2009 No. 134 (Cth), with the exception of small amount credit contracts and consumer leases where heightened obligations will be introduced;
- ensuring that authorised deposit-taking institutions (ADIs) will continue to comply with the Australian Prudential Regulation Authority (APRA's) lending standards requiring sound credit assessment and approval criteria;
- adopting key elements of APRA's ADI lending standards and applying them to non-ADIs;
- protecting consumers from the predatory practices of debt management firms by requiring them to hold an Australian Credit Licence when they are paid to represent consumers in disputes with financial institutions;
- allowing lenders to rely on the information provided by borrowers, replacing the current practice of "lender beware" with a "borrower responsibility" principle; and
- removing the ambiguity regarding the application of consumer lending laws to small business lending - where a proportion of an application for credit is for a business purpose, irrespective of the proportion, the new framework will not apply.

The Federal Government states that the objective of the proposed reforms is to "enable the more efficient flow of credit to consumers and small businesses while maintaining strong consumer protections". In relation to the proposed reforms relating to responsible lending obligations (RLOs), the government states that RLOs have been implemented in a way "that is no longer fit for purpose and which risks slowing our economic recovery".

"The prescriptive approach in RLO guidance and internal lenders' systems developed to comply with the guidance leaves borrowers and lenders facing a 'one-size-fits-all' approach. This means lenders are required to adopt a similar approach to credit assessment for most consumers and credit products, irrespective of their circumstances. Lenders face prescriptive obligations, with close to 100 pages of guidance advising how they should meet their obligations under RLOs. The guidance puts the onus on lenders to verify information provided by borrowers, with borrowers bearing limited responsibility for providing incorrect or misleading information to lenders. In response, many lenders have put in place detailed and lengthy credit approval processes aimed solely at meeting these requirements, but without necessarily improving a lender's ability to understand if the loan is suitable for the customer."

For further details, see the Department of the Treasury Consumer Credit Reforms Fact Sheet.

1.7 NZ: FMA reports on monitoring of financial services firms and advisers

24 September 2020 - A New Zealand Financial Markets Authority (FMA) report on its supervision activities over the past 18 months says large parts of the financial services sector are working hard to meet the FMA's expectations, but calls for further and more widespread improvements to governance and compliance. The FMA has found weaknesses across its regulated sectors in four main areas:

- governance and oversight;
- conduct and culture;
- compliance assurance programmes; and
- compliance and controls.

A Compliance Assurance Programme (CAP) is required by certain entities regulated by the FMA and entity boards are expected to seek assurances that CAPs are up to standard and to challenge management when needed. Notwithstanding this, the FMA found examples of CAPs that were poorly designed or implemented.

Issues with QFEs, advisers and derivatives issuers

Three sectors were identified as having particular issues: derivatives issuers, authorised financial advisers (AFAs) and qualifying financial entities (QFEs).

A questionnaire completed by derivatives issuers indicated significant weaknesses in the way many issuers assessed customers' knowledge, experience and understanding of derivatives, which are complex financial products. In some cases, issuers had insufficient processes or policies to support their compliance with client money handling obligations. The FMA will be applying targeted monitoring to follow up on the questionnaire responses.

Weaknesses were found in some AFAs' and QFEs' financial advice disclosure practices. The FMA said it will increase its focus on these two sectors and expects improvements, especially given the new financial advice regime, which begins in 2021.

1.8 US: SEC adopts amendments to shareholder proposal rule

23 September 2020 - The United States (US) Securities and Exchange Commission (SEC) has voted to adopt amendments to amend its shareholder proposal rule, which governs the process for a shareholder to have its proposal included in a company's proxy statement for consideration by the company's shareholders.

Under the rules, any shareholder may submit an initial proposal after having held US$2,000 of company shares for at least three years, or higher amounts for shorter periods of time. The rules also provide for a transition period so that shareholders who are currently eligible at the US$2,000 threshold will remain eligible to submit a proposal for inclusion in the company's proxy statement so long as they continue to maintain at least their current holdings through the date of submission (and through the date of the relevant meeting). The amendments also update, for the first time since 1954, the levels of shareholder support a proposal must receive to be eligible for resubmission at future shareholder meetings.

View Final Rule.

1.9 Temporary changes to continuous disclosure provisions for companies and officers extended

23 September 2020 - The Federal Government has announced that the temporary changes to the continuous disclosure provisions have been extended until 23 March 2021.

On 25 May 2020, the Federal Government temporarily amended the continuous disclosure provisions that apply to companies and their officers so that they will only be liable if there has been "knowledge, recklessness or negligence" with respect to updates on price-sensitive information to the market.

The extension has been implemented by the Corporations (Coronavirus Economic Response) Determination (No. 4) 2020 (the Determination). The Determination modifies the operation of the civil penalty provisions in ss. 674(2), 674(2A), 675(2) and 675(2A) of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) to establish a temporary test based on a disclosing entity or its officers' knowledge, recklessness or negligence with respect to whether certain information would have a material effect on the price or value of its enhanced disclosure (ED) securities and therefore should be disclosed under ss. 674 or 675 of the Corporations Act.

Under s. 111AC of the Corporations Act, if any securities of a body are ED securities, the body is a disclosing entity for the purposes of that Act. Generally, ED securities are issued by a listed company that is subject to the listing rules of a prescribed financial market.

The Determination has effect for six months from its commencement. It is automatically repealed at the end of six months beginning on the day after it was made.

In a media release dated 23 September 2020, the Australian Treasurer stated:

"The heightened level of uncertainty around companies' future prospects as a result of COVID-19 exposes companies to the threat of opportunistic class actions for allegedly falling foul of their continuous disclosure obligations if their forecasts in the middle of a pandemic are found to be inaccurate. In response, companies may hold back from making forecasts of future earnings or other forward-looking estimates, limiting the amount of information available to investors during this period. Importantly, evidence to date shows that the temporary exemption has assisted companies to continue to update the market during this difficult and uncertain time. In fact, Treasury has identified that there has been an increase in the number of material announcements to the market during the period the relief has been in place, relative to the same period last year. So while this temporary measure has not detracted from information being provided to the market, it has made it harder to bring such actions against companies and officers during the coronavirus crisis and while allowing the market to continue to stay informed and function effectively".

1.10 IOSCO issues measures to reduce conflict of interests in debt capital raising

21 September 2020 - The Board of the International Organization of Securities Commissions (IOSCO) has published final guidance to help its members address potential conflicts of interest and associated conduct risks market intermediaries may face during the debt capital raising process. The guidance also seeks to address some specific concerns observed by certain regulators during the COVID-19 crisis that may affect the integrity of the capital raising process.

Conflicts of interest and associated conduct risks can weaken investor confidence and undermine debt capital markets as an effective vehicle for issuers to raise funding. To help regulators identify and address these risks, IOSCO has published the final report on Conflicts of interest and associated conduct risks during the debt capital raising process.

The report also explores the potential benefits and risks of Blockchain technology in addressing conflicts of interest in the debt capital raising process. The report describes the key stages of the debt raising process and identifies where the role of intermediaries might give rise to conflicts of interest. The guidance comprises nine measures that address potential issues when issuers are preparing to raise debt finance, including such things as the use of risk management transactions, the quality of information available to investors, and the allocations process.

The consultation report on the guidance comprised eight measures published in December 2019 prior to the start of the COVID 19 pandemic. The final report includes an additional ninth measure that addresses specific concerns that emerged from the crisis. It seeks to address the potentially problematic conduct of lenders that may opportunistically leverage their role during debt capital raising to pressure corporate clients into awarding them future mandates.

While the guidance focuses on traditional corporate bonds, it may prove useful to IOSCO members considering raising capital through other types of debt securities. The guidance is the second part of a two-stage project on conflicts of interest in capital raising. The first stage focused on the equity capital raising process with the final report Conflicts of interest and associated conduct risks during the equity capital raising process published in September 2018.

1.11 US: Audit committee reporting to shareholders in 2020

14 September 2020 - For the ninth consecutive year, the EY Center for Board Matters has reviewed voluntary proxy statement disclosures by Fortune 100 companies relating to audit committees, including their oversight of the audit.

These disclosures are an important tool for investors and other stakeholders to gain insight into the activities of audit committees, whose role in promoting high-quality and reliable financial reporting is widely acknowledged. The US SEC, for example, has affirmed that independent audit committees have proved to be one of the most effective financial reporting enhancements included in the *Sarbanes-Oxley Act*. The transparency provided by these disclosures can help strengthen investor confidence in financial reporting and US capital markets.

The report provides data on the types of audit committee-related disclosures that the largest public companies are providing on a voluntary basis, above what is required by US securities laws and regulations. It also includes some samples of the disclosures examined to illustrate the information being provided to investors.

This year's data demonstrates a continuity of voluntary disclosures across areas of continued interest for investors and other stakeholders. Beyond emerging disclosures around critical audit matters, the type and extent of audit committee-related disclosures remain largely unchanged since last year. The COVID-19 pandemic does not appear to have had a significant impact on the disclosures, although that may be due in part to the timing of many proxy filing deadlines, which fell before the full extent of the pandemic was felt.

While the year-over-year change in the percentage of companies providing these voluntary disclosures has changed only slightly, there has been a dramatic increase in disclosures in most categories since EY began examining these disclosures in 2012. For example:

- this year nearly 80% of companies disclosed that the audit committee is involved in selecting the lead audit partner. None of these companies made that disclosure in 2012; and
- nearly 90% of companies disclosed that the audit committee considers non-audit fees and services when assessing auditor independence, vs. just 19% in 2012.

Nearly two-thirds of companies stated that they consider the impact of changing auditors when assessing whether to retain the current external auditor, and 76% disclose the tenure of the current auditor. That's up from just 3% and 25%, respectively, in 2012.

- 64% of companies disclose factors used in the audit committee's assessment of the external auditor qualifications and work quality, which is four times the 15% that did so in 2012;

- this year, there was an increase in audit committees with two or more financial experts (up to 91%, compared with 70% in 2012). This could be indicative of the increasing complexity of risks that audit committees are dealing with, requiring more financial expertise;
- fifteen companies (21%) provided voluntary disclosures relating to the critical audit matters (CAMs) added to the auditor's report in the current year for the largest filers. As this is the first year that CAMs disclosures have been required, there is no previous data with which to compare. These disclosures generally noted that the audit committee reviewed and discussed with the external auditor CAMs that arose during the current period audit; and
- consistent with the trends of voluntary audit committee disclosures, companies continue to expand their description of audit committee oversight about the roles and responsibilities of the audit committee. This year, EY reviewed the key committee responsibility-related disclosures to assess if there were additional disclosures around additional risks/issues falling under the audit committee's purview beyond financial reporting, compliance and legal matters.

View report.

1.12 Proposed US stakeholder legislation

7 September 2020 - B Lab USA and Shareholder Commons have published a report titled From Shareholder Primacy to Stakeholder Capitalism - A Policy Agenda for Systems Change. The report recommends a new US Federal Act titled The Stakeholder Capitalism Act. Key parts of the proposed Act are:

- fiduciary duties for Institutional Investors: require investment fiduciaries to consider a broad array of beneficiary interests that extend beyond the financial return provided by individual companies;
- corporate fiduciary duties: require corporate fiduciaries (including directors) to consider the interests of stakeholders as well as shareholders;
- asset owner/manager disclosure: introduce a US federal disclosure regime that provides beneficiaries - including the owners of mutual funds and ETFs - and other members of the public with information as to how asset owners and managers are allocating capital, voting shares and otherwise engaging with companies so as to protect broad stakeholder interests;
- board leadership: require, for large companies, that the compensation (remuneration) committee be charged with ensuring that the company incorporates consideration of stakeholder concerns into its decision-making process, and that the company's compensation scheme for senior employees is reflective of stakeholder considerations; and
- company disclosure: expand current SEC disclosure requirements to address not just matters material to a company's financial performance, but also information relevant to systemic risk and the impact of the company on all of the interests of its shareholders and stakeholders.

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2. Recent ASIC Developments

2.1 Regulators urge Australian institutions to adhere to the ISDA IBOR Fallbacks Protocol and Supplement

13 October 2020 - Regulators and industry are taking further steps to transition away from London Interbank Offered Rate (LIBOR), which is expected to cease after the end of 2021. In particular, on Friday 9 October 2020 the International Swaps and Derivatives Association (ISDA) announced that it will launch the 2020 interbank offered rates (IBORs) Fallbacks Protocol and associated Supplement to the 2006 ISDA Definitions on 23 October 2020. These are needed to implement robust fall-back provisions for derivative contracts referencing key IBORs, including the LIBOR. The protocol and supplement are informed by extensive consultation with industry, including in Australia.

While the regulators welcome the progress of LIBOR transition in Australia to date, continued focus and effort are necessary. ASIC, with the support of APRA and the Reserve Bank of Australia (RBA), strongly urges Australian institutions to adhere to the ISDA Protocol and Supplement. The Financial Stability Board has also released a statement encouraging broad and timely adherence to the protocol.

Adherence is an important step towards the orderly transition of LIBOR-referenced derivatives contracts. It is critical to the mitigation of both individual entity risks and systemic risks associated with the discontinuation of LIBOR.

All financial and corporate institutions that use derivatives contracts referencing LIBOR are strongly encouraged to review and adhere to the protocol by its effective date of 25 January 2021.

2.2 Remake of two "sunsetting" class orders relating to credit

30 September 2020 - ASIC has remade ASIC Class Order [CO 10/381] relating to notification requirements for unlicensed carried over instrument (COI) lenders, which was due to end on 1 October 2020.

The new instrument, *ASIC Credit (Notice Requirements for Unlicensed Carried Over Instrument Lenders) Instrument 2020/834*, continues to impose an obligation on unlicensed COI lenders to notify ASIC when they become an unlicensed COI lender.

ASIC has also remade ASIC Class Order [10/1230] relating to credit disclosure obligations, which was due to end on 1 April 2021.

The new instrument, *ASIC Credit (Electronic Precontractual Disclosure) Instrument 2020/835*, continues relief allowing credit providers to give pre-contractual disclosure in the same manner as they give other disclosure documents under r. 28L of the National Consumer Credit Protection Regulations 2010 No. 44 (Cth).

The relief was remade following public consultation through Remaking ASIC class orders on unlicensed COI lenders and credit disclosure obligations (CP 331), issued in July 2020. ASIC did not receive any submissions in response to CP 331.

View:

- ASIC Credit (Notice Requirements for Unlicensed Carried Over Instrument Lenders) Instrument 2020/834;

- ASIC Credit (Electronic Precontractual Disclosure) Instrument 2020/835; and
- ASIC Credit (Repeal Instrument) 2020/836.

2.3 Restriction of certain retail offers of "stub equity" in takeovers to maintain investor protection

24 September 2020 - ASIC has modified the Corporations Act 2001 No. 50 (Cth) to prevent stub equity offers of scrip in a proprietary company being made to large numbers of retail target holders in takeover bids and schemes of arrangement.

The modification follows ASIC consultation on proposals to address concerns with offers of stub equity to retail investors in control transactions (19-127MR). ASIC's response to submissions received as part of this consultation process is contained in *Report 669 Response to submissions on CP 312 Stub equity in control transactions (REP 669)*.

"Stub equity" is sometimes offered as consideration under a takeover or scheme of arrangement. It typically consists of securities or interests in an unlisted bid or holding vehicle that provides offerees the option to retain continued economic exposure to the performance of the underlying business of an entity as an alternative to another form of consideration (such as cash) that does not provide the same exposure.

ASIC's proposals during consultation sought to restrict certain structures that would result in retail investors not being covered by the normal protections available under Australian law when participating in a public offer of securities. This can occur when shares in a proprietary, rather than public company are offered as consideration under a takeover bid or scheme of arrangement. It can also arise when scrip consideration is required to be held by a custodian.

ASIC decided not to proceed with one of the proposals in its consultation paper, which sought to restrict offers of stub equity in public companies that use mandatory custodial structures. However, ASIC has included anti-avoidance measures within the instrument to ensure that these types of public companies do not convert to proprietary companies after the takeover is completed.

View:

- Report 669 Response to submissions on CP 312 Stub equity in control transactions (REP 669);
- ASIC Corporations (Stub Equity in Control Transactions) Instrument 2020/734; and
- Consultation Paper 312 Stub equity in control transactions (CP 312).

2.4 Extension of COVID-19 relief for certain capital raisings and financial advice

23 September 2020 - ASIC has extended the temporary relief for capital raisings and financial advice due to the continuing uncertain impacts of COVID-19. ASIC has also extended the financial advice relief related to the COVID-19 early release of superannuation scheme in light of the extension of the scheme by the Government.

The capital raisings relief aims to assist listed entities affected by the COVID-19 pandemic to raise capital in a quicker and less costly way without undermining investor protection. It was originally announced on 31 March 2020 (20-075MR). The temporary relief enables certain 'low doc' offers (including rights offers, placements and share purchase plans) to be made to investors without a prospectus, even if they do not meet all the normal requirements.

The financial advice relief and the no-action position for superannuation trustees providing 'intra-fund advice' aims to assist industry in providing consumers with affordable and timely advice during the COVID-19 pandemic. These measures were announced on 14 April 2020 (20-085MR).

To extend relief, ASIC has registered the *ASIC Corporations (Amendment) Instrument 2020/862*, which means:

- the earlier amendment to the ASIC Corporations (Share and Interest Purchase Plans) Instrument 2019/547 will now be repealed on 1 January 2021 (instead of 2 October 2020);
- the ASIC Corporations (Trading Suspensions Relief) Instrument 2020/289 will now be repealed on 1 January 2021 (instead of 2 October 2020); and
- the ASIC Corporations (COVID-19 - Advice-related Relief) Instrument 2020/355 will now be repealed on 15 April 2021 (instead of 15 October 2020).

ASIC has also amended its temporary no-action position for expanded intra-fund advice on early release of superannuation relating to COVID-19 to extend it until 31 December 2020 to align with the extension of the COVID-19 early release of superannuation scheme.

ASIC will continue to monitor the appropriateness of these temporary relief measures in light of the impacts of COVID-19 on capital markets and on the demand for financial advice. If ASIC considers it appropriate to end the relief before the expiration dates or to further extend it, ASIC will give sufficient notice before any early repeal or extension is implemented.

View:

- ASIC Corporations (Amendment) Instrument 2020/862;
- Explanatory statement;
- Temporary no-action position for expanded intra-fund advice on early release of superannuation relating to COVID-19;
- ASIC Corporations (Amendment) Instru;ment 2020/565; and
- 20-135MR ASIC amends financial advice and capital raisings COVID-19 instruments of 12 June 2020.

Capital raisings

- 20-075MR Facilitating capital raisings during COVID-19 period of 31 March 2020;
- 20-097MR ASIC supports increase transparency in capital raisings of 23 April 2020;
- ASIC Corporations (Trading Suspensions Relief) Instrument 2020/289;
- ASIC Corporations (Share and Interest Purchase Plans) Instrument 2019/547;
- ASIC Corporations (Amendment) Instrument 2020/290; and
- REP 605 Allocations in equity raising transactions of 20 December 2018.

Financial advice

- 20-085MR ASIC grants relief to industry to provide affordable and timely financial advice during the COVID-19 pandemic of 14 April 2020;
- ASIC Corporations (COVID-19 - Advice-related Relief) Instrument 2020/355; and

- Information on COVID-19 related regulatory issues for the financial advice industry.

Superannuation

- Information on COVID-19 related regulatory issues for the superannuation industry.

2.5 ASIC report on conflicts of interest within debt capital raising process

22 September 2020 - ASIC has issued *Report 668 Allocations in debt capital market transactions* (REP 668). REP 668 outlines findings from ASIC's surveillance of market practices in debt capital market (DCM) transactions and sets out better practice guidelines, including ASIC's expectations that Australian Financial Service licensees:

- identify and manage potential conflicts of interest when making allocation recommendations;
- have effective policies and procedures for identifying and managing confidential and market-sensitive information;
- have processes to ensure that information provided to issuers and investors (including updates) is accurate and not misleading or deceptive; and
- have active and effective supervision and monitoring for DCM transactions.

ASIC's report follows the 21 September 2020 release of the Final report on Conflicts of interest and associated conduct risks during the debt capital raising process (IOSCO Report) by the Board of the IOSCO. The IOSCO Report helps regulators to identify and address conflicts of interest and associated conduct risks from the role of intermediaries in debt capital raisings, which can impact market integrity and investor outcomes. The better practices outlined in REP 668 are consistent with the measures in the IOSCO Report.

REP 668 builds on ASIC's previous work on improving conduct in capital raising transactions, including the better practices in Report 605 Allocations in equity raising transactions and guidance in Regulatory Guide 264 Sell-side research.

View Report 668 Allocations in debt capital market transactions.

2.6 ASIC tells fund managers to be "true to label"

22 September 2020 - A recent ASIC surveillance has found that fund managers must do more to ensure their products are "true to label" - that the product name aligns with the underlying assets.

ASIC undertook a targeted surveillance of 37 managed funds operated by 20 responsible entities that collectively hold approximately $21 billion in assets. This followed ASIC having concerns with product labelling practices (refer to 20-107MR). These funds were identified after data analysis and an initial assessment of the product names and labelling practices of more than 350 funds in the cash, fixed-income, mortgage and property sectors across funds collectively holding more than $65 billion in assets.

ASIC recognises that during times of market volatility, consumers may be looking for alternate investment options offering regular or higher returns, and financial product labels are used as a guide for consumers about what they are investing in.

ASIC examined the appropriateness of the product labels used by the 37 managed funds and assessed whether the funds were described and promoted in a manner that reflects the underlying assets in terms of risk and liquidity.

Confusing or inappropriate "cash" product labels:

- while most of the funds reviewed in the fixed-income, mortgage and property sectors were appropriately labelled, ASIC identified concerns with the labelling of some cash funds;
- out of the 22 managed funds, with over $15 billion in funds under management, that used the term "cash" in their labelling, 14 funds had confusing or inappropriate labels;
- some funds that were labelled as "cash funds" had asset holdings more akin to a bond or diversified fund, which have significantly higher risk and less liquidity compared to a traditional cash fund. This was especially prominent in funds that use words such as "cash enhanced" and "cash plus" in their labelling; and
- on average, funds labelled as "cash plus" and "cash enhanced" had more than 50% and 70% of their respective assets invested in assets other than cash or cash equivalents such as fixed-income securities and mortgages.

Mismatch between redemption features offered and the liquidity of underlying assets:

- generally, the redemption features offered by the funds reviewed in the fixed-income and property sectors were satisfactorily matched to the liquidity of the underlying assets; and
- in a small number of funds, there was a significant mismatch between redemption features and asset liquidity, i.e. the liquidity of the underlying assets did not support the short redemption terms offered to consumers.

ASIC's expectations - "cash" labelling

If the underlying liquidity of a fund is inconsistent with its redemption promises, investors may not be able to redeem their investments when they anticipated they would be able to do so. In periods of market volatility, especially during COVID-19, this exacerbates the liquidity risks faced by the funds and ultimately investors.

Where there is a mismatch between a fund's redemption terms and the underlying assets, responsible entities need to take proactive steps to revise the redemption terms or move to less frequent redemptions if appropriate.

ASIC's corrective action

Following the review, ASIC sought corrective action from 13 responsible entities where significant concerns were identified. As a result, to date:

- seven responsible entities have voluntarily changed or proposed to change the names of their funds (nine in total) to reflect the product composition;
- one responsible entity is proposing to change the asset allocation of the fund to reflect its name;
- three responsible entities have undertaken or committed to undertake a review of their funds; and

- one responsible entity withdrew misleading promotional materials on their website and subsequently wound up its fund.

ASIC's engagement with some responsible entities is continuing. ASIC will continue to monitor the outcomes and consider appropriate regulatory action, including enforcement action where necessary.

Responsible entities should consult ASIC's Regulatory Guide 168 Product Disclosure Statements (and other disclosure obligations) for guidance on labelling and disclosure requirements.

Investors who have exited a managed fund but believe they have suffered financial loss as result of inappropriate or confusing labelling, should contact their fund's responsible entity in the first instance. They can also seek recourse by making a complaint to Australian Financial Complaints Authority (AFCA), which offers fair, free and independent dispute resolution.

2.7 ASIC enforcement update January to June 2020

22 September 2020 - ASIC has released its enforcement update report for the period 1 January to 30 June 2020. The report outlines key actions taken over the past six months to enforce the law and support ASIC's enforcement objectives.

To address the impact of the COVID-19 pandemic on the Australian financial system, ASIC has developed a set of pandemic-related enforcement priorities to guide the organisation's response to misconduct associated with the pandemic. The priorities are set out in the enforcement update report and ASIC's Office of Enforcement has a number of investigations into pandemic-related misconduct.

View Report 666 ASIC enforcement update January to June 2020.

3. Recent ASX Developments

3.1 ASIC and RBA announce expectations for CHESS replacement

1 October 2020 - ASIC and the RBA (the regulators) have outlined their expectations of the Australian Securities Exchange (ASX) as it replaces the Clearing House Electronic Sub-register System (CHESS). This follows the release of the RBA's 2020 Assessment of ASX Clearing and Settlement Facilities.

The regulators expect ASX to replace CHESS as soon as this can be safely achieved by ASX and users of CHESS. CHESS is a critical clearing and settlement (CS) system for the Australian cash equity market. It contributes to investor confidence, the reduction of systemic risk, and the performance and stability of the Australian financial system. The importance of replacing CHESS in a safe and timely manner was particularly highlighted in recent record trading volumes and the associated CHESS processing delays observed in March (refer to 20-062MR). In implementing the replacement, ASX should take into account CHESS user feedback from its recent consultation on a revised implementation timeline. ASX is expected to demonstrate the readiness of the CHESS replacement system and will be required to provide supporting independent assurances to the regulators before migrating to the new system.

ASIC and the RBA, as co-regulators of licensed CS facilities, continue to closely monitor ASX's compliance with its CS facility licence obligations. ASX Clear Pty Limited and ASX Settlement Pty Limited, as licensed CS facilities, are required to ensure that their facilities' services are provided in a fair and effective way, and that they have sufficient resources (including financial, human, and technological) to operate their facilities. CS facilities are also subject to the RBA's Financial Stability Standards (FSS).

ASIC and the RBA, with the broader Council of Financial Regulators (CFR) and the Australian Competition and Consumer Commission are also closely supervising ASX's conduct in the CHESS replacement program of change in accordance with the CFR's Regulatory Expectations for Conduct in Operating Cash Equities Clearing and Settlement. The Regulatory Expectations seek to ensure that ASX remains responsive to users' evolving needs and provides access to its monopoly cash equity CS services on a transparent and non-discriminatory basis with terms and conditions, including pricing, that are fair and reasonable.

The regulators' supervision and engagement with ASX is focused on ASX's governance of the change program, its engagement with stakeholders, the functional and technical aspects of the replacement system, and its management of the risks associated with the migration to the new system.

In order to demonstrate its readiness to migrate to the new system, ASX is expected to provide independent assurances to the regulators. Seeking independent assurances is also consistent with an enterprise risk management three-lines-of-defence model. At a minimum, the new system must meet requirements which CHESS meets today for system availability, resilience, recoverability, performance and security. ASX has announced non-functional business requirements for the replacement system that will exceed these minimum requirements. ASX will need to provide assurances to demonstrate that these non-functional requirements have been met.

ASX is also expected to achieve a significant uplift in intraday trade processing capacity and end-of-day processing performance in the new system.

3.2 RBA assessment of ASX clearing and settlement facilities

1 October 2020 - The RBA has released the October 2020 Assessment of the ASX Clearing and Settlement Facilities (the Assessment). The Assessment concludes that ASX's CS facilities "observed" or "broadly observed" all relevant requirements under the RBA's FSS as at 30 June 2020, with the exception of the standard relating to margin, which was rated as "partly observed" in ASX Clear (Futures) (ASXCLF), and the standard relating to operational risk, which was rated as "partly observed" in ASX Clear and ASX Settlement.

The RBA is responsible for the supervision of Australian-licensed CS facilities focusing on the reduction of systemic risk. Systemically important CS facilities are assessed on a regular basis against the FSS set by the RBA.

On balance, the RBA has concluded that the facilities have conducted their affairs in a way that causes or promotes overall stability in the Australian financial system. However, ASX will need to place a high priority on addressing recommendations related to margin at ASXCLF and operational risk at ASX Clear and ASX Settlement, including via the replacement of CHESS.

The Assessment also describes progress made by the ASX CS facilities in addressing recommendations from the 2019 Assessment.

3.3 Public consultation: Default management of exchange traded derivatives

On 30 September 2020, ASX released a consultation paper outlining proposed changes to the ASXCLF Operating Rules and Procedures that seek to introduce a framework for default management auctions of exchange traded derivatives and extend the existing default indemnity.

ASX is proposing to introduce a clear and transparent framework for the auctioning of exchange traded derivatives by ASXCLF in the event that a future clearing participant defaults. ASX is also proposing to align the default management powers available to both ASX Clear and ASXCLF through the extension of the existing ASXCLF indemnity.

The consultation paper is available on the ASX website.

3.4 Response to consultation: CHESS Replacement Tranche 2 rule amendments

On 24 September 2020, ASX released its response to consultation feedback regarding the CHESS Replacement Tranche 2 Rule Amendments.

The response:

- summarises the feedback ASX has received;
- describes ASX's response to the feedback, providing further clarification where requested; and
- outlines the changes ASX will be making to the draft rules in response to the feedback received and provides the text of the draft rules as updated to include these changes.

The response can be found on the ASX website.

3.5 ASX revises temporary emergency capital raising measures

On 15 September 2020, ASX announced that it is revising the temporary emergency capital raising measures that were introduced in March to help listed entities affected by the COVID-19 pandemic.

ASX considers it prudent and timely to revise the settings given the stabilisation in market conditions. From 16 September 2020, any entity wishing to rely on the measures must satisfy ASX that it is raising capital predominantly for the purpose of addressing the existing or potential future financial effect on the entity from the COVID-19 health crisis, and/or its economic impact.

The media release is available on the ASX website.

3.6 Reports

On 7 October 2020, ASX released the ASX Monthly Activity Report for September 2020.

4. Recent Takeovers Panel Developments

4.1 Remaking of procedural rules - Panel releases consultation draft

2 October 2020 - The Takeovers Panel has conducted a review of its Procedural Rules and has published a draft set of remade rules on its website for public consultation.

The Panel's current Procedural Rules are due to sunset on 1 April 2021. Given the Panel's preliminary view that the existing Procedural Rules are operating effectively and efficiently, the Panel proposes to remake the Procedural Rules in a new instrument prior to the sunset date without significant changes.

The new Procedural Rules simplify the existing Procedural Rules by removing the "guidance" (which currently appears as notes under the existing Procedural Rules) from the "rules" themselves. The "guidance" has been incorporated into a separate Procedural Guidelines document which has been prepared to assist market participants, parties and advisers understand and apply the new Procedural Rules.

While the Panel proposes a change to the way in which the "rules" and "guidance" is presented, it is the Panel's intention that the procedure to be followed in Panel proceedings will remain fundamentally the same following the implementation of the new Procedural Rules.

View Consultation Paper - Remaking of Procedural Rules.

4.2 Keybridge Capital Limited 14 - Panel declines to conduct proceedings

23 September 2020 - The Takeovers Panel has declined to conduct proceedings on an application dated 11 September 2020 from WAM Active Limited in relation to the affairs of Keybridge Capital Limited.

WAM Active submitted (among other things) that Keybridge and Aurora had an understanding or were acting in concert in relation to Keybridge to concentrate ownership of ordinary shares in Keybridge in entities associated with Keybridge board members and Aurora for the purpose of "stymieing" WAM Active's bid, "ultimately with the shared goal of ensuring that WAM Active and its associates are unable to obtain sufficient voting shares to remove the current Keybridge board" (see TP20/55).

The Panel considered that (among other things) there was not sufficient probative material to justify making further enquiries as to whether Keybridge and Aurora were associated.

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

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

5.1 Sharing the pain: How did boards adjust CEO pay in response to COVID-19?

Scrutiny of chief executive officer (CEO) pay increases during times of economic stress, when it is not clear how much pay CEOs should receive when corporate profitability suffers due to an unforeseen decline in the operating environment. On the one hand, the board might want to preserve incentives, recognising that a decrease in pay punishes executives through no fault on their own. On the other hand, maintaining or supplementing CEO pay while a company is laying off workers looks bad.

In this paper, the authors examine the CEO compensation decisions of large publicly traded companies in the US following the spread of COVID-19 to see how many elected to modify CEO pay and how many left it unchanged. The authors examine the characteristics of the companies that altered pay, and consider whether those that altered pay did so to "share the pain" or insulate CEOs from lost value.

They ask:

- How much economic pain did the typical CEO really suffer?;
- Do outcomes signal the success or failure of compensation program design?;
- Should CEOs receive supplemental awards in the future to compensate for lost value?;
- Do asymmetries arise if CEOs are sheltered from reversals but do not give back excess value in positive economic environments?; and
- What do corporate actions tell us about our ability to accurately measure ESG?

Sharing the Pain: How Did Boards Adjust CEO Pay in Response to COVID-19?

5.2 The effectiveness of disclosure law enforcement in Australia

This article examines the empirical incidence of the private and public enforcement of disclosure laws in Australia. Disclosure laws aim to ensure the reduction of information asymmetries and the accuracy of share prices, but their success is predicated on enforcement. In order to assess the enforcement landscape, this article presents two new datasets comprising both private class actions (including whether litigation funding is in place) and public enforcement for further examination. In light of these findings, this article addresses the question of whether the Australian system of enforcement is effective, by reference to whether the enforcement actions compensate, deter, and signal. Overall, the empirical analysis confirms the signalling function of enforcement and shows that there is likely to be a reasonable degree of deterrence where directors are targeted, however, the compensation rationale is not met. This results in a moderately effective enforcement framework with notable room for improvement across both modalities of enforcement.

The Effectiveness of Disclosure Law Enforcement in Australia

5.3 Purpose-based governance: A new paradigm

The permissibility of corporations pursuing purposes other than profit has been the subject of debate for a number of years. This debate has intensified recently with proposals to allow or mandate the adoption of purposes by corporations. At the same time, purpose is central to governance in the charitable sphere. This article proposes a model of "purpose-based governance", which offers significant potential advantages in both the charitable and for-profit spheres, as well as forming the basis of a unifying governance paradigm.

Purpose-Based Governance: A New Paradigm

5.4 In whose best interests? Regulating financial advisers, the Royal Commission and the dilemma of reform

Following the Future of Financial Advice reforms, the "suitability" and "appropriateness" focus for financial advice has been relocated and supplemented by a "best interests" focus in s. 961B of the Corporations Act 2001 No. 50 (Cth). Yet, as the Australian Government's *Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* has pointed out, structural issues may often work against best interests being paramount. Further, moves to make the statutory obligation replicate a fiduciary obligation have been resisted in the consultative process that developed s. 961B and related obligation sections and any replication is far from clear. Another key issue is the extent to which aspects of the best interests duty are satisfied by a 'tick a box' approach. This aspect of s. 961B is said to provide 'safe harbour' for advisers, yet has been criticised by the Royal Commission as more procedural rather than substantive. However, removing the safe harbour altogether may create more problems than it solves. We argue that a catch-all provision in s. 961B(2)(g) preserves substantive flexibility, and caution against any reform that leaves no procedural guidance for financial advisers to anchor their behaviour in fulfilling the best interests duty.

In Whose Best Interests? Regulating Financial Advisers, the Royal Commission and the Dilemma of Reform

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5.5 Capital raising by companies during the COVID-19 crisis: An analysis of recent ASX reforms

The effects of the COVID-19 crisis have driven many listed Australian companies to raise emergency capital. These share issues have been facilitated by a relaxation of the rules applying to capital raising by the ASX, a move supported by ASIC. The reforms to the rules draw on the experience of the financial crisis in 2008-2009. They are designed to assist companies adversely affected by the COVID-19 crisis to raise capital to survive the crisis. The nature of the reforms and the capital raisings to which they relate have been the subject of competing concerns. In particular, the enhanced disclosure requirements that have accompanied the relaxation of the capital raising rules have been criticised by some as unwarranted and by others as insufficient. In this research note, the authors provide information on the number of capital raisings since the beginning of COVID-19 and evaluate the competing arguments regarding the recent capital raising reforms.

Capital Raising by Companies During the COVID-19 Crisis: An Analysis of Recent ASX Reforms

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5.6 An analysis of board of director appraisal disclosures in Australia and the US

Appraisals of boards of directors are now well established and viewed as important contributors to the effectiveness of boards. Because board appraisal practices vary between companies and the benefits of an appraisal will only be obtained where an appropriate practice is followed, there is significant interest in the board appraisal practices adopted by companies. The authors first outline the benefits and challenges of board appraisals and identify the key features of an effective board appraisal. They then present the results of their study of how board appraisals are conducted in Australia in relation to large and small listed companies and compare the findings with the board appraisal practices of US Fortune 100 companies.

The results of the study show that the largest Australian listed companies outperform smaller listed companies on nearly all measures relating to the quality of board appraisals, including:

- the breadth of subjects evaluated;
- how often the appraisal is conducted;
- how often the appraisal is externally facilitated;
- the breadth of techniques used to gather data when conducting the appraisal; and
- the level of detail in the disclosure of the results of the appraisal.

No stark differences emerge when comparing both groups of Australian companies with the largest US companies, with the exception that the largest Australian companies performed significantly better than the US companies when it came to the frequency of externally facilitated appraisals.

An Analysis of Board of Director Appraisal Disclosures in Australia and the United States

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5.7 The geography of bankruptcy in Australia

This study analyses a unique data set to explore geographic variations in bankruptcy across Australia, drawing upon US research that points to striking differences between urban and rural bankruptcies. The US research finds that rural debtors enter bankruptcy in much more severe financial distress than their urban counterparts. The present study draws upon data obtained from the Australian Financial Security Authority, as well as data gathered by the Australian Bureau of Statistics.

It finds that, compared with debtors in regional areas, debtors in major cities earn higher incomes, are more likely to be employed and more likely to cite the "excessive use of credit", rather than unemployment, as the cause of their financial problems. In most respects, however, it finds that differences between Australian bankruptcies in urban and non-urban locations are neither consistent nor pronounced. It concludes that broad generalisations about financial hardship in regional areas cannot do justice to the complex geography of bankruptcy in Australia. In this sense, the study poses a contrast to the US research, which identifies stark differences between urban and rural debtors. It offers a nuanced account, one that links bankruptcy rates to localised factors such as housing prices and the impact of specific industries, such as mining.

The Geography of Bankruptcy in Australia

5.8 Insolvency law reform in Australia and Singapore: Directors' liability for insolvent trading and wrongful trading

This article compares reforms to directors' liability for insolvent trading in Singapore and in Australia. The authors analyse the law in these two countries because they are important Asia-Pacific trading partners and their laws were originally largely the same - Singapore's law on insolvent trading reflected the law in Australia from the 1960s. However, the law in the two countries has now diverged substantially. The comparison of these two countries therefore represents an interesting case study in how countries differ in their approaches to balancing the competing interests evident in laws that impose personal liability on company directors for insolvent trading. Reform of the prohibition against insolvent trading was a focus of Australia's insolvency law reforms in 2017 which led to the introduction of a safe harbour for directors from liability. Singapore's omnibus insolvency law reforms of 2018-19 include amendments to update Singapore's fraudulent and insolvent trading provisions by introducing a concept of "wrongful trading".

The article finds that there are some areas of convergence between these two jurisdictions when it comes to debates about such provisions, but concludes that the different contemporary legislative histories in Australia and Singapore have affected their approaches to reform. Reformers in both jurisdictions have attempted to find an appropriate balance between protecting creditors, discouraging director misconduct and encouraging entrepreneurship and innovation; however, this comparison suggests that the weight that reformers place on creditor protection compared to the concern that excessive personal liability can make directors unduly risk-averse is influenced by their existing legislative framework and experience of those laws. Although Australia has shifted away from a strict focus on creditor protection, to give directors more opportunities to engage in restructuring, Singapore's amendments may provide a more creditor-friendly regime.

Insolvency Law Reform in Australia and Singapore: Directors' Liability for Insolvent Trading and Wrongful Trading

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5.9 "Contrary to the spirit of the age": Imprisonment for debt in colonial Victoria, 1857-90

The reintroduction in 1857 of imprisonment for debt in colonial Victoria flew in the face of international momentum for its abolition. In its criminalisation of debt and poverty, the *Fellows Act 1857 (Vic)* also defied the rapid advancement of democratic and egalitarian principles in the fledgling colony. Frequently referred to as "gross class legislation", the law was used unabashedly to target poor small debtors, leaving "mercantile men" with significant debt untroubled by the prospect of a debtors' gaol. Despite consistent and broad opposition to the *Fellows Act*, its advocates resisted repeated attempts to abolish or meaningfully amend it. It is argued here that the law, and its survival against the "spirit of the age", can be understood as part of a broader story of conservative resistance to the democratic innovations that threatened the power of the Victorian mercantilist establishment.

"Contrary to the Spirit of the Age": Imprisonment for Debt in Colonial Victoria, 1857-90

6. Recent Corporate Law Decisions

6.1 Application by deed administrators to transfer shares under s. 444GA of the Corporations Act 2001 No. 50 (Cth)

(By Joshua McKersey, MinterEllison)

In the matter of Gulf Energy Ltd (subject to deed of company arrangement) [2020] NSWSC 1323 (29 September 2020) Supreme Court of New South Wales, Black J

(a) Summary

The plaintiffs sought leave to transfer all of the shares in a company subject to a deed of company arrangement to the proponent of the deed. Black J granted the relief sought by the plaintiffs, holding that allowing the transfer of shares did not cause unfair prejudice to the defendant shareholders because Gulf Energy's shares had no residual value.

(b) Facts

(i) Background

Gulf Energy Ltd (Gulf Energy), an unlisted public company, was placed into administration on 21 October 2019. The company's only material asset was a Petroleum Exploration Permit authorising exploration of an area in the Gulf of Carpentaria for oil and gas. It was apparent that Gulf Energy had incurred significant liabilities, had not commenced commercial drilling, did not receive a trading income, and had operated for several years at a loss. It was also apparent that Gulf Energy's capacity to raise additional capital had been impaired by significant declines in the price of crude oil.

Following the first meeting of creditors, several parties made proposals for a deed of company arrangement. The plaintiffs initially recommended that creditors accept a proposal from Drake Management LLC (Drake DOCA), which creditors accepted at the second meeting of creditors on 22 January 2020. The Drake DOCA was executed on 13 February 2020 and the plaintiffs were appointed as deed administrators. Difficulties arose under the Drake DOCA and, at a further meeting of creditors, creditors approved the Drake DOCA being wholly amended in the form of an earlier proposal put forward by Petroventures Pty Ltd (Petroventures).

The varied deed of company arrangement (Petroventures DOCA) was executed on 7 May 2020 and the plaintiffs were again appointed as deed administrators. A provision of the Petroventures DOCA required the plaintiffs to make an application under s. 444GA of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) for the transfer of all shares in Gulf Energy to Petroventures.

(ii) Proceedings

The plaintiff administrators applied under ss. 444GA and 447A of the Corporations Act for leave to transfer all of the shares of Gulf Energy to Petroventures, in its capacity as trustee of the New Horizons Trust or its nominee, pursuant to the Petroventures DOCA, and for ancillary orders.

The defendant shareholders, who collectively held about 1.78% of Gulf Energy's shares, opposed the plaintiffs' application on several grounds, including by reference to an alternative deed of company arrangement proposed by the defendants that provided for all shares in Gulf Energy to be transferred to an entity controlled by one or more of the defendants.

(c) Decision

Black J granted the plaintiffs' application and made the orders sought by the plaintiffs.

His Honour accepted the legal principles relied upon by the plaintiffs. The plaintiffs contended that, relevantly, the mere transfer of shares without compensation does not establish unfair prejudice under s. 444GA per se and, if the shares have no value and there would be no distribution in the event of a liquidation - liquidation being the only realistic alternative - there is no unfair prejudice under s. 444GA.

The evidence before the Court indicated that Gulf Energy's shareholders were unlikely to recover any money in a liquidation. Indeed, his Honour observed that "[i]t is readily apparent that the value of the Permit and Gulf Energy's assets . is significantly less than its creditors' claims" (at [27]). On this basis, his Honour was satisfied that Gulf Energy's shares had no value.

Accordingly, his Honour held that, subject to consideration of the defendants' arguments, the transfer of the shares in Gulf Energy involved no unfair prejudice to its shareholders, and the Court would grant leave under s. 444GA.

His Honour dismissed each of the defendants' arguments. In essence, these arguments foreshadowed alternate proposals or further court applications, but his Honour considered that none of these warranted a different conclusion. In dismissing the defendants' arguments, his Honour observed that:

- "the mere possibility that the defendants might bring an application under s. 90-21 of the Insolvency Practice Schedule (Corporations) directing that a meeting of creditors be convened to vote on a resolution, under s. 445A of the Corporations Act, that an alternate proposal be adopted did not alter the result";
- "in any case, it was unlikely that the Court would grant such an application since the creditors approved the Petroventures DOCA and did not appear in support of the defendants in this case";
- "s. 445A did not contemplate a variation that excluded the deed proponent from the benefit contemplated by its entry into the deed, after it had paid an amount into the deed fund and, if it did, that such a variation might be set aside under ss. 445B or 447A of the Corporations Act"; and
- "if the defendants had applied for orders under ss. 445D(1)(f), (g) and 447A of the Corporations Act, it was doubtful that orders under those sections would have been made".

6.2 Application to set aside a statutory demand because of a genuine dispute

(By Shane Montgomery and Scott Sharry, Clayton Utz)

Re The Knowledge Warehouse Pty Ltd [2020] VSC 617 (25 September 2020) Supreme Court of Victoria, Randall AsJ

(a) Summary

The Victorian Supreme Court has reiterated the standard necessary to set aside a statutory demand on the grounds that there is a genuine dispute about the existence of a debt, whilst distinguishing the extent to which companies, compared to trustee companies, may informally make resolutions and determinations.

(b) Facts

The plaintiff trustee, The Knowledge Warehouse Pty Ltd, conducted its business as trustee for The Knowledge Warehouse Unit Trust (TKW Trust).

The defendant, Mr Malcolm Slinger, was both a former director of the plaintiff and also held 19 units in the TKW Trust as trustee of the Cadre Family Trust No. 2 (Slinger's Trust). The TKW Trust Deed (Trust Deed) materially provided that:

- Clause 10.1: the Trustee was entitled to make determinations regarding what monies received constituted income, in order to minimise income and capital gains tax liabilities. If, however, the Trustee did not make such a determination, the "net income" for that year would be taken as the income of the Trust Fund for the purpose of the Deed;
- Clause 10.3: the remaining income of the trust fund for that financial year was to be distributed to the unit holders of the Trust, in proportion to the number of units owned; and
- Clause 10.4: the Trustee could determine that a part of the distributed income (not exceeding 50%) could be retained as "Retained Moneys", and in certain circumstances only payable upon a Unit Holder giving at least six months' written notice requiring payment.

Prior to his retirement, Mr Slinger was the chief financial officer of the plaintiff. Under Mr Slinger's instructions, draft financial statements were prepared for the year ended 30 June 2019 which provided that the total unpaid trust distributions to the Slinger's Trust was $684,670.

On 12 February 2020, Mr Slinger served a statutory demand on the plaintiff seeking payment of $684,674.00 in respect of "unpaid trust distributions" to the Slinger's Trust, in accordance with cl. 10.3 of the Trust Deed. This figure was incorrect however, a subsequent and final financial statement was prepared, reflecting a revised total unpaid distribution of $543,988, consisting of the following components:

- Balance at beginning of year - 626,726
- Share of profit - 190,662
- Drawings - (273,400)
- Total - 532, 988

Mr Slinger, for the purpose of this matter, accepted the revised total. The plaintiff, however, alleged that a genuine dispute existed as it denied that any amount was due and payable, arguing:

- the total unpaid trust distributions consisted of multiple components, including loans and introduced capital, and not all of which formed part of the TKW's Trust's net income;
- though it conceded that the $190,662 consisting of the "Share of Profit" was appropriated for the defendants' benefit, this was Retained Moneys and therefore not payable as six months written notice had not been received; and
- the figures contained in the Financial Statements, although prepared by the plaintiff, were not admissions that those amounts were actually due and payable.

The case ultimately, however, turned on the classification of the components of the unpaid trust distributions, and whether any declaration or resolution (for the purposes of cll. 10.1 and 10.3) had been made.

(c) Decision

His Honour firstly confirmed the necessary threshold for the plaintiff to succeed. A statutory demand may be set aside pursuant to s. 459G of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act), if there is a genuine dispute between the company and the respondent about the existence or amount of a debt to which the demand relates (s. 459H). His Honour noted the relatively low bar, which requires only that the dispute be genuine, bona fide and truly exist in fact, as opposed to "spurious, hypothetical, illusory or misconceived".

In determining whether a genuine dispute existed, his Honour first considered s. 1305 of the Corporations Act, which relevantly provides that a book kept by a body corporate is admissible in evidence in any proceeding and is prima facie evidence of any matter stated or recorded in the book.

Citing Sloss J's decision in *Shot One Pty Ltd (in liq) v Day* [2017] VSC 741, his Honour acknowledged that s. 1305 does not establish a presumption that company accounts are prima facie true, correct and accurate; they are only prima facie evidence, which may be rebutted or outweighed by other evidence, of any matter stated or recorded in them. On balance, his Honour accepted that the final financial statement was prima facie evidence that:

- the total unpaid trust distribution was $543,988; and
- of that amount, $190,662 consisted of the defendants' share of profit.

His Honour next considered whether any determination had been made in respect of what the income of the TKW Trust was, and how that income was to be distributed, for the purpose of cll. 10.1 and 10.3. If no determinations had been made then by default the "net income" of the Trust Fund would constitute income for the purposes of the Trust Deed. His Honour considered the following principles:

- the determination of whether a 'genuine dispute' exists between the parties is an interlocutory matter, and therefore the court may consider hearsay and opinion evidence;
- in the case of family run, or tightly held companies where directors have close personal relationships, inferences can be made in respect of concurrences, and the necessary corporate decision-making, between directors where there are otherwise irregularities in the company's records: *Swiss Screens (Australia) Pty Ltd v Burgess* (1987) 11 ACLR 756 at 758;
- if it can be shown that all shareholders who have a right to attend and vote at a general meeting of the company assent to some matter which a general meeting of the company could carry into effect, that assent is as binding as a resolution in a general meeting would be: *Re Duomatic Ltd* [1969] 2 Ch 365 at 373; and
- this is however distinguishable in the case of trustee companies with fiduciary duties, particularly in circumstances such as this where a formal determination was required under the Trust Deed. Noting the trustee company's fiduciary duties, and the requirement that it comply with the terms of the Trust Deed, his Honour suggested that any informal determinations purportedly made under the trust may likely be invalid.

His Honour ultimately found that the plaintiff could not point to any evidence that there was consensus between directors as to the treatment of income for the year ended 30 June 2019. In the absence of any determination or resolution, the net income constituted "income" for the purposes of cl. 10.3.

His Honour, however, partially accepted the plaintiff's argument that it was not entirely obvious what components of the Unpaid Trust Distributions (totalling $543,988) constituted income that was due and payable at the time. His Honour accepted that the plaintiff's position was "at least arguable" and warranted further investigation, an exception to this being the "Share of Profit" component (of $190,662) which his Honour found was the substantiated amount of the claim as it was clearly due and payable at the time the statutory demand was issued. His Honour therefore ordered that the demand be rewritten and the amount of the demand be $190,662.

6.3 Secured creditor subrogated to the rights of employee creditors

(By Steph Griffin, Ashurst)

Blakeley, in the matter of Akron Roads Pty Ltd (in liq) [2020] FCA 1378 (24 September 2020) Federal Court of Australia, Anderson J

(a) Summary

This case concerned an application made by the liquidators of Akron Roads Pty Ltd (In Liquidation) (Akron) seeking directions that they were justified in regarding the secured creditor, Australia and New Zealand Banking Group Limited (ANZ), as subrogated to the priority rights of the employee creditors in respect of priority debts under s. 556 of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) paid to employee creditors, with ANZ's consent, from the proceeds of realisation of secured assets.

The application went unchallenged and Anderson J made the declaration and orders sought by the liquidators.

In his reasoning, Anderson J applied Finkelstein J's obiter dicta in *Cook (Liquidator), in the matter of Italiano Family Fruit Company Pty Ltd (in liq) v Italiano Family Fruit Company Pty Ltd (in liq)* [2010] FCA 1355 (*Cook*) and its subsequent application in *Carter, in the matter of Damilock Pty Ltd (in liquidation)* [2012] FCA 1445 (*Carter*). The *Cook* and *Carter* decisions provide a basis for an equitable right of subrogation arising in Akron's circumstances, where the secured creditor consents to the relevant payment and there is no breach of trust in making the payment prior to determining whether sufficient free assets would be realised to make the payment.

(b) Facts

Mr Blakeley and others were appointed as administrators of Akron on 1 February 2010, and later as liquidators when the creditors resolved to wind up Akron on 9 March 2019. At this time, Akron owed debts in relation to its employee creditors of $3,113,047.

During the course of the administration and liquidation of Akron, the liquidators realised assets subject to ANZ's fixed charges and distributed the recovered funds to ANZ. Akron remained indebted to ANZ in the amount of $8.497 million. The liquidators also realised assets subject to ANZ's floating charge and recovered funds in relation to unfair preference proceedings and a trading while insolvent claim.

As at 15 April 2011, the liquidators held net funds of approximately $1.5m, the majority of those funds comprised from the realisation of assets subject to ANZ's floating charge.

On 15 April 2011, Mr Blakeley wrote to ANZ seeking ANZ's consent to make an interim distribution to priority employee creditors using the proceeds of ANZ's floating charge funds in accordance with s. 561 of the Corporations Act. On 16 May 2011, ANZ consented to the liquidators' proposal, reserving its right to seek to be subrogated to the rights of priority creditors.

On 19 December 2011 and 7 November 2012 the liquidators paid, from the proceeds of the realisation of assets subject to ANZ's floating charge, certain priority debts in relation to Akron's employee creditors totalling $1,455,085. These debts included superannuation contributions, wages and salaries, annual leave and long service leave payments.

As a result of further realisations of assets subject to ANZ's floating charge, the liquidators held an additional $842,851. The liquidators anticipated having an additional $1,948,719 for distribution, derived from settlements of unfair preference proceedings and the trading while insolvent claim.

The liquidators intended to pay the proceeds of realisation of assets subject to ANZ's floating charge to ANZ in the amount of $1,455,085, reducing Akron's indebtedness to ANZ to $7.654m.

Between 9 June 2011 and 9 September 2020, the liquidators made the creditors aware of an intention to make the application. Neither the liquidators nor the court received any objections to the orders or the subrogation of ANZ to the priority rights of the employee creditors.

(c) Decision

Anderson J declared the liquidators were justified in regarding ANZ as subrogated to the rights of employee creditors in respect of priority debts that were paid by the liquidators to the employee creditors from the proceeds of ANZ's floating charge in the amount of $1,455,085.

Anderson J ordered:

- "the amount of $1,455,085 (in addition to any proceeds of assets subject to ANZ's floating charge) be paid to ANZ"; and
- "the costs of the Plaintiffs of the application be costs in the liquidation of Akron Roads Pty Ltd (In Liquidation)".

(i) Statutory Scheme

In his reasoning, Anderson J assessed the relevant statutory scheme and determined that the following debts paid from proceeds of ANZ's floating charge assets were priority debts under s. 556(1)(e) and (g) of the Corporations Act:

- superannuation contributions and wages payable to employees in respect of services rendered to Akron by employees before 1 February 2010; and
- annual leave payments and long service leave payments due to, or in respect of, employees on or before 1 February 2010.

(ii) Equitable right of subrogation

Citing Orakpo v Manson Investments Ltd [1978] AC 95, Anderson J described subrogation as "the transfer of rights from one person to another without assignment or assent of the person from whom the rights are transferred". His Honour also emphasised that unconscionability is the "rubric on which equitable subrogation is built", referring to the High Court decision in *Bofinger v Kingsway Group Ltd* [2009] HCA 44.

In deciding whether the liquidators of Akron were justified in regarding ANZ as subrogated in equity to the priority rights of employee creditors, Anderson J considered Finkelstein J's judgment in *Cook* and its subsequent application in *Carter*.

While an equitable right of subrogation was recognised in similar circumstances in *Cook*, the facts of *Cook* differ from the Akron case. Most significantly, in Akron, ANZ consented to the liquidators paying the priority debts from the proceeds of realisation of its floating charge assets meaning that there was no breach of trust in making the payment from those proceeds, which a liquidator holds in trust until it is determined whether sufficient free assets will be realised to pay priority debts. Finkelstein J considered such circumstances in obiter dicta in Cook at [101] and [108] indicating that, where a secured creditor consented to the early payment of priority debts from its floating charge assets, the secured creditor would be entitled to subrogation. In such circumstances, Anderson J explained that equitable subrogation was available because it would be unconscionable for the debtor to escape the liability which had been discharged by the assets subject to the secured creditor's security.

Finkelstein J's obiter dicta reasoning in *Cook* was subsequently adopted by the Federal Court in *Carter*. Therefore, the *Carter* decision provides a clear basis for an equitable right of subrogation arising in the circumstances of the *Akron* case.

Anderson J considered that the intention of the Act is to prioritise the payment of employee entitlements in a liquidation. Accordingly, ANZ agreed to the early payment of Akron's employee creditors from proceeds of realisation of assets subject to ANZ's floating charge. It did so at a time when it was not clear that sufficient free assets would be realised to make that payment. If ANZ had not consented to the payments, payment to the employee creditors would have been delayed causing potential hardship to the employees. Importantly, ANZ acted in the interests of the employee creditors by consenting to the payment in circumstances where that consent diminished ANZ's own security.

In this context, Anderson J's view was that it would be unconscionable for Akron to escape the liability discharged using the proceeds of ANZ's floating charge assets, and for Akron and its unsecured creditors to enjoy a windfall.

6.4 NSW Court of Appeal clarifies the rules surrounding defective notices of meeting

(By Thomas Smalley, King & Wood Mallesons)

Primary Securities Limited v Aurora Funds Management Limited [2020] NSWCA 230 (23 September 2020) New South Wales Court of Appeal, Bell P, Leeming JA and White JA

(a) Summary

The New South Wales Court of Appeal has clarified several laws concerning deficiencies in notices of meetings for listed schemes. White JA (Bell P and Leeming JA agreeing) held that:

- a notice of meeting issued by members pursuant to s. 252D of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) will be invalid if it does not identify the members calling the meeting;
- the failure to identify the members concerned alone will not be enough for this procedural irregularity to be considered a substantial injustice pursuant to s. 1322(2) of the Corporations Act - there must be a consequential impact on the meeting; and
- the failure to identify the members concerned alone will not be enough for an explanatory memorandum accompanying such a notice of meeting to be considered misleading and deceptive.

White JA also distinguished between ss. 1322(4) and 1322(6)(c) which raises the question of whether the making of a validating order would cause substantial injustice and s. 1322(2), where the question is whether the procedural irregularity has caused or may cause substantial injustice. Leave to allow the Appellant to amend its notice of appeal was not granted to seek an order pursuant to s. 1322(4) on the basis that it would substantially widen the enquiry and may result in the trial being run differently.

(b) Facts

Primary Securities Limited (Appellant) and Aurora Funds Management Limited (Respondent) were providers of financial services, including acting as responsible entities of management investment schemes. The Respondent was the responsible entity of the listed managed investment scheme, Aurora Absolute Returns Fund (Fund).

In April 2017, the Respondent caused the Fund to invest in Molopo Energy Ltd which proved problematic and contributed to the Fund reporting losses in the financial years ended 30 June 2017 and 30 June 2018. The Appellant purportedly represented dissatisfied Fund members seeking to replace the Respondent as responsible entity.

Pursuant to s. 252D of the Corporations Act, the Appellant on behalf of the dissatisfied investors circulated notices of meeting to be held on 15 January 2019. The notices did not identify the dissatisfied investors calling the meeting. The first set of notices of meeting were circulated based on an incomplete register on 21 December 2018. When the Respondent provided the Appellant with the complete register, a second set of notices was circulated on 28 December 2018. As a result, 25% of members did not receive adequate notice under the Act.

In addition, the directors of the Respondent did not become aware the meeting had been called until 7 January 2019 and the Auditors only became aware of the meeting on 17 January 2019 (after the date of the meeting). The meeting proceeded on 15 January 2019 and resolutions were passed replacing the Respondent with the Appellant as the responsible entity of the Fund. Shortly after, the Respondent commenced proceedings challenging the validity of the meeting and the resolutions.

The primary judge held that the meeting and the resolutions were invalid, and accordingly, that the Respondent remained as the responsible entity of the Fund. The primary judge did so on the basis that substantial injustice has been or was likely to be caused if the resolutions were permitted to stand as a result of the following procedural irregularities:

- the failure to identify in the notice of meeting the members calling the meeting was a substantive irregularity; and
- the required notice period of 21 days was not given to 25% of members and three members received no notice at all.

(c) Decision

There were four issues on appeal:

- was the notice calling the meeting invalid for failing to identify the members;
- was the failure to give the required notice to 25% of the members a substantive irregularity or procedural irregularity which caused substantial injustice;
- should the primary judge have found that the notice of meeting and explanatory memorandum were not sent to the directors and to its auditor within 21 days of the meeting, and if so was that a substantive irregularity, or, alternatively, a procedural irregularity that caused substantial injustice; and
- was the explanatory memorandum that accompanied the notice of meeting misleading and deceptive by not disclosing that certain members of the Fund, who between them held more than 20% of the units, were acting together in a covert and concerted attempt to remove the Respondent.

(i) The First Issue

White JA (Bell P and Leeming JA agreeing) affirmed the primary judge's decision, finding that the notices of meeting issued pursuant to s. 252D of the Corporations Act were invalid because they did not identify the members requisitioning the meeting.

White JA (Bell P and Leeming JA agreeing) added that s. 252D does not exclude the common law requirement that a member calling a meeting of members disclose their identity. Their Honours found transparency is important to ensure the entitlement of those calling the meeting can be verified and proper, informed debate of the resolutions can take place at the meeting.

(ii) The Second Issue

White JA (Bell P and Leeming JA agreeing) stated that had it been necessary to make a finding, contrary to the primary judge, there was no substantial injustice pursuant to s. 1322(2) of the Corporations Act caused by not providing proper notice to 25% of members.

This was because there was no evidence that a member would have conducted themselves any different or that the Respondent would have become aware of the meeting at an earlier stage had proper notice been given.

(iii) The Third Issue

White JA (Bell P and Leeming JA agreeing) found that, although a failure to give requisite notice to the directors of the Respondent would have been a procedural irregularity giving rise to substantial injustice, the evidence supported the primary judge's conclusion that the notices were given to the directors on time at the Respondent's last known place of businesses, and notice was provided to the auditor at the same time. White JA determined that substantial injustice would have arisen as the directors gave evidence that they would have prepared a communique addressing the matters in the explanatory memorandum had they become aware of it at an earlier date.

Their Honours also found that, although the notice to the auditor was wrongly addressed, this was not a procedural irregularity causing a substantial injustice because there was no evidence that it being provided earlier would have resulted in the directors becoming aware of the meeting at an earlier date.

(iv) The Fourth Issue

White JA (Bell P and Leeming JA agreeing) agreed with the primary judge's conclusion that the explanatory memorandum that accompanied the notice of meeting was not misleading and deceptive by not disclosing the names, unit holdings and details of the members who were acting together to remove the Respondent.

Their Honours found that the evidence at first instance did not establish that the Appellant knew or actually suspected that the undisclosed investors were acting in concert in a way that contravened the requirements of Chapter 6 of the Corporations Act. Their Honours also found that, even if the contrary were true, the unitholders would not hold a reasonable expectation that the Respondent would disclose matters of suspicion in the explanatory memorandum, particularly matters that were not directly relevant to the merits of the proposed resolutions and that may give rise to illegal behaviour. Therefore, in their Honours' view the memorandum was not misleading by omission.

6.5 Entitlement of a liquidator to distribute a winding up surplus to one or more charities: Recipients must meet constitutional criteria

(By Ellie Nolan, Corrs Chambers Westgarth)

In the matter of Maitland Benevolent Society Ltd (in liquidation) [2020] NSWSC 1284 (21 September 2020) Supreme Court of New South Wales, Rees J

(a) Summary

Following the winding up of the Maitland Benevolent Society Ltd (MBS), its liquidator Mr Jeffrey Shute sought to pay the $8.15 million surplus to the Royal Freemasons' Benevolent Institution Ltd (RFBI). Shute applied to the Court for an order to do so in two alternative methods:

- through an order under s. 23 of the Supreme Court Act 1970 No. 52 (NSW) (the SCA); or
- through a direction under s. 90-15 of Schedule 2 of the Corporations Act 2001 No. 50 (Cth) (Insolvency Practice Schedule).

The MBS owned and operated the Benhome Residential Aged Care facility (Benhome) in Maitland. The United Protestant Association of NSW Limited (UPA) appeared, seeking half (or alternatively a quarter) of the surplus. The MBS constitution required that any surplus be used to benefit Benhome "residents", and the UPA submitted that, on a wide reading, "residents" extended to the broader aged community of Maitland, and that their provision of aged care services in Maitland also entitled them to the surplus.

Rees J rejected the UPA's proposed interpretation, additionally finding that by enabling the payment of directors' fees, the UPA was not an eligible entity for the surplus payment. Her Honour ordered that pursuant to s. 90-15 of the Insolvency Practice Schedule, the MBS was entitled to pay the surplus in its entirety to the RFBI.

(b) Facts

In 2018, MBS decided to sell Benhome to a larger, better resourced professional provider. The RFBI and the UPA made expressions of interest in the purchase.

MBS represented to the RFBI that surplus funds from their winding up would be distributed to the successful purchaser for capital improvements of the facility. It then sold the business and associated land to RFBI in May 2019.

Separately to the sale, the MBS proposed a trust deed to ensure that the surplus to be granted to RFBI would be used for the sole purpose of Benhome. The proposed deed also requested that RFBI indemnify MBS for any third party claims arising after the winding up, limited to the value of the surplus funds remaining undistributed at the time of the claim. The deed was not finalised prior to Shute's appointment as liquidator in September 2019. Shute was instructed by MBS that, despite the lack of a finalised deed, the funds were intended to be distributed to RFBI alone. Shute sought the imprimatur of the Court to distribute the funds in this manner.

(c) Decision

(i) Requirements of MBS constitution

In the event of MBS being wound up, cl. 105 of the MBS constitution provided that any surplus should be paid to a benevolent institution with objectives similar to those in cl. 2, and which prohibits the payment of fees to its directors.

According to cl. 2 of its constitution, MBS' objective was to enhance the quality of life of aged and frail people by providing care to its residents. Rees J interpreted "residents" to refer to persons living at Benhome.

Clause 21 of its constitution further provided that MBS "must not pay any fees to a Director for performing that person's duties and responsibilities as a Director. The Company must not pay any amount to a Director unless that payment has been approved by the Directors". Rees J noted that indeed, directors as fiduciaries have historically had no right to be paid for their services, and any monies paid to directors is considered a gratuity (citing Bowen LJ in *Hutton v West Cork Railway Co* (1883) 23 Ch D 654, 671-2). To be eligible for the surplus, both the RFBI and UPA could not allow the payment of directors' fees.

(ii) Allowances for directors fees in RFBI and UPA constitutions

There was no dispute before the Court that RFBI satisfied all of the conditions under cl. 105 of MBS' constitution. Its constitution mirrored the objectives of cll. 2 and 21.

As to the UPA, no part of its constitution excluded the possibility of paying directors' fees. Clauses 2.8(a) and 22.3 of its constitution in fact allowed for the "reasonable and proper remuneration [of staff or members] ... in return for ... services actually rendered". Rees J noted that in practice, the UPA has never paid directors' fees. However, its constitution ultimately does not prohibit it. Further, the constitution does not require director or member approval to reimburse directors for expenses, or to approve other payments made to directors. Therefore, Rees J found that the standards of cl. 105 of the MBS constitution were not met. Accordingly, the UPA was not an appropriate entity to be granted the surplus.

(iii) Interpretation of "residents"

In regards to the interpretation of "residents", Rees J found no basis for applying a broad interpretation of the MBS constitution. Her Honour stated that "the role of the Court is to make a determination in accordance with the constitution. The [MBS] constitution . is a contract between the society and each member, between the society and each director, and between the members themselves". As such, the objectives of MBS were best served by granting the surplus to the RFBI. As the new owner and operator of Benhome, it was best placed to conduct capital improvements to the facility to improve residential care.

6.6 UK High Court case on business interruption insurance for COVID-19

(By Kemsley Brennan, Kathryn Rigney and James Stanton, MinterEllison)

Financial Conduct Authority v Arch Insurance (UK) Ltd [2020] EWHC 2488 (Comm) (15 September 2020) High Court of Justice (UK), Flaux LJ and Butcher J

(a) Summary

The UK High Court considered 21 exemplar insurance policy wordings from eight insurers in the market. The purpose of examining those wordings was, in short, to consider whether they could respond to certain types of business interruption loss that affected insureds during the Novel Coronavirus SARS-CoV-2 (COVID-19) pandemic.

The case dealt with how business interruption policies could and ought to operate in circumstances where there has been no physical damage to the insured premises. That issue was tested in other Commonwealth jurisdictions following the outbreak of Severe Acute Respiratory Syndrome (SARS) outbreaks in 2002 but not in the magnitude dealt with by the Court in this case.

In short, the Court largely agreed with the Financial Conduct Authority's (FCA) arguments. Subject to an appeal, the expected effect of this would be that many insureds under those policies may be entitled to cover. Of course, cover will still be dictated by the terms of those policies and the circumstances of each case.

(b) Facts

(i) Background

In the midst of the global COVID-19 pandemic, the global insurance market saw and is still seeing numerous notifications of loss to businesses due to the disease, interruption to trade, and government-mandated closures. Insurers have also worked to respond to those notifications, with varying effect. As a consequence, in the United Kingdom, the FCA determined to resolve questions relating to the coverage available under certain exemplar insurance wordings by way of the test case.

The eight insurer defendants agreed to participate in the test case. The FCA represented the interests of the policyholders, many of which were small to medium sized enterprises. There were 21 sample wordings considered, but the FCA estimates that, in addition to these particular wordings, some 700 types of policies across 60 different insurers and 370,000 policyholders could potentially be affected by the test case.

The business interruption policies in question were issued by insurers to small, medium and large businesses alike. Such policies are ordinarily intended to cover damage and loss to business premises, as well as the consequential loss of profit and any additional expense consequent upon that physical loss.

Classically, the business interruption cover in those policies would trigger following incidents such as floods, fires and building collapses. However, a large number of those policies also extend to cover other incidents which do not strictly result from damage to the property. Those types of cover were directly called into question by COVID-19 and examined by the Court.

(ii) Agreed facts

The following matters were largely agreed for the purposes of this case:

- on 3 March 2020 the British Government announced its COVID-19 action plan;
- on 5 March 2020, England and Wales deemed COVID-19 a notifiable disease;
- on 11 March 2020 the World Health Organisation (WHO) declared COVID-19 to be a pandemic;
- on 16 March 2020, the British Government directed people to stay at home, stop non-essential contact and unnecessary travel, work from home where possible, and avoid social venues;
- on 20 March 2020, the British Government directed various categories of business to close, such as pubs, restaurants, gyms etc (given legal effect by Regulations coming into force on 21 March 2020); and
- on 23 March 2020 the British Government announced a lock-down involving closure of further businesses including all non-essential shops and restrictions on individual movement (given legal effect by Regulations coming into force on 26 March 2020).

Different businesses were affected in differing ways across each of the above steps. The Court acknowledged this, and the parties generally agreed certain matters had different application to, for instance, schools, churches and holiday accommodation.

(iii) Policy wordings considered

The Court examined three specific categories of policy wording issues arising from the exemplar policies:

- "Disease clauses"- these were sections of the insurance policy which afforded business interruption cover in consequence of or following or arising from the occurrence of a notifiable disease within a specified radius of the insured premises;
- prevention of access/public authority clauses - these were policy sections which afforded business interruption cover in the event of a prevention or restriction of access or use of the insured's premises as a consequence of government or other authority action or restrictions; and
- hybrid disease and prevention clauses - these were a hybrid of the first two categories, where policies featured cover which would be triggered by restrictions imposed on the premises in relation to a notifiable disease.

(c) Decision

(i) Disease Clause findings

The "Disease Clauses" appeared in policies written by four insurers in the market (RSA, Argenta, MS Amlin and QBE). Each policy contained its own variation of the wording, but in general the clauses provided cover for loss which was the result of:

- "interruption or interference with the business. following / arising from / as a result of any notifiable disease / occurrence of a notifiable diseases / arising from any human infectious or human contagious disease manifested by any person.within 25 miles / 1 mile / the "vicinity" of the premises / insured location".

Some of the QBE wordings deviated from that language slightly, importantly using the words "in consequence of.any occurrence of a notifiable disease". As noted below, the Court considered this variation was important in the context.

In summary, it was the position of each relevant insurer that the Disease Clauses would only provide cover for a "local occurrence of a notifiable disease". Given COVID-19 was actually a wider disease spread, the Insurers said that only the effects of the particular local element would be covered. The Court disagreed with that approach and favoured the FCA's argument, which was that the proper test was not a "but for" test in relation to a local outbreak, but a proximate cause test.

Since the COVID-19 outbreak in the relevant policy area was indivisible from the broader disease spread, it should be covered under the Disease Clauses. They also argued that it was not truly "local versus global" but that the outbreak was the same disease in a large number of places. The Court determined that:

- "when the disease broke out in the relevant area, that was an "occurrence". The Disease Clauses were therefore triggered as soon as there was a diagnosable case of the disease in the area relevant to the particular policy (i.e. within the relevant radius to that insured's business)";
- "the insured peril is the combination of interruption/interference to the Business, which follows the occurrence of the notifiable disease within the relevant radius";
- "there must be proximate causation between the loss claimed by the insured and the insured peril (interruption flowing from the occurrence of the disease within the radius)"; and
- "cover was not limited to outbreaks wholly occurring within the relevant policy area. As such, cases in one radius were not independent separate causes from other cases outside the radius".

As noted above, the Court separately dealt with two wordings issued by QBE which contained the words "in consequence of" and "events". Those words distinguished the clause from the others outlined above, and limited the clause to matters occurring at a particular time, in a particular place and in a particular way.

The practical effect would therefore be that insureds under the particular QBE wordings would only be able to recover if they could show that disease cases in that local area (but not elsewhere) were the cause of the business interruption.

(ii) The Prevention of Access / Public Authority Clauses

The Prevention of Access Clauses appeared in policies written by six insurers in the market (Arch, Ecclesiastical, Hiscox, MS Amlin, RSA and Zurich). Again, each policy contained its own variation of the wording, but in general the clauses provided cover for loss which was the result of:

- "Prevention / denial / hindrance of access to the Premises. Due to actions / advice / restrictions of / imposed by order of. A government /local authority /police / other body. Due to an emergency likely to endanger life / neighbouring property/incident within a specified area".

In construing those clauses, the Court indicated they should be given a more restrictive interpretation than most Disease Clauses. The particular words of those Prevention of Access Clauses were key to the Court's assessment, and some of the matters the Court noted were:

- Words such as "emergency in the vicinity", and "injury in the vicinity" required an event that was more specific than a general existence of an outbreak. It had to occur at that place and at a particular time. Those types of clause provide a narrower, local cover;
- British Government announcements on 16, 20 and 23 March 2020 were not mandatory, but advisory. That could trigger some of the wordings which featured the word "advice", or "action";
- Wordings which required there to be steps or action to "prevent" access, required more than mere advice, but called for the force of law to prevent access. The same was held for the requirement that there be any restriction "imposed by order";
- Wordings which specifically required a "prevention" of access (e.g. rather than mere "hindrance") did not require physical prevention but there needed to be closure of those premises such that business could not be carried on there; and
- Wordings requiring "interruption" did not mean a complete cessation of the business but only the general interruption of business (including disruption or interference). Some policies had defined "interruption", so those were not captured by the Court's observation.

In short, determining whether the Prevention of Access Clauses will trigger depends still on the particular terms of that policy and the precise facts affecting the insured.

For instance, directions for a café to close could be a "prevention of access", since the premises themselves were closed to business. If the insured's wording features that wording then there may be cover (subject to other terms and facts). If the café continued to offer takeaway, then that wording might not offer cover since they were not strictly "prevented access". Each case will turn on its facts.

(iii) Disease and Prevention Hybrid

The Hybrid Disease and Prevention of Access Clauses appeared in policies written by Hiscox and RSA. The policies contained their own variations of the wording, but in general the clauses provided cover for loss which was the result of:

- "An interruption to the business.Due to an inability to use the premises.Due to restrictions imposed by a public authority.Following an occurrence of disease".

In summary, the Court largely followed its interpretation for the Disease Clauses. It agreed with the FCA that they should not be limited to local outbreaks only. Further, in line with the Prevention of Access construction mentioned above, the Court also noted that "restrictions imposed" and "inability to use" should be construed narrowly (again, they required something more compulsory or mandatory such as force of law or, for "inability to use" the premises, something more than ordinary impairment of use.

4. Practical takeaways for Australia

While the Court noted that each case had to be determined on its own facts, the Court provided its guidance in relation to how each policy wording should be effectively construed. It also outlined that certain pieces of evidence could potentially be used by the insureds to establish whether there had been outbreaks, or cases falling within their local radius areas. Those included:

- categories of evidence put forward by the FCA (eg. specific evidence, NHA Deaths Data, and reported cases) may prima facie demonstrate the presence of COVID-19;
- a distribution-based analysis, or an undercounting analysis (eg. there are more cases than the reported cases), could in principle discharge an insured's burden of proof; and
- insurers did not indicate that they would require exact precision to establish cover.

Subject to an appeal, the Court's interpretation will assist a large number of insureds in assessing whether their particular circumstances fall for cover under the Disease Clauses, Prevention of Access Clauses or Hybrid policy wordings.

In Australia, the Insurance Council of Australia and the Australian Financial Complaints Authority are preparing a test case for the NSW Court of Appeal. The case, *HDI Global Specialty SE v Wonkana No 3 Pty Limited trading as Austin Tourist Park*, is chiefly intended to seek clarity from the Court in relation to certain exclusion clauses which reference the Quarantine Act 1908 No. 3 (Cth) (the Quarantine Act) as amended, whether those references encompass the Biosecurity Act 2015 No. 61(Cth) (the Biosecurity Act) and, if so, the timing of the application of the exclusion.

The Australian test case has not raised the scope or extent of issues that were canvassed by the UK High Court in the FCA Case. However, that determination will go some way towards assisting Australian insureds and insurers in considering whether their own policies might cover their business interruption losses resulting from COVID-19.

The common law doctrine in England and Australia dictates that, while compelling, the English Court's determination is not strictly binding on Australian courts. As such, once the Australian test case determines the questions raised regarding the Quarantine Act and the Biosecurity Act, it seems probable that Australian insureds might seek to run a second test case. That case would, much like the FCA Case, likely need to address the Australian position in relation to when, how, and whether various classes of policy in the Australian market provide cover for an insured's business interruption losses.

6.7 Court refuses to allow inspection of a company's insurance policy to assist a class action

(By James Atcheson, King & Wood Mallesons)

Ingram as trustee for the Ingram Superannuation Fund v Ardent Leisure Limited [2020] FCA 1302 (11 September 2020) Federal Court of Australia, Derrington J

(a) Summary

Colin Ingram and Judy Tolloch (Applicants) are the lead applicants in a class action against Ardent Leisure Group Limited and its subsidiaries, Ardent Leisure Limited and Ardent Leisure Management Limited (together "the Respondents"). The Applicants sought an order under s. 247A of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act) authorising them to inspect certain documents held by the Respondents, including insurance documents, correspondence between the Respondents and their insurer and an intercompany guarantee. In refusing the order, the Court found that the Applicants were not acting in good faith and for a proper purpose as is required by s.247A.

(b) Facts

The Applicants acquired stapled securities in the Ardent Leisure Group in July 2016 on the ASX. At that time, the Ardent Leisure Group was a stapled entity comprising Ardent Leisure Limited and Ardent Leisure Management Limited as responsible entity of the Ardent Leisure Trust. In October 2016, four people tragically died on the Thunder River Rapids Ride at Dreamworld, an amusement park owned by Ardent Leisure Group. The price of Ardent Leisure Group's stapled securities decreased significantly following that incident.

In 2018 the Ardent Leisure Group underwent a corporate "top-hatting" restructure which resulted in Ardent Leisure Group Limited becoming the head entity.

In June 2020, the Applicants became the lead applicants in a securities class action against the Respondents (Class Action). The Class Action alleges that representations made by the Ardent Leisure Group regarding the safety standards at Dreamworld were misleading or deceptive and that had the Applicants known, they would not have acquired the stapled securities. The Class Action is to be supported by a litigation funder. However, that funding is contingent on the Applicants obtaining copies of all relevant policies of insurance covering the Respondents against all liabilities arising out of the claim.

The Applicants sought orders pursuant to s. 247A of the Corporations Act to inspect certain documents held by the Respondents, including insurance documents, insurance related correspondence between the Respondents and their insurer and an intercompany guarantee (to ensure that Ardent Leisure Group Limited guaranteed Ardent Leisure Limited in respect of its liabilities for the benefit of its creditors).

The Respondents submitted that the orders should not be made as the Applicants' purposes were not "proper purposes" within the meaning of s. 247A and, that even if they were, the Court should exercise its discretion to refuse relief.

(c) Decision

Derrington J found that:

- the Applicants were not acting in good faith and for a proper purpose in seeking the orders; and
- the Court would not have exercised its discretion to grant the relief in any event.

(i) Good faith and for a proper purpose

Section 247A requires the Court to be satisfied that the Applicants are acting in good faith and that the inspection is made for a proper purpose. Derrington J confirmed that this is now accepted as a composite phrase and requires an objective test.

In particular, the purpose must be connected to the person's rights as a member of the entity, and the right in question must arise because of the person's status as a member. The Court accepted Brereton J's finding in *Re Tolco Pty Ltd* [2016] NSWSC 1069 that authority to inspect will be refused where the purpose is unrelated to the interests of the member being a member or is an abuse of process.

Derrington J found that the Applicants' claim did not arise in relation to their rights and entitlements as members. Rather, the Respondents' alleged conduct was said to have affected the Applicants in their capacity as potential investors. Derrington J emphasised that although the damage that the Applicants suffered arose after they became members and occurred because they were members, it was not because of any infringement of a right or entitlement that attached to them in their capacity as members. Accordingly, Derrington J found that the purposes for which the Applicants sought to inspect the documents were not proper purposes within the meaning of s. 247A.

The Court further clarified that separate proceedings being on foot does not automatically preclude there being a proper purpose under s. 247A. Rather, if seeking inspection of a company's documents to ascertain the commercial viability of an action was for a proper purpose, it would not matter whether any proceedings had commenced.

(ii) Discretion

An order pursuant to s. 247A is, in any event, discretionary. Derrington J found that the Court's discretion would have been exercised against granting the order even if it was determined that the Applicants' purpose was within the scope of s. 247A.

The Court found that six matters identified by Beach J in *Evans v Davantage Group Pty Ltd (No 2)* [2020] FCA 473 were relevant to the exercise of discretionary power in s. 247A and, that if the discretion had been enlivened, the application of these six matters would have weighed heavily against allowing the order.

These six matters were:

- that insurance documents are generally commercially confidential between the insurer and the insured;
- if a policy of insurance responds to a claim advanced against a respondent, it is likely that respondent is capable of enforcing its rights to coverage and to contest any refusal wrongly made;
- that an insurance policy is usually discoverable only where it has a direct relevance to an issue arising on the pleadings;
- that an applicant does not usually have the ability to examine a potential respondent's creditworthiness before commencing an action;
- that despite the settlement of a class action under Part IVA of the Federal Court of Australia Act 1976 No. 156 (Cth) requiring curial approval, this does not support the disclosure of insurance policies; and
- that the disclosure would give the Applicants a not insignificant commercial advantage in negotiations which is more than any advantage ascertainable through the court rules.

Derrington J also identified other considerations which would have weighed against the Court's use of its discretion. These were that:

- the Respondents were solvent;
- the Respondents' net assets exceeded the amount of the claim of the class action;
- there was no apparent risk of dissipation of any insurance policy proceeds;
- inspection was also sought for the benefit of third parties as some members of the Class Action may no longer be shareholders; and

- there is a special importance of communications between an insured and an insurer (regarding the correspondence between the Respondents and their insurer).

6.8 Appointment of provisional liquidators pending determination of a winding-up application

(By Matthew Anderson, Herbert Smith Freehills)

Re IPO Wealth Holdings No 2 Pty Ltd [2020] VSC 549 (9 September 2020) Supreme Court of Victoria, Robson J

(a) Summary

Robson J of the Supreme Court of Victoria considered an application to appoint provisional liquidators pending the determination of winding-up applications over a group of companies.

In finding sufficient grounds to appoint provisional liquidators, Robson J held the applicant must satisfy the Court of two matters:

- first, that there is a reasonable prospect that a winding-up order will be made. The requisite "lack of confidence in the company's affairs" may arise where the company is in default, unable to pay debts when due, and is placed into voluntary liquidation; and
- secondly, that there are sufficient factors to require the exercise of the court's discretion. The court will consider whether the assets of the corporation are at risk, the degree of urgency, and the need for an independent examination of the company's accounts. Sufficient grounds may arise upon evidence which "strongly suggests that assets have been wrongly dealt with to the detriment of investors".

(b) Facts

IPO Wealth is a managed investment scheme that was open to high net worth members of the public. Under the terms of the scheme, the fund's trustee loaned the invested money to IPO Wealth Holdings Pty Ltd and a number of special purpose vehicles (the SPVs), all of which were controlled by Mr James Mawhinney.

Following significant defaults under the investment loan, IPO Wealth Holdings Pty Ltd and the SPVs were placed into receivership. Upon discovering evidence of voidable transactions and accounting irregularities, the trustee sought to wind up the entities and appoint the current receivers, Dye & Co, as their provisional liquidators.

(i) The trustee and receiver's concerns

An April 2020 asset portfolio summary indicated a $17.7 million drop in assets of the IPO Wealth Group worth "almost a quarter of the IPO Wealth Group's assets", due in part to an investment in software development business, Accloud PLC. Mr Mawhinney provided multiple conflicting explanations for this investment, originally claiming the shares had been sold to a British Virgin Islands company outside of the IPO Wealth Group that he controlled.

The receivers and managers further submitted that the accounts kept by Mr Mawhinney were "misleading at worst and sloppy at best". Significant arithmetical errors had been identified and assets had been re-valued in circumstances where the receivers and managers could not find documentation to support their revaluation.

(ii) Submissions of Mr Mawhinney

Arguing that provisional liquidators were not necessary, Mr Mawhinney submitted that the receivership had already secured the assets and diverted their management from him. Further, Mr Mawhinney submitted that the functional similarities between receivership and provisional liquidation meant there was nothing the receivers wished to do that they could not already do (except for commencing proceedings in respect of voidable transactions, which had not yet been pursued).

(c) Decision

Robson J found sufficient grounds to warrant the appointment of provisional liquidators to both IPO Wealth Holdings Pty Ltd and the SPVs prior to the hearing of the winding up application, and ordered their appointment.

In respect of an application to appoint provisional liquidators, Robson J affirmed what Gordon J said in *ASIC v ActiveSuper Pty Ltd (No 2)* [2013] FCA 234 and held the applicant must satisfy the court of two matters:

- that there is a reasonable prospect that a winding-up order will be made; and
- that there are present factors sufficient to require the exercise of the court's discretion to appoint a provisional liquidator prior to the final hearing.

(i) Reasonable prospect of winding up

A winding up application can be granted where there is "a justifiable lack of confidence in the conduct and management of the company's affairs" such that there is a risk to the public interest (*Loch v John Blackwood Ltd* [1924] UKPC 45).

Robson J identified a number of factors in finding a real prospect that a winding up order will be made:

- first, the action of Mr Mawhinney in placing IPO Wealth Holdings Pty Ltd into voluntary liquidation of itself admits insolvency;
- secondly, IPO Wealth Holdings Pty Ltd is in default and is unable to repay its approximately $80 million debt to the trustee. The investors are not receiving their interest payments; and
- thirdly, the inadequacy of Mr Mawhinney's explanation of the Accloud PLC share transfer induces a lack of confidence in the way in which the affairs of IPO Wealth Holdings Pty Ltd and the SPVs have been conducted.

(ii) Factors sufficient to require the exercise of the court's discretion

An applicant "must point to some good reason for intervention" (*Allstate Exploration NL v Batepro Australia Pty Ltd* [2004] NSWSC 261, [30]) as the appointment of provisional liquidators "is a drastic intrusion into the affairs of the company and will not be done if other measures would be adequate to preserve the status quo" (*ASIC v ActiveSuper Pty Ltd* (No 2) [2013] FCA 234).

Robson J identified several factors sufficient to require the exercise of the court's discretion:

- first, the interests of investors are of 'of primary importance', particularly for schemes that solicit investments from the public. Provisional liquidators would be better placed to protect their interests and identify any available returns;
- secondly, the fact that the assets of the corporation may be at risk is a relevant consideration. There were several aspects of the scheme which strongly suggested that assets had been wrongly dealt with to the detriment of investors, including a prima facie case that Mr Mawhinney had diverted assets to several director-related entities outside the IPO Wealth Group; and
- thirdly, there appeared to be the possibility of substantive misreporting and a need for the independent examination of accounts.

6.9 Liquidators found liable to pay the EPA's costs of cleaning up contaminated land, despite disclaimer

(By Michael Sloan, Robert Jamieson, Jane Hall and Daniel Dai, Ashurst)

EPA v Australian Sawmilling Company Pty Ltd (in liq) [2020] VSC 550 (2 September 2020) Supreme Court of Victoria, Garde J

(a) Summary

The Victorian Supreme Court has found that the liquidators of a wood processing business (The Australian Saw Milling Company or TASCO) were liable to pay the Victorian Environment Protection Authority's (EPA) costs of remediating contamination on TASCO's land, despite the liquidators disclaiming the land.

This finding will send a shiver through the insolvency profession, and those appointing and indemnifying practitioners. It suggests that the costs of environmental liabilities will be put on indemnifying creditors. In this case, the EPA undertook to limit the liquidators' exposure to the extent that they enjoyed an indemnity from their appointors. However, such a concession does not apply by default. Practitioners will need to carefully consider taking appointments over land that is potentially subject to environmental liabilities.

Having said that, the facts of this case were of particular concern to the EPA, and it is very unlikely that a blanket pursuit of practitioners and their indemnifiers will occur as a matter of course.

(b) Facts

TASCO leased land (Land) to C&D Recycling, who operated a materials recycling business. The Land became contaminated after it was used to store industrial waste such as concrete, asbestos, plastic, and tyres. C&D Recycling subsequently went into liquidation, and ceased to occupy the Land.

Liquidators were then appointed to TASCO by way of a creditors' voluntary winding up. At that time, the Land was TASCO's only asset. Dongwha Australia (an entity related to TASCO) granted the liquidators an indemnity for an unlimited amount in respect of environmental liabilities (including for the liquidators' costs and remuneration arising out of such liabilities) (Indemnity).

During the liquidation, the EPA exercised its statutory powers under the Environment Protection Act 1970 No. 8056 (Vic) (EP Act) to enter the Land and remediate the contamination. The EPA has a right to recover remediation costs from the polluter or "occupier" of the land as a statutory debt.

The next day, the liquidators disclaimed TASCO's interest in the Land on the basis that the contamination made the Land unsaleable, and the costs of realising the Land would exceed any potential return. The disclaimer would effectively terminate the liquidators' obligations in respect of the Land, including any potential obligation to pay the EPA's remediation costs.

The EPA and the State of Victoria (the State) then brought an application to set aside the liquidators' disclaimer under s. 568B(1) of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act). In the course of the proceedings, the EPA gave an undertaking to the Court that it would limit the liquidators' liability to the amount recovered by them under the Indemnity (Undertaking).

(c) Decision

There were six key issues in the case. The Court's findings with respect to each are summarised below:

(i) The EPA may recover remediation costs as a statutory debt from parties who are "occupiers" of "premises" (e.g. the Land) under ss. 4(1) and 62(3) of the EP Act. Are the liquidators "occupiers" of the Land?

- when the liquidators were appointed and assumed control of TASCO's affairs, they became "occupiers" of the Land under s. 4(1) of the EP Act. They were therefore potentially liable for the EPA's remediation costs;
- a person is an "occupier" if they are in control of land. There is no requirement that an "occupier" own or be in possession of the land;
- the liquidators held physical and legal control over the Land pursuant to their powers under the Corporations Act as external administrators. This is despite the fact that legal ownership of the Land remained with TASCO, and the liquidators exercised their control over the Land as TASCO's agents; and
- it would be contrary to the objectives of the EP Act if companies occupying or controlling contaminated land could be placed into liquidation to avoid environmental liabilities.

(ii) Did the liquidators cease to be "occupiers" of the Land when the EPA entered the Land and conducted remediation works?

- the liquidators continued to be "occupiers" of the Land, because the EPA's remediation actions did not end the liquidators' control over the Land;
- nor did the EPA become an "occupier" to the exclusion of the liquidators. If that were the case, the EPA's power to recover remediation costs would be pointless, because it would only be entitled to recover from itself; and
- in any case, there can be multiple "occupiers" of land.

(iii) A liquidator does not have to incur post-liquidation expenses unless there is sufficient available property: s. 545(1) of the Corporations Act. Does this section bar the EPA's claim for remediation costs if TASCO does not have sufficient available property?

- the Indemnity constituted 'sufficient available property' to meet the EPA's remediation costs;
- where there is sufficient available property, s. 545(1) puts a cap on the liquidators' liability. It does not give the liquidators immunity from specific liabilities such as statutory debts; and
- he Court also considered whether the EPA's right to recover remediation costs as a statutory debt was inconsistent with the liquidators' right to not incur post-liquidation expenses unless there is sufficient available property. It found that there was no inconsistency. Post-liquidation statutory debts (e.g. rates, charges, taxes etc.) have always operated concurrently with s. 545(1). This case was no different, because the EPA's right to recover remediation costs is consistent with corporate insolvency laws relating to debt recovery, priority of debts, and liquidation procedures.

(iv) A person who has or claims to have an interest in disclaimed property has standing to apply to the Court to have the disclaimer set aside: s. 568B(1) of the Corporations Act. Are the EPA and the State persons who have, or claim to have an interest in the Land?

- both EPA and the State had an interest in the Land, and therefore standing to apply to the Court to set aside the disclaimer;
- EPA had an interest in the Land as a prospective chargee, because remediation costs incurred by the EPA can form a charge over land; and
- the State had an interest in the Land pursuant to a claim to radical title, and to be the fee simple owner if the Land vested back in the Crown by the operation of the disclaimer.

(v) The Court can only set aside a disclaimer if it is satisfied that the disclaimer would cause prejudice to those with an interest in the property that is grossly out of proportion to the prejudice suffered by the creditors if the disclaimer was set aside: s. 568B(3) of the Corporations Act. Would the EPA and the State be so prejudiced by the disclaimer?

- the Court was satisfied that the EPA and the State would be so prejudiced;
- TASCO only had four known creditors: Dongwha Australia, Dongwha Holdings (TASCO's sole shareholder and a related entity), the State (for land tax) and the ATO (for PAYG payments);
- it was clear that TASCO's creditors would not receive a dividend whether or not the disclaimer was set aside;
- TASCO's creditors would suffer no prejudice if the disclaimer was set aside, other than a delay in finalising the liquidation;
- if the Indemnity was called on, Dongwha Australia would incur costs as TASCO's indemnifier. However, it would not be prejudiced in its capacity as TASCO's creditor; and
- by contrast, if the disclaimer was not set aside, the EPA and the State would be heavily prejudiced, because they would have to bear the remediation costs.

(vi) Even if standing and prejudice have been established, the Court has discretion on whether or not to set aside a disclaimer: s. 568B(2) of the Corporations Act. Should the Court exercise its discretion to set aside the disclaimer?

The Court exercised its discretion to set aside the disclaimer, taking into account the following factors:

- voluntary liquidation (and a liquidator's power to disclaim property) should not be used to avoid environmental responsibilities, or to impose the cost of remediation on tax payers or the State;
- voluntary liquidation (and a liquidator's power to disclaim property) should not be used to avoid environmental responsibilities, or to impose the cost of remediation on tax payers or the State;
- voluntary liquidation (and a liquidator's power to disclaim property) should not be used to avoid environmental responsibilities, or to impose the cost of remediation on tax payers or the State;
- the creditors would not be materially prejudiced if the Indemnity was called on;
- the liquidators were unlikely to be prejudiced. They were protected by the Indemnity (which extended to their costs and remuneration) and sheltered from personal liability by s. 545(1) of the Corporations Act and the Undertaking; and
- setting aside the disclaimer is consistent with the purpose of the EP Act (e.g. minimising harm to the environment and holding polluters accountable).

6.10 Administrators following a constrained sale process considered not to be acting with bias or impropriety

(By Morgan Hartley-Marschner, DLA Piper)

Strawbridge, in the matter of Virgin Australia Holdings Ltd (administrators appointed) (No 8) [2020] FCA 1344 Federal Court of Australia, Middleton J, date of judgment: 17 August 2020; date of publication of reasons: 18 September 2020

(a) Summary

This proceeding concerned an interlocutory application by Broad Peak Investment Advisers Pte Ltd and Tor Investment Management (Hong Kong) Ltd, the applicants, seeking an order that a rival deed of company arrangement (DOCA) be considered at the second meeting of creditors regarding the administration of the Virgin Companies and for a facilitator to assess the rival DOCAs and prepare a report for inclusion in the administrators' report to the creditors.

The administrators secured a DOCA with Bain Capital (Bain DOCA) which was to be considered at the second meeting of creditors. The applicants wanted to present the rival DOCA to the creditors of the Virgin Companies before the Bain DOCA was approved. However, the terms of the Sale and Implementation Deed (SID) between the administrators and Bain Capital did not permit this. The administrators did propose that their report to creditors contain details of the rival DOCA put forward by the applicants. The court dismissed the application.

(b) Facts

Prior to the second meeting of creditors, the administrators, in line with their powers under s. 437A(1)(c) of the Corporations Act 2001 No. 50 (Cth) (the Corporations Act), arranged for the business and assets of the Virgin Companies to be sold to Bain Capital. In preparation for the sale, various documents were prepared, including the Bain DOCA but importantly, the SID, which contained the contractual mechanism that the sale was to follow.

The SID was found to be a binding agreement between the parties and provided:

- the option that the sale could occur pursuant to approving the Bain DOCA at the second meeting of creditors or by way of an asset sale agreement (ASA);
- the obligation to adjourn the second meeting of creditors if the Bain DOCA was not approved and for the sale to proceed pursuant to the ASA;
- that the assets of the Virgin Companies, which would have formed part of the estate under the Bain DOCA would also form the assets under the ASA, meaning that any alternative DOCA proposals could not manage these assets; and
- that alternative DOCA proposals could not be considered by the administrators pursuant to an exclusivity clause.

The finding that the SID was binding was based on the intentions of both parties, the lawfulness of the agreement and the absence of the administrators acting inappropriately. As the administrators were bound to follow this process, the rival DOCA prepared by the applicants would not be formally proposed to the creditors at the meeting but would be referred to in the administrators' report to the creditors.

The applicants' basis for wanting a facilitator to review the rival DOCA and prepare a report stemmed from their view that the administrators lacked independence given their contractual duties to Bain Capital under the SID.

(c) Decision

The court stated that the future of the company and thus any sale of its business or assets is up to the creditors to decide, subject to the administrators performing their obligations under s. 437A(1)(c) of the Corporations Act. Middleton J highlighted the importance of the administrators facilitating the second meeting of creditors in a proper manner and according to law, ensuring that the creditors are given reasonable opportunity for informed debate and provided with all the necessary information and time to consider that information before the meeting. There was no bias in the administrators agreeing to the SID and pursuing the sale of the Virgin Companies business and assets through the Bain DOCA so long as the creditors were informed.

Middleton J did not consider the extent to which the Bain Capital process of sale was assessed by the administrators, whether the SID was in the best interests of creditors or to what extent the SID was conditional. There was no reason or application made to impugn the business and commercial judgments of the administrators, which courts are reluctant to interfere with regardless. Middleton J noted that any affected party could challenge the outcome of any process at the second meeting of creditors should the DOCA be approved.

Given that the administrators' report to the creditors would include the rival DOCA put forward by the applicants, Middleton J did not find it appropriate to compel the administrators to go further than the obligations imposed upon them already. Likewise, an independent facilitator was deemed unnecessary given Middleton J's confidence that the administrators would fully report to the creditors in compliance with their statutory and general law obligations, affording the applicants and the other creditors access to sufficient information for the purposes of the second meeting of the creditors. Appointing a facilitator was further seen as involving unnecessary costs to the creditors and disruption to the administrators' preparation of their report for the meeting.

6.11 Ode to a dying corporation

Bell Group (UK) Holdings Ltd (in liquidation) [2020] WASC 347 (22 September 2020) Supreme Court of Western Australia, Sanderson M

Note from the editor: Occasionally there are judgments that are particularly interesting to read. Here is one - a brief judgment of nine paragraphs of Master Sanderson of the Supreme Court of Western Australia dealing with one of the longest pieces of litigation of which we are aware. The 404 day trial that Master Sanderson refers to was before Justice Owen and the 2,643 page judgment of Justice Owen was [*The Bell Group Ltd (in liq) v Westpac Banking Corporation (No 9)* [2008] WASC 239]. The background to the litigation was summarised by Justice Owen in the opening paragraphs of his 2008 judgment:

- "the Bell group of companies had a splendid radiance in the commercial life of Australia during the 1970s and early to mid-1980s. The group also had aspirations to international prominence. It was a favourite of the stock market and had accumulated (at least on paper) a relative fortune. But as the Bard so wisely remarked: "You fools of fortune, trencher-friends, time flies". By the early 1990s fortune, friends and time had flown. This litigation is a result. It is a dispute of Brobdingnagian proportions that emerges wraith like from the still-smoking ashes of the late 1980s: an unfortunate period in this State's business and political history";
- "in 1988 and 1989, as the Bell star waned, the group's bankers became increasingly concerned about their exposure to the companies. Early in 1990, the banks took security over assets of group entities to support existing borrowings of some of those companies. In 1991 the companies were placed in receivership or liquidation. The banks realised on their securities. The liquidators raised concerns about the way in which the securities were given and taken. In 1995 they commenced this litigation seeking recovery of the proceeds of realisation and consequential relief"; and
- "the plaintiffs contend that, at the time the parties entered into the refinancing transactions (including the securities), the main companies in the group were insolvent. In the circumstances, the directors breached their duties to the companies by causing them to enter into the transactions. The plaintiffs say the banks are liable because (among other things) they knowingly assisted the directors to breach their duties, they knowingly received property arising from the breach of duties and they perpetrated an equitable fraud on the companies and their creditors. The banks deny all liability".

It is worth recalling the final few paragraphs of Justice Owen's very lengthy 2008 judgment:

- "9759 I am not so naïve as to believe that the handing down of these reasons will mark the end of the litigation. But stranger things have happened. It is still not too late for the parties to put an end to this saga by a negotiated settlement, guided (perhaps) by the findings I have made. If formal judgment is never entered, or if there is a consent judgment on negotiated terms (whether or not they accord with what is contained in these reasons) I will be the last person to complain";
- "9760 whatever the parties decide to do from here, my role in the litigation will come to an end in the near future. Selfish though it may seem, for me that is the primary concern. I will try to engender sympathy for those who come after me, but I make no promises";
- "9761 from time to time during the last five years I felt as if I were confined to an oubliette. There were occasions on which I thought the task of completing this case might be sempiternal. Fortunately, I have not yet been called upon to confront the infinite and, better still, a nepenthe beckons. Part of the nepenthe (which may even bear that name) is likely to involve a yeast-based substance. It will most certainly involve a complete avoidance of making decisions and writing judgments"; and
- "9762 for the moment, in the words of Ovid (with an embellishment from the old Latin Mass): Iamque opus exegi, Deo gratias.[dxxvii]".

Here is the nine paragraph 2020 judgment of Master Sanderson:

- "these reasons are not so much a judgment as a requiem";

- "this was an application to terminate the winding up by Bell Group (UK) Holdings Ltd (In liq) (the company) of Western Interstate Pty Ltd. This was one of a group of companies around which what is known as the "Bell litigation" swirled for 25 years";
- "thousands of people worked on this case. Most have put the experience behind them and moved on; many, shattered by the experience, have retired; more than a few have gone mad. Now the guns have fallen silent. The smell of cordite, gun powder and napalm no longer fills the air. The dead and wounded have been removed from the battle field. The victors have divided the spoils and departed";
- "the trial involving this company, and others, lasted for 404 days between July 2003 and September 2006. The judgment took two years and ran to 2,643 pages. The trial judge was Justice Neville Owen. No Australian judge before or since could have handled the case better than his Honour. Anyone who dips into the judgment - and I do not for a moment suggest anyone should read it in its entirety - will be struck by the detailed consideration of the evidence, the careful balancing of the issues and the clear exposition of a difficult area of the law";
- "the defendants in the action were a group of banks. At first instance they were held liable. They appealed. Not only did they lose the appeal, they lost the cross-appeal and the amount of damages was increased. The banks made an application for special leave to appeal to the High Court. Astonishingly, they were successful. At this point even the bare-knuckled litigators were exhausted. The action was settled. More than a billion dollars was to be divided between the plaintiffs";
- "the plaintiffs then set to squabbling among themselves. For years they had an uneasy relationship with one another but were united against a common foe. Now the prospect of vast riches proved too much. The relationship rapidly became poisonous. Years passed and no resolution proved possible. The battle lines were drawn. The State government attempted to resolve the matter by effectively confiscating the proceeds of the case and paying to each of the parties what they deemed to be a fair entitlement. This strategy failed spectacularly - the legislation was struck down by the High Court. At a directions hearing, not long after the High Court decision, I was told by counsel they anticipated the trial of the issues between the plaintiffs would take longer to hear than the original case. A date was set for trial. Then someone blinked. Further negotiations took place. Mercifully, the matter settled";
- "over the years, I dealt with the case on more than a dozen occasions. Most of these hearings were for judicial directions. It was clear there existed between counsel a mutual loathing. That was probably due to frustration - not only frustration with the glacial progress of the case, but frustration with the clients. Occasionally, agreement was reached - the time of the day, the day of the week - but agreement was otherwise rare. Invariably, the liquidator was represented by Vaughan SC (as his Honour then was). There were times when I thought even his sphinxlike visage would crack. But somehow, the matter edged forward. Now it is settled and it remained for me to give this, and other companies in the group, a decent burial";
- "it was tempting to drive a wooden stake through the heart of the company to ensure it does not rise zombie-like from the grave. As an alternative, I considered ordering the files be removed to a secure facility in Roswell and marked: "Never to be opened". In the end, trusting in divine providence, I made the following orders":
    - the applicant have leave to discontinue the winding up application;
    - The applicant's winding up application is hereby dismissed;
    - There be no orders as to costs as to the winding up application.
- "Amen".

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