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Recent developments in Corporations Law

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A Judge of the Supreme Court of New South Wales

Introduction

This note reviews recent developments in the corporations law, some in 2014 and some in the first half of 2015.

I first consider an appellate and a first instance decision dealing with liability for knowing involvement in a breach of fiduciary duty, an important appellate decision dealing with the application of deeds of indemnity in favour of directors and officers in respect of the costs of criminal proceedings, and two cases dealing with termination payments to company officers. I will also note a recent decision dealing with the requisition of shareholder meetings, in the particular context of capital reductions.

I then consider several recent decisions in respect of insolvency, including two first instance decisions concerning the transfer of shares by a deed administrator; appellate decisions relating to verification of and setting aside creditor's statutory demands; a decision of the High Court concerning the scope of a liquidator's equitable lien; an appellate decision taking a broad view of the provisions dealing with unreasonable director-related transactions in insolvency; and decisions of the Court of Appeal of the Supreme Court of New South Wales and the High Court dealing with extensions of time for a liquidator to bring proceedings under s 588FF of the *Corporations Act* 2001 (Cth).

I also note two decisions of the High Court dealing with managed investment schemes and further decisions dealing with continuous disclosure, indirect causation in continuous disclosure and misleading disclosure claims, and a decision of the High Court, concerning the complex proportionate liability regime under Pt 7.10 Div 2A of the *Corporations Act*. I finally note further developments in financial services regulation, including in respect of the Future of Financial Advice regime under Pt 7.7A of the *Corporations Act* and the possibility of further reforms arising from the 2014 Financial System Inquiry (Murray Inquiry) and the Senate Economics Committee's inquiry into the performance of the Australian Securities & Investments Commission ("ASIC").

Directors and officers

Liability for knowing involvement in a breach of fiduciary duty

A person may be held liable for knowingly assisting in a breach of fiduciary duty, where that breach can be characterised as amounting to a "dishonest and fraudulent design" on the part of the company. This liability involves the application of the second limb in *Barnes v Addy* (1874) LR 9 Ch App 244 at 251-252; (1874) 43 LJ Ch 513, referring to knowingly assisting a trustee in a dishonest and fraudulent design. The matters that are required to establish the element of a "dishonest and fraudulent design" have been formulated in different terms in recent cases. In *Farah*

Constructions Pty Ltd v Say-Dee Pty Ltd (2007) 230 CLR 89; [2007] HCA 22, the High Court observed (at [179]) that *Consul Developments Pty Ltd v DPC Estates Pty Ltd* (1975) 132 CLR 373 established a requirement that any breach of trust or breach of fiduciary duty relied on to establish liability for knowing assistance must be dishonest and fraudulent, so that the impugned conduct must involve circumstances attracting a degree of opprobrium beyond an innocent breach of trust or duty (at [183]). At first instance in *The Bell Group Ltd (in liq) v Westpac Banking Corporation (No 9)* (2008) 39 WAR 1; 70 ACSR 1; [2008] WASC 239, Owen J followed *Farah Constructions* in holding that the plaintiff could not establish liability under the second limb of *Barnes v Addy* where the plaintiff had not sought to establish that a breach of fiduciary duty by the relevant directors involved a higher degree of wrongdoing than a simple breach of trust or fiduciary duty. On appeal in *Westpac Banking Corporation v The Bell Group Ltd (in liq) (No 3)* (2012) 44 WAR 1; 89 ACSR 1; [2012] WASCA 157, the majority reversed that finding. Drummond AJA (at [2112]-[2113], [2117]) (with whom Lee AJA agreed at [1099]) held that liability could be established if the breach of duty was more than trivial and too serious to be excusable on the basis that the fiduciary had acted honestly, reasonably and ought fairly to be excused under provisions such as s 1318 of the *Corporations Act*.

This nature of the conduct that could support a claim in knowing assistance was considered by the Court of Appeal of the Supreme Court of New South Wales in *Hasler v Singtel Optus Pty Ltd* (2014) 311 ALR 494; 101 ACSR 167; [2014] NSWCA 266. In that case, an executive of Optus, Mr Curtis, established a company that provided warehousing services to Optus, brokered through another company which charged a mark-up on those services. A former employee of Optus, Mr Hasler, managed the warehousing company’s day-to-day operations. Optus brought a claim for equitable compensation against Mr Curtis and also brought a claim against Mr Hasler on the basis that he was knowingly involved in Mr Curtis’ dishonest and fraudulent design. Leeming JA indicated his disagreement with the view expressed by Drummond AJA in *Bell Group* that it was sufficient to establish liability for knowing involvement if a breach was more than trivial and too serious to be excusable on the basis that the fiduciary had acted honestly, reasonably and ought fairly to be excused. His Honour also held that a party bringing a claim for knowing assistance did not need to exclude the possibility that the principal had not ratified the breach or given informed consent to it, and that the onus of establishing that matter rested on a defendant. Gleeson JA agreed with the observations of Leeming JA and expressed the view that the reasoning in *Bell Group* was plainly wrong, so far as it treated *Farah Constructions* as expanding the concept of a dishonest and fraudulent design to include all breaches of duty more serious than a trivial breach and not excusable by statute. Barrett JA did not express a view as to the correctness of the approach in *Bell Group.*

These issues have again been considered by Jackson J in *Sino Iron Pty Ltd v Palmer* [2015] QSC 94, although a claim for knowing assistance in a breach of trust failed in that case because the relevant contractual arrangements were not found to give rise to a trust. Jackson J referred to earlier authority suggesting that such a claim could be established if the defendant knew the facts as to the basis on which the relevant funds were held, and did not require that he or she knew that they were held on trust, and his Honour took the same view (at [143]ff). His Honour also noted

(at [117]ff) the circumstances in which a party may be held liable for procuring or inducing a breach of trust, as an alternative to a claim for knowing assistance.[1]

Indemnification of company officers for costs of criminal proceedings

Section 199A(3) of the *Corporations Act* relevantly provides that a company must not indemnify a person against legal costs incurred in defending an action for liability incurred as an officer or auditor of the company if the costs are incurred in defending or resisting criminal proceedings in which the person is found guilty. Section 212 of the *Corporations Act* permits a company to make a loan or advance to a director in respect of legal costs as long as it is reasonable to give the benefit in the circumstances and the director is required to pay back any amounts advanced if he or she is found guilty in subsequent proceedings so the amounts could not be the subject of indemnity under s 199A of the *Corporations Act*. In *Rickus v Motor Trades Association of Australia Superannuation Fund Pty Ltd* (2010) 265 ALR 112 at 118–119; [2010] FCAFC 16, the Full Court of the Federal Court held that the prohibition in s 199A(3)(a) on indemnifying a person for his or her legal costs in defending or resisting proceedings in which he or she is found to have a liability applied only if a person was found liable in the particular proceedings in respect of which the claim for indemnity was made, and held that a deed of indemnity in favour of a director gave rise to a present entitlement to indemnity up to the time that any adverse finding was made in those proceedings.

The scope of s 199A was again considered in *Leckenby v Note Printing Australia Ltd* (2014) 291 FLR 32; [2014] VSC 538 (Sifris J) and on appeal as *Note Printing Australia Ltd v Leckenby* [2015] VSCA 105. The former chief executive officer of the company, Mr Leckenby and others had been charged with conspiring to bribe foreign officials to secure contracts for the company. Mr Leckenby sought indemnification for legal costs incurred in the criminal proceedings from the company, under a deed of indemnity given by the company. The relevant deed was in a common form and provided for the company to indemnify an officer for legal costs and expenses which he or she incurred or for which he or she was liable in defending an action for a liability incurred as an officer of the company. Mr Leckenby contended that indemnity was available prior to a verdict as to his guilt or innocence and the company contended that it was only available if he were found not guilty in the criminal proceedings, that is, after the determination of those proceedings.

At first instance, Sifris J noted that s 199A(3) did not expressly deal with the position where payment was made prior to a verdict in the criminal proceedings, but held the section was not contravened where the deed provided for repayment if there was a guilty verdict, and the deed of indemnity should be read as permitting indemnity prior to the determination of the criminal proceedings. An appeal was dismissed by the Court of Appeal of the Supreme Court of Victoria. Tate JA (with whom Whelan and Ferguson JJA agreed) observed (at [39]–[40]) that s 199A(3)(b) and the corresponding provision in the deed of indemnity was expressed in the future perfect tense, and was directed to whether there was a future finding of guilt, so that the obligation to indemnify subsisted until a finding of guilt occurred. Her Honour noted that that reading of s 199A(3)(b) was consistent with the decision of the Full Federal

[1] See also the discussion of this claim in *Farah Constructions Pty Ltd v Say-Dee Pty Ltd* (2007) 230 CLR 89 at [161]; *Australian Super Developments Pty Ltd v Marriner* [2014] VSC 464 at [301]ff.

Court in *Rickus v Motor Trades Association of Australia Superannuation Fund Pty Ltd* above. Her Honour also noted (at [52]) that that interpretation of s 199A(3)(b) was supported by a comparison of the words of the section with its predecessor, s 241 of the *Corporations Law.* Tate JA also held (at [59]) that the provision in the relevant deed should be construed consistently with s 199A(3)(b) as conferring a present entitlement upon Mr Leckenby to an indemnity for legal costs and expenses incurred up and until and unless, in the future, he is found guilty. Her Honour summarised the position (at [60]) as that:

> "What s 199A(3)(b) prohibits is an indemnity that holds the promisee harmless against loss despite the promisee having been found guilty of a criminal offence; it does not prohibit an entitlement to be indemnified against legal costs incurred in defending or resisting criminal proceedings until verdict which determines whether or not the promisee is entitled to the benefit of the indemnity permanently."

That decision is likely to be of general application since there is a substantial degree of uniformity in the manner in which such deeds are drafted.

Termination benefits under Pt 2D.2 of the Corporations Act

Part 2D.2 Div 2 of the *Corporations Act* deals with termination payments to directors of listed companies, executives named in the company's remuneration report and directors of private companies including subsidiaries of listed companies. Section 200B prohibits the company, or an associate of the company (other than a related body corporate that is itself a company) or a prescribed superannuation fund in relation to the company giving a benefit in connection with a person's retirement from an office or position of employment in a company or related body corporate if that office or position is a managerial or executive office (as defined) or the retiree has held a managerial or executive office in the company or a related body corporate in the 3 years before his or her retirement, unless member approval is given under s 200E of the *Corporations Act*, or the benefit is within the exceptions in ss 200F, 200G and 200H of the *Act*.

The present form of these provisions was introduced by the *Corporations Amendment (Improving Accountability on Termination Payments) Act* 2009 and applies in relation to a retirement from office, or a position of employment, held under an agreement, inter alia, entered into, renewed, extended, or where there was a variation of a condition of the agreement, on or after the commencement of Pt 1 of the Amending Act, 24 November 2009. The effect of the provision was summarised by Brereton J in *Re Cummings Engineering Holdings Pty Ltd* [2014] NSWSC 250 at [36] as that the former, and higher, limit for such benefits continues to apply in respect of employment under contracts made before, and not renewed, extended or materially varied since 24 November 2009. His Honour also there noted (at [37]) that directors remain subject to their duties in respect of a decision whether to make a payment to a director, even if the relevant provisions do not apply because the benefit is not given in connection with a retirement from office or position, or an exception under s 200F applies or the payment is permissible under s 200G.

The scope of the provisions was again considered by the Full Court of the Federal Court in *Renshaw v Queensland Mining Corp Ltd* (2014) 103 ACSR 358; [2014] FCAFC 172. The Full Court noted (at [29]) that the purpose of Pt 2D.2 Div 2 was to

bring transparency to "golden handshakes" that involved significant expenditures of a company's money in connection with the cessation of employment or a services relationship of senior officeholders or employees and (at [30]) that the word "benefit" and the phrase "in connection with" in Pt 2D.2 Div 2 should be given a broad construction reflecting Parliament's intention to:

> "create a broad nexus between the benefit concerned and the cessation of the person's relationship with the company so as to protect the rights and interests of its shareholders to know of, and approve, the expenditure of the company's money."

The Full Court held that the connection required by s 200B was established by the commercial substance of the execution of a deed, a payment and the contemporaneous resignation of the director in that case, and it was sufficient to establish that connection that the director would not have entered into the resignation without payment, irrespective of whether the payment related to the company's obligation to engage him for a specified period under a separate agreement. The Court also observed (at [31]) that a direct link between the director ceasing work and the benefit was not required, although it was established in that case.

Shareholders meetings and reductions of share capital

Section 256B of the *Corporations Act,* introduced by the *Company Law Review Act* 1998, provides that a company may reduce its share capital in a way that is not otherwise authorised by the law if that reduction is fair and reasonable to the company's shareholders as a whole; does not materially prejudice the company's ability to pay creditors; and is approved by shareholders under s 256C of the *Corporations Act*. Section 256C of the *Corporations Act* provides for information to be provided to shareholders and for approval of the proposed reduction in general meeting.

These provisions were recently considered in *Re Molopo Energy Ltd* (2014) 104 ACSR 46; [2014] NSWSC 1864, where a substantial shareholder in that company sought to require its directors to convene a general meeting to consider a resolution amending the company's constitution to authorise shareholders to reduce the company's capital. At that time, proceedings claiming substantial damages had been commenced against the company and a subsidiary in Canada. White J held that a proposal for reduction of the company's share capital could only be initiated by directors, since allowing shareholders an unqualified power to initiate a reduction of capital would lessen the protection otherwise available to creditors. His Honour noted (at [72]–[74]) that shareholders' interests and creditors' interests were likely to be opposed in that situation and that:

> "Where the decision to effect a reduction lies with the directors, subject to shareholder approval, creditors are at least protected by sanctions that could be available against directors if the reduction materially prejudiced the company's ability to pay its creditors."

His Honour also noted that protection would be lost if such a reduction could be made in a general meeting and held (at [77]) that shareholders' function was limited to approving but not initiating such a resolution. His Honour also noted that the

proposed resolution would not satisfy the requirements of s 256B of the *Corporations Act* if the capital reduction *might* materially prejudice the company's ability to pay creditors, not only if it was certain to do so.

The conclusion reached by White J is arguably supported, first, by the use of the word "approve" in s 256B of the *Corporations Act*, which appears to contemplate that a proposal formulated by others will be put to shareholders for approval; and, second, by the interaction between s 256B and the liability imposed upon directors under s 588G of the *Corporations Act* if a reduction of capital is made in contravention of s 256B. It would be manifestly unfair to directors if they were potentially held liable under that section for a reduction of capital that they had not initiated and could not prevent; but, if directors would not be held liable under that section where a general meeting initiates the relevant capital reduction, then a significant protection for creditors in respect of such capital reductions would not apply, and no corresponding liability is imposed on shareholders.

Insolvency

Transfer of shares by a deed administrator

Section 444GA of the *Corporations Act* permits a deed administrator to transfer shares in a company that is subject to a deed of company arrangement with the consent of the owner of those shares, or with the Court's leave, and provides that the Court may only grant such leave if it is satisfied that the transfer would not "unfairly prejudice" the interests of members of the company. The authorities indicate that whether there is prejudice, and unfair prejudice, to shareholders is to be determined, inter alia, by reference to whether the shares would have value in a liquidation of the company.[2] In *Re Mirabela Nickel Ltd (subject to deed of company arrangement)* [2014] NSWSC 836, which was an uncontested application under this section relating to shares in a listed company, the Supreme Court of New South Wales similarly held that the question of unfair prejudice depended on the value of the shares in a liquidation scenario, at least if winding up was a likely or necessary consequence of the transfer of shares not being approved, and that members did not suffer prejudice if the shares would have no residual value and the members were unlikely to receive a distribution in a winding up.

In *Re Nexus Energy Limited (subject to deed of company arrangement)* (2015) 105 ACSR 246; [2014] NSWSC 1910,[3] the Court determined a second case involving shares in a listed company, where that application was opposed by shareholders. By way of background, Nexus Energy Limited had fallen into financial difficulty, and a subsidiary of Seven Group Holdings ("SGH") proposed a scheme of arrangement which provided for the acquisition of shares in Nexus Energy at 2¢ per share, which did not achieve the necessary majority to proceed. Another subsidiary of SGH provided bridging finance to Nexus Energy in connection with that proposed scheme of arrangement and interests associated with SGH also acquired the senior debt of Nexus Energy and more than two-thirds of unsecured notes issued by Nexus Energy. Nexus Energy was then placed in administration by its directors after the scheme of arrangement was not approved. The administrators solicited proposals to

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[2] *Weaver v Noble Resources Ltd* (2010) 41 WAR 301; (2010) 79 ACSR 237; [2010] WASC 182.
[3] For commentary, see P Pan, "Unfair prejudice and value breaks in corporate insolvency" (2015) *Insolvency law Bulletin* 58.

acquire its assets and a subsidiary of SGH proposed a deed of company arrangement that provided for repayment of the senior debt (owed to its associated entity) in full, payment of $30m to settle a third party litigation claim, payment of 74.5¢ in the dollar for unsecured noteholders and payment of unsecured creditors in full through a creditors' trust, subject to the Court granting leave under s 444GA for the transfer of shares in Nexus Energy to that subsidiary and relief from the applicable takeover provisions under Chapter 6 given by the ASIC. The decision in Nexus involved the additional complexity that, although the listed parent company was subject to the deed of company arrangement, the financing arrangements ensured the continued solvency of the operating subsidiaries, at least while those arrangements were in place.

The trial judge accepted expert evidence led by the deed administrators that Nexus Energy's liabilities substantially exceeded its assets and its shares had no value. The trial judge did not accept that it was sufficient to establish value in the shares, or prejudice to shareholders by an order for their transfer, that SGH might make a more favourable offer if the application under s 444GA of the *Corporations Act* was refused, where it was at least equally possible that a receiver would then be appointed and a forced sale of the company's assets would occur, with no recoveries for shareholders and a substantial loss of value for creditors. The trial judge also held that any loss of opportunity by the shareholders to require SGH to negotiate with them or decline to transfer their shares unless their expectations were met was not prejudice or unfair prejudice for the purposes of the section. The transfer of the shares was therefore approved.

That decision was in turn referred to by Sifris J in *Re 3GS Holdings Pty Ltd (subject to DOCA)* [2015] VSC 145 where his Honour noted (at [14]) that the relevant question was whether the shares to be transferred had a residual value if the transfer was not approved and (at [22]) that no unfair prejudice to shareholders arose from a transfer of shares to a third party if it was unlikely that those shares would support a dividend to shareholders or contributories in any scenario.

Form of affidavit verifying a creditor's statutory demand

The question of the form of an affidavit verifying a creditor's statutory demand has been the subject of further appellate authority. Section 459E of the *Corporations Act* provides that a statutory demand may be served on a company relating to a debt or debts that is or are due and payable, the total amount of which is at least the statutory minimum. Unless the debt to which a statutory demand relates is a judgment debt, the demand must be accompanied by an affidavit that verifies that the debt is due and payable by the company and which complies with the Harmonised Corporations Rules of the State Supreme Courts and the Federal Court of Australia. In *Kisimul Holdings Pty Ltd v Clear Position Pty Ltd* [2014] NSWCA 262, the Court of Appeal of the Supreme Court of New South Wales took the same approach as the Court of Appeal of the Western Australian Supreme Court in *Wildtown Holdings Pty Ltd v Rural Traders Co Ltd* (2002) 172 FLR 35; [2002] WASCA 196 and held that the omission from an affidavit verifying a creditor's statutory demand, of a statement that the deponent believed there was no genuine dispute about the existence or amount of the debt, constituted some other reason why the demand should be set aside for the purposes of s 459J(1)(b) of the *Corporations Act*. Barrett JA (with whom Beazley P and Gleeson JA agreed)

emphasised the importance of the requirement for such a statement in directing the creditor's attention to the requirement that only an undisputed debt should be made the subject of a statutory demand, as well as informing the company served with the demand of the creditor's belief that the debt was undisputed.

Whether a genuine dispute or offsetting claim is established

The Court of Appeal delivered an important decision in respect of the test for setting aside a creditor's statutory demand by reason of a genuine dispute or offsetting claim in *Britten-Norman Pty Ltd v Analysis and Technology Australia Pty Ltd* (2013) 85 NSWLR 601; [2013] NSWCA 344. That decision refers to well-established authorities but is also receiving significant attention in recent cases.[4] The Court of Appeal there noted at [30] that:

> "It is settled law that s 459H requires the court to be satisfied that there is a 'serious question to be tried': see *Scanhill v Century 21 Australasia* at 467, or 'an issue deserving of a hearing' as to whether the company has such a claim against the creditor: see *Chase Manhattan Bank Australia Ltd v Oscty Pty Ltd* [1995] FCA 1208; 17 ACSR 128 at [42] per Lindgren J; *Eumina Investments Pty Ltd v Westpac Banking Corp* [1998] FCA 824 ; 84 FCR 454 per Emmett J (as his Honour then was). The claim must be made in good faith: *Macleay Nominees v Belle Property East Pty Ltd*. In that case, Palmer J observed, at [18], that good faith, in this context, meant that the offsetting claim was arguable on the basis of facts that were asserted 'with sufficient particularity to enable the court to determine that the claim is not fanciful'".

The Court of Appeal also observed (at [36]) that there must, relevantly, be evidence that satisfies the Court that there is a "serious question to be tried" or "an issue deserving of a hearing" or a "plausible contention requiring investigation" of the existence of an offsetting claim and that:

> "… evidence sufficient to satisfy this test, given the time period in which the affidavit must be filed, cannot and need not conclusively prove the claim or otherwise be incontrovertible or substantially non-contestable."

The Court of Appeal also observed (at [46]) that:

> "In determining whether there is evidence of a genuine dispute as to the debt, or that there is an offsetting claim, except in extreme cases, the Court is not concerned to engage in an inquiry as to the credit of the deponent of the affidavit filed in support of the application."

At the same time, the Court of Appeal referred to *Eyota Pty Ltd v Hanave Pty Ltd* (1994) 12 ACSR 785 and recognised that the Court is not required to accept uncritically every statement in an affidavit, where it is inconsistent with undisputed contemporary documents, inherently improbable, does not have sufficient prima

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[4] See, for example, *Re AP & HR Investments Pty Ltd* [2013] NSWSC 1989; *Pravenkav Group Pty Ltd v Diploma Construction (WA) Pty Ltd (No 3)* [2014] WASCA 132; (2014) 46 WAR 483; *Hallinan & Co Pty Ltd v A&B Cotton Pty Ltd* [2014] QSC 112; *Re Diveva Pty Limited* [2015] NSWSC 509; *Re Sinadios Haulage Pty Ltd* [2015] NSWSC 596; *Re Tuffrock Pty Ltd* [2015] NSWSC 738; and for commentary see M Bianca & J Hidayat, "Requirements Eased to Set Aside Statutory Demands" (2014) 52(3) *LSJ* 44.

facie plausibility to merit further investigation or is an assertion of facts unsupported by evidence. The Court of Appeal summarised the position (at [47]) as being that the Court's role is:

> "to determine whether there was plausible evidence to establish the existence of a genuine dispute [or offsetting claim], not whether the evidence was disputed or even likely to be accepted on a final hearing of any such claim."

The Court of Appeal also did not accept that inconsistent contemporaneous documents were sufficient to displace an offsetting claim, notwithstanding that they might pose "difficulties for the ultimate proof of the claim" (at [70]), and gave little weight (at [80]) to the absence of documents that might support a claim for loss of profit, although it held that an offsetting claim for loss of profits was not established in that case where essential integers in the calculation of lost profits had not been established.

The decision in *Britten-Norman* will be of particular importance where, for example, a director or officer of the company on which a demand was served leads affidavit evidence, in support of an application to set aside the demand, alleging an oral representation by the creditor that might support a genuine dispute or offsetting claim. On the other hand, in *Re Diveva Pty Limited* [2015] NSWSC 509 at [26], I observed that:

> "I do not understand the Court of Appeal's approach in *Britten-Norman* above to require the Court to eschew any evaluative exercise as to whether there is a plausible basis for an offsetting claim, where such an evaluation is contemplated by the earlier cases to which they refer, and seems to me to be necessarily required by any determination of whether there is a serious question to be tried, an issue deserving of a hearing, or a plausible contention requiring investigation."

In *Britten-Norman*, the Court of Appeal also gave weight to the absence of cross-examination to challenge the evidence led in support of the offsetting claim. As a result, Courts at first instance may now more readily permit at least limited cross-examination in genuine dispute and offsetting claim cases than had previously been the case: *Re Diveva Pty Ltd* [2015] NSWSC 794.

Liquidator's equitable lien

The scope of a liquidator's equitable lien for costs of litigation was considered by the High Court of Australia in 2014. The principle in *Re Universal Distributing Co Ltd (in liq)* (1933) 48 CLR 171; [1933] HCA 2 is usually taken as having the effect that a secured creditor may not take the benefit of a fund created by the liquidator's efforts in a company's winding up without meeting the liquidator's costs and expenses, including remuneration, of creating that fund, and that the liquidator has a charge over the fund in priority to the secured creditor's claim to secure that result.

In *Stewart (in his capacity as liquidator of Newtronic Pty Ltd (in liq)) v Atco Controls Pty Ltd (in liq)* (2014) 307 ALR 562; 88 ALJR 594; 98 ACSR 601; [2014] HCA 15, the High Court considered the circumstances in which a liquidator's equitable lien would be available over a settlement amount in liquidation. In that case, a liquidator had received an amount by way of settlement of a claim brought against receivers

appointed to the company's assets, and paid that amount to an unsecured creditor as reimbursement of funding for the conduct of the proceedings. A secured creditor, Atco, which was also a defendant in the proceedings, claimed to be entitled to payment of those monies on the basis that they were an asset of the company and subject to its security. The liquidator resisted the claim for payment on the basis that he had an equitable lien to secure his costs of the proceedings which was a prior claim over the monies received in settlement of the proceedings. At first instance, the Supreme Court of Victoria held that the principle in *Universal Distributing* applied to the amount recovered by the liquidator in the litigation. The Court of Appeal of the Supreme Court of Victoria held that an equitable lien had not arisen, where the liquidator was acting in the interests of an unsecured creditor and against the secured creditor's, Atco's, interests in bringing the proceedings. The Court of Appeal held that it was not unconscientious of Atco to claim the settlement sum, notwithstanding the costs incurred by the liquidator in recovering it and, conversely, it would be unconscientious for the liquidator to retain the fund on the basis of the claimed equitable lien.

The High Court observed that that principle in *Re Universal Distributing* applies where an insolvent company is in liquidation; the liquidator has incurred expenses and rendered services in the realisation of an asset; the resulting fund is insufficient to meet both the liquidator's costs and expenses of realisation and the debt due to the secured creditor; and the creditor claims the fund. Their Honours noted that the application of the principle avoids the result that a secured creditor would unconscientiously take the benefit of the liquidator's work without the liquidator's expenses being met. Their Honours held that that principle was not displaced by the matters to which the Court of Appeal had referred, observing that a liquidator's duty was owed to the body of creditors as a whole and to the Court and the liquidator had the power to bring proceedings in order to realise the company's assets, and that the availability of a lien was not affected by the facts that the particular proceedings could be said to be in an unsecured creditor's commercial interests or that that unsecured creditor had indemnified the liquidator, or that the proceedings were contrary to a secured creditor's interests. The Court held (at [41]) that such a lien arose simply from the fact that the liquidator's costs and remuneration were incurred in realising the assets that created the relevant fund.

Voidable transactions

Unreasonable director-related transactions

An intermediate appellate court has also recently considered the scope of s 588FDA of the *Corporations Act* which deals with unreasonable director-related transactions. That section applies in respect of payments made by a company, a conveyance, transfer or other disposition by the company of its property, the issue of securities by a company or its incurring an obligation to make such a payment, disposition or issue of securities, if that payment, disposition or issue of securities is made to a director of the company, close associate of a director of the company, or a person on behalf of either the director or his or her close associate. Transactions between a company on the one hand, and a director or his or her close associate on the other, are treated as voidable on a winding up of the company if they occur in circumstances where a reasonable person in the company's circumstances would not have entered into the transaction. Earlier authority indicated that the section did

not extend to a dealing with a company or trust where a director or his or her "close associate" was a shareholder or beneficiary of that entity.[5]

The Court of Appeal of the Supreme Court of Victoria took a broader view of the section in *Vasudevan v Becon Constructions Australia Pty Ltd* (2014) 97 ACSR 627; [2014] VSCA 14. In that case, two companies owed debts to a construction company and the sole director and shareholder of the two companies had guaranteed the debts. The construction company instituted proceedings against the guarantor and the two companies entered into an arrangement to restructure the debts so that a third company would become liable for one of the company's debts and would execute a mortgage in the construction company's favour as security under the deed, and the third party would discontinue the proceedings against the director and release him from liability. A liquidator who was ultimately appointed to the third company contended that the obligations assumed by that company under the restructuring and the disposition of property under the relevant mortgage were undertaken for the director's benefit and were voidable under s 588FDA of the *Corporations Act*. That claim was dismissed at first instance, on the basis that the director had not received a direct benefit from the transaction.

On appeal, Nettle JA (as his Honour then was) (with whom Beach JA and McMillan AJA agreed) held that the director had obtained a direct benefit from the transaction, by being relieved of his obligations to the third party as guarantor, but also took a broader view of the section, observing (at [19]) that the section was an "anti-avoidance provision aimed at preventing errant directors from stripping benefits out of companies to their own advantage" and that, in its ordinary usage, such benefits include both direct and indirect benefits, and that that construction would accord with the apparent objective of the section. The Court of Appeal also held that the section extended to financial benefits, including a company incurring an obligation to a third party in order to relieve a director of his obligations to the third party. The Court also observed (at [26]) that a disposition may be "for the benefit of" a director where it "legally or financially advantages the director in question regardless of whether it is paid or directed to a close associate of the director"; and (at [28]) that the purpose of the section is "to catch director-related transactions of kinds not otherwise liable to avoidance as unfair preferences, uncommercial transactions or unfair loans".

Extension of time for proceedings brought by a liquidator under s 588FF of the Corporations Act

Section 588FF of the *Corporations* Act specifies the orders that a court may make if a transaction is voidable under s 588FE of the *Corporations* Act, as an insolvent transaction which is an unfair preference (within the scope of s 588FA), an uncommercial transaction of the company (within the scope of s 588FB), an unfair loan to the company (within the scope of s 588FD) or an unreasonable director-related transaction (within the meaning of s 588FDA). An application under this section may be made during the period beginning on the relation-back day (as defined in s 9) and ending on the later of 3 years after the relation-back day or 12 months after the first appointment of a liquidator in relation to the winding up of the

[5] *Ziade Investments Pty Ltd v Welcome Homes Real Estate Pty Ltd* (2006) 57 ACSR 693; [2006] NSWSC 457, aff'd *Welcome Homes Real Estate Pty Ltd v Ziade Investments Pty Ltd (in liq)* [2007] NSWCA 167; *Re Lawrence Waterhouse Pty Ltd (in liq)* [2011] NSWSC 964 at [280]; *Verge v Stinson* [2011] WASC 158; *Re Great Wall Resources Pty Ltd (in liq)* [2013] NSWSC 354.

company (s 588FF(3)(a)) or within such longer period as the court orders on an application by the liquidator brought within that period (s 588FF(3)(b)).[6]

A power to make "shelf orders", which extend the time for a liquidator to bring proceedings in relation to voidable transactions that are not identified at the relevant time, has been recognised at least since *BP Australia Ltd v Brown* (2003) 58 NSWLR 322; (2003) 46 ACSR 677; [2003] NSWCA 216. The existence of that power was challenged in one of several cases arising out of the liquidation of Octaviar Limited and Octaviar Administration Limited. In that case, the liquidators of two companies in the Octaviar Group had sought a "shelf order" that the time for making applications in respect of those companies under s 588FF(1) of the *Corporations Act* be extended. They had not given notice to the Fortress parties of the application, where they were not then aware of the possibility of a claim against them. The Fortress parties sought to vary or set aside the shelf order so far as it applied to them. They were unsuccessful at first instance and appealed from that decision, contending that the Court of Appeal's earlier decision in *BP v Brown* should be overruled. In *Fortress Credit Corporation (Australia) II Pty Ltd v Fletcher* (2014) 308 ALR 166; 99 ACSR 312; [2014] NSWCA 148, the Court of Appeal of the Supreme Court of New South Wales (constituted by a five judge bench) followed *BP Australia Ltd v Brown* above in upholding the Court's power to make an extension order under s 588FF(3)(b) that does not specifically refer to named parties or transactions in extending the time for the commencement of proceedings under s 588FF(1) of the *Corporations Act*. Bathurst CJ (with whom Beazley P, Macfarlan, Barrett and Gleeson JJA agreed) held that the decision in *BP v Brown* was not plainly wrong and should not be overruled and that, where a party is not a target at the time a shelf order is made, the court has a discretion whether or not to set aside the shelf order as against that party.

The High Court unanimously upheld that approach on appeal in *Fortress Credit Corporation (Australia) II Pty Ltd v Fletcher* (2015) 317 ALR 421; (2015) 89 ALJR 425; [2015] HCA 10; BC201501284. The Court referred to an observation of Spigelman CJ *in BP Australia Ltd v Brown* above that, where a liquidator is still investigating the identity of recipients of benefits under voidable transactions and cannot identify the transactions to be targeted for the Court, the power "should be broad enough to allow … for an order granting an extension of time in general terms" and observed (at [8]) that that view:

> "involved a balancing of the requirements of commercial certainty on the part of those who had past dealings with the Corporation against the conflicting interest of the creditors of the company."

The Court reviewed the legislative history of s 588FF and noted (at [24]) that the function of s 588FF(3)(b) was "to confer a discretion on the Court to mitigate, in an appropriate case, the rigors of the [3 year] time limits". The Court held (at [27]) that the availability of shelf orders was open on the construction of the section, was consistent with the evident purpose of the section, and was supported by the re-enactment of the section in its existing form after the Court of Appeal had decided

[6] *BP Australia Ltd v Brown* (2003) 58 NSWLR 322; 46 ACSR 677; [2003] NSWCA 216; *Tolcher v Capital Finance Australia Ltd* (2005) 143 FCR 300; 52 ACSR 328; [2005] FCA 108; *Australian Securities and Investments Commission v Karl Suleman Enterprizes Pty Ltd (in liq)* (2004) 52 ACSR 103; [2004] NSWSC 1244.

BP Australia Ltd v Brown above. The availability to make such orders has therefore now been confirmed.

The interaction between s 588FF and the Court's procedural rules, including for extensions of time, was considered by the High Court of Australia in another decision arising from the Octaviar liquidation, *Grant Samuel Corporate Finance Pty Ltd v Fletcher* (2015) 317 ALR 301; (2015) 89 ALJR 401; [2015] HCA 8. The liquidator of Octaviar Limited had there initially obtained an extension of the three year period specified in s 588FF(3) to bring recovery proceedings, for a period of six months, and then applied to the Court, within that extended period, for a second extension of six months under s 588FF(3)(b) or a variation of that extension under r 36.16(2)(b) of the Uniform Civil Procedure Rules, which allows the Court to vary an order made in the absence of a party including, perhaps oddly, on the application of the party who had been present and made that application.

On the first application, Ward J (as her Honour then was) held that a second extension of time was not available under s 588FF(3)(b) but varied the period of that extension under UCPR r 36.16(2)(b). The liquidator then commenced preference proceedings against several parties within the further extended six month period and they applied to set aside the order made by Ward J. That application raised questions as to the application of s 79(1) of the *Judiciary Act* 1903 (Cth), which provides that the laws of a State or Territory, including relating to procedure, apply to a Court that is exercising Federal jurisdiction in that State or Territory, except as otherwise provided by the constitution or the laws of the Commonwealth, and as to the extent to which s 588FF of the *Corporations Act* operated as a code so as to exclude procedural rules of the State or Territory. The application to set aside the orders made by Ward J was unsuccessful at first instance and, by majority, in the Court of Appeal. On appeal, the High Court emphasised that the commencement of preference proceedings within the time limit under s 588FF(3), as extended under s 588FF(3)(b) was a precondition to the Court's jurisdiction under s 588FF; approved the observation of Spigelman CJ in *BP v Brown* above that the section contemplated a single determinate extension of time; and held that s 588FF "otherwise provided" for the purposes of s 79 of the *Judiciary Act*, so that an extension of time under that section could not be supplemented or varied by procedural rules of the Court in which the application has been brought.

In a third decision, in *Fletcher v Anderson* (2014) 293 FLR 269; (2014) 103 ACSR 236; [2014] NSWCA 450, the Court of Appeal considered the position in respect of preference claims against the Commissioner of Taxation under s 588FA of the *Corporations Act* and consequential claims to indemnity under s 588FGA of the *Corporations Act*. As I noted above, Ward J had made a shelf order under s 588FF(3) of the *Corporations Act* extending the time for proceedings to be brought in respect of preference and other transactions on the liquidator's application. The liquidator subsequently brought proceedings against the Commissioner of Taxation alleging that a number of payments made to it were unfair preferences under s 588FA of the *Corporations Act* and insolvent transactions under s 588FC of the *Act* and claiming orders under s 588FF of the *Act*. Section 588FGA(2) of the *Act* in turn obliged each director of the company, at the time the relevant payment was made, to indemnify the Commissioner in respect of loss or damage resulting from an order

under s 588FF and s 588FGA(4) allowed the Court to make orders to give effect to that right of indemnity.

On an application to set aside the extension order made by Ward J, Young AJA held that, where a liquidator was contemplating proceedings against the Commissioner of Taxation, the directors who would become subject to the statutory indemnity were directly affected by the proposed action and should have been given notice of the application to extend time, and set aside the order extending time. The Court of Appeal observed that s 588FGA(2) of the *Corporations Act* creates a statutory liability on the part of the director, in respect of the claim against the Commissioner of Taxation, whether or not the Commissioner ultimately brings proceedings to enforce that statutory liability, and also held that directors were immediately affected by the extension order made under s 588FF of the *Corporations Act* and should have been given notice of the application and an opportunity to be heard. However, the result was not that the extension order should necessarily be set aside, but instead that they should be allowed a further opportunity to be heard as to the question whether that order should have been made.

Managed investment schemes

The High Court twice considered issues arising under Ch 5C of the *Corporations Act*, dealing with the regulation of managed investment schemes, in 2014.

The first of those decisions deals with whether units in a managed investment scheme can be redeemed in accordance with their terms of issue, when withdrawals from the scheme are suspended under Pt 5C.6 of the *Corporations Act*. In *MacarthurCook Funds Management Ltd v TFML Ltd* (2014) 308 ALR 202; 88 ALJR 616; [2014] HCA 17, the High Court considered an appeal from the decision of the Court of Appeal of the Supreme Court of New South Wales in respect of a claim by Macarthur Cook Funds Ltd ("MFML") for breach of contract, arising from TFML's failure to redeem units in an unlisted unit trust, which was a registered managed investment scheme under Ch 5C of the *Corporations Act* in accordance with their terms of issue. MFML had subscribed for units in the trust on terms that, subject to compliance with any requirements under the *Corporations Act* and the constitution of the trust, the relevant units must be redeemed by the responsible entity commencing 6 months from the subscription date, using funds received on accepting applications under a public offer. The trust subsequently received such funds from a public offer, but the responsible entity then suspended withdrawals from the trust until further notice, including the redemption of any subscription units, on the basis that the fund was not liquid for the purposes of s 601KA(4) of the *Corporations Act*. TFML, the successor to the responsible entity of the trust, contended that its obligation to redeem the units was qualified by the scheme's constitution and the *Corporations Act*. Relevantly, s 601KA(3) of the *Corporations Act* provides that a responsible entity must not allow a member to withdraw from a scheme, which is not a liquid scheme for the purposes of s 601KA(4) of the *Corporations Act*, other than in accordance with the scheme's constitution and ss 601KB–601KE of the *Corporations Act*. The High Court held that TFML's failure to redeem the units constituted a breach of the terms of issue of the units for which TFML was liable in damages. The Court held that a withdrawal, for the purposes of Pt 5C.6 and s 601GA(4) of the *Corporations Act* involved an "act of volition" on the part of the member and did not

include a compulsory redemptions in accordance with the scheme's constitution or under the terms of issue of a member's units.

The second decision dealt with the powers of a responsible entity to deal with scheme property. Section 601FB(1) of the *Corporations Act* provides for the responsible entity of a registered scheme to operate the scheme and perform the functions conferred on it by the scheme's constitution and the *Corporations Act*. The duties of a responsible entity are set out in s 601FC(1) and the responsible entity holds scheme property on trust for scheme members under s 601FC(2). In *Wellington Capital Ltd v Australian Securities & Investments Commission* [2014] HCA 43, the High Court considered the position where the responsible entity of a managed investment scheme had sold a substantial proportion of the fund's assets to an unlisted public company, in consideration for the transfer of all of the issued shares in that company to the fund, and distributed those shares in specie to the fund's unitholders without their consent.

The plurality of the High Court (French CJ, Crennan, Kiefel and Bell JJ) held that provisions in the scheme's constitution which conferred on the responsible entity the powers that it would have if it were an absolute owner of the scheme property and authorised it to dispose of the scheme property were constrained by the duties imposed on the responsible entity under s 601FC(1) of the *Corporations Act* and the statutory trust under s 601FC(2) of the *Corporations Act*. The plurality held (at [35]) that those provisions were not directed to dealings between the responsible entity and unitholders and did not authorise the transfer of scheme assets to unitholders, where the scheme's constitution made express provision for the payment of cash distributions to unitholders, although not accepting the Full Court's wider observation that trust property could not be transferred to unitholders without their unanimous consent. Gageler J reached the same result in a separate judgment, also observing that the relevant constitutional provisions did not extend to dealings between the responsible entity and unitholders in that capacity.

Continuous disclosure, indirect causation and class actions

Listing Rule 3.1 of the ASX Listing Rules requires a listed entity immediately to notify ASX of any information concerning the entity of which it becomes aware, which a reasonable person would expect to have a material effect on the price or value of the entity's securities. Section 674 of the *Corporations Act* imposes liability on a listed entity if it fails to comply with rule 3.1. The elements of a contravention of that section are that a listed entity has information that rule 3.1 requires it to notify to ASX; that information is not generally available; a reasonable person would expect that information, if it were generally available, to have a material effect on the price or value of securities of the listed entity; and the entity does not notify ASX of that information in accordance with rule 3.1: s 674(2).

In *ASIC v Newcrest Mining Ltd* (2014) 101 ACSR 46; [2014] FCA 698, the Federal Court imposed a substantial pecuniary penalty of $1.2 million for two contraventions of the continuous disclosure regime, involving a failure to notify Australian Securities Exchange Limited of a company's expectation as to its total gold production for the 2014 financial year and of management's expectations as to capital expenditure for that year, in circumstances that confidentiality in that information had been lost by disclosure of it to several analysts and to a conference. Middleton J recognised (at [15] – [17]) that, but for that disclosure, that information may not have been

disclosable, so far as it was generated for internal management purposes, but held that disclosure was required once its confidentiality was lost. The size of the penalty is significant, particularly in circumstances that the disclosure did not involve a deliberate breach of the relevant provisions, but resulted from an erroneous understanding that the information had previously been disclosed. Middleton J noted (at [85]) the need for the penalty to reflect "the importance of a system of continuous disclosure to promote confidence in the integrity of the Australian capital markets" and to "encourage the giving to the market timely indications of corporate performance".

In order to establish a claim for damages[7] under the misleading and deceptive conduct provisions under s 1041H of the *Corporations Act*, or under s 1041E of the *Corporations Act*, which is contravened by deliberate, negligent or reckless conduct that is, for example, materially misleading, a plaintiff must establish that it has suffered loss by the conduct of another person in contravention of the relevant sections. That can be established by proof of individual reliance by security holders. Reliance can also be inferred in an appropriate case, rather than proved by direct evidence of security holders.[8] Plaintiffs in continuous disclosure claims and securities class actions will typically seek to conduct their cases so as to avoid proof of individual reliance, at least for reasons of cost efficiency and possibly also for substantive reasons. In order to do so, plaintiffs typically seek to advance "market-based" or indirect causation cases, arguing that the fact that the other investors constituting the market were misled gave rise to their loss. There is authority, outside the class action context, that suggests that such a case may not be available where the relevant security holder's investment decision is part of the causal chain, without proof of his or her individual reliance on a misrepresentation.[9] The ability to bring such a case in a class action has not yet been the subject of a final decision, where it was squarely in issue, but has recently arisen in two interlocutory judgments and has been addressed by obiter comments in a recent final decision where a claim failed on other grounds.

In *Camping Warehouse Australia Pty Ltd v Downer EDI Ltd* [2014] VSC 357, the Supreme Court of Victoria declined to strike out a claim that did not plead actual reliance by an investor on a company's allegedly misleading or deceptive conduct. Sifris J noted that the question of what was required to establish causation involved matters of some complexity that required comprehensive and detailed analysis and would not desirably be addressed on a strike out application. The Federal Court also declined to strike out such a claim in *Caason Investments Pty Ltd v Cao* (2014) 104 ACSR 67; [2014] FCA 1410, although Farrell J there questioned whether causation

[7] A person who suffers loss as a result of a contravention of the financial services civil penalty provisions, including a contravention of the continuous disclosure obligation under *Corporations Act* s 674, can recover damages under s 1317HA of the *Corporations Act*. A person who suffers loss or damage by conduct of another person in contravention of the prohibition on misleading and deceptive conduct under Corporations Act s 1041H may recover damages under s 1041I. A person who suffers loss or damage by conduct that contravenes the prohibition on misleading or deceptive conduct under *Australian Securities and Investments Commission Act* 2001 (Cth) s 12DA may recover damages under *ASIC Act* s 12GF.

[8] *Smith v Chadwick* (1884) 9 App Cas 187 at 196; *Gould v Vaggelas* [1985] HCA 75; (1985) 157 CLR 215 at 236.

[9] *Digi-Tech (Australia) Ltd v Brand* (2004) 62 IPR 184; ATPR ¶46-248; [2004] NSWCA 58 at [158]–[159]; *Ingot Capital Investments Pty Ltd v Macquarie Equity Capital Markets Limited* (2008) 73 NSWLR 653; 68 ACSR 595; [2008] NSWCA 206.

could be established in respect of an initial public offering, prior to market trading, without evidence of reliance.

In *Grant-Taylor v Babcock & Brown Ltd (in liq)* (2015) 104 ACSR 195; [2015] FCA 149, Perram J expressed the view, obiter, that shareholders could establish causation, in respect of a company's breach of its continuous disclosure obligations or corresponding misleading conduct by non-disclosure, without proving direct reliance on the relevant non-disclosure. The plaintiffs failed in that case because they did not establish the relevant non-disclosure, that dividends of a particular company within the Babcock & Brown Group had been paid out of capital, was misleading where the value of the company's shares reflected the consolidated position of the Group not the position of that company on a stand-alone basis. Perram J there noted that reliance was a sufficient, but not necessary, basis for establishing causation in claims for compensation brought under ss 1317HA and 1325 of the *Corporations Act* arising from a failure of disclosure. His Honour noted the possibility, left open by the Court of Appeal's decision in *Ingot Capital Investments Pty Ltd v Macquarie Equity Capital Markets Ltd* (2008) 73 NSWLR 653; (2008) 68 ACSR 595; [2008] NSWCA 206 that causation may be established so that C may recover loss arising from conduct where A misleads B who misleads C. His Honour noted at ([219]) that C is not necessarily prevented from recovering his or her loss from A "when A misleads B and in consequence B misleads C"; that the facts of non-disclosure to the market may have the result that "A misleads the market (ie many B's) which then bid up the price which then caused loss to C"; and that "it is artificial to speak of reliance" in such a non-disclosure case. His Honour also observed at ([220]) that:

> "I would accept that a party who acquires shares in a stock exchange can recover compensation for price inflation arising from a failure to disclose material required by s 674 to be disclosed, so long as they are not themselves aware of the non-disclosed material."

That reasoning seems to assume, however, that the B's in his Honour's example were in fact misled by the relevant information, and leave open to question how the conduct of the B's in turn misled the ultimate purchaser, C. The answers to those questions are by no means self-evident in markets that are increasingly driven by sophisticated trading strategies, and where a large proportion of trades by number and volume will be prompted by algorithmic trading strategies rather than by any fundamental assessment of the value of securities.

This is a convenient point to note another recent decision of the High Court dealing with the scope of the apportionment provisions under the *Corporations Act*, which are of particular importance in securities class actions. Pt 7.10 Div 2A of the *Corporations Act* contains a complex proportionate liability regime. That Part applies to an "apportionable" claim for damages under s 1041I for economic loss or damage to property caused by conduct in contravention of the prohibition on misleading and deceptive conduct in s 1041H: s 1041L(1). The proportionate liability regime applies to claims against a concurrent wrongdoer, defined as a person who is one of two or more persons whose acts or omissions caused, independently of each other or jointly, the damage or loss that is the subject of the claim, and that concept does not require that any concurrent wrongdoer has a causative role in another's contravening conduct: s 1041L(3). No account is taken of the fact that a concurrent wrongdoer is

insolvent, is being wound up, or had ceased to exist or died: s 1041L(5). The proportionate liability regime does not apply if the relevant loss was caused intentionally or fraudulently: s 1041M(1). In proceedings involving an apportionable claim, the liability of a defendant who is a concurrent wrongdoer in relation to that claim is limited to an amount reflecting that proportion of the damage or loss claimed that the court considers just having regard to the extent of the defendant's responsibility for the damage or loss; and the court may give judgment against the defendant for not more than that amount: s 1041N(1). In apportioning responsibility between defendants in the proceedings, the court is to exclude that proportion of the damage or loss in relation to which the plaintiff is contributorily negligent under any relevant law; and the court may have regard to the comparative responsibility of any concurrent wrongdoer who is not a party to the proceedings: s 1041N(3). That regime is applicable to an apportionable claim whether or not all concurrent wrongdoers are parties to the proceedings: s 1041N(4).

Two decisions of the Federal Court of Australia had held that the proportionate liability provisions applied to the loss or damages that was (or, potentially, could have been) claimed under the prohibition on misleading or deceptive conduct in s 1041H of the *Corporations Act*, even if the same loss was claimed on a different basis, for example under s 1041E of the *Corporations Act.* That approach was taken by Jagot J at first instance in *Bathurst Regional Council v Local Government Financial Services Pty Ltd (No 5)* [2012] FCA 1200 at [3485] and by the majority of the Full Court of the Federal Court in *Wealthsure Pty Ltd v Selig* (2104) 312 ALR 183; 100 ACSR 566; [2014] FCAFC 64. However, on appeal in *ABN Amro Bank NV v Bathurst Regional Council & Others* (2014) 309 ALR 445; 99 ACSR 336; [2014] FCAFC 65, a differently constituted Full Court of the Federal Court (Jacobson, Gilmour and Gordon JJ) overturned Jagot J's finding that damages for a contravention of s 1041E of the *Corporations Act* were apportionable, to the extent the defendants were each found liable for the same economic loss that was also caused by conduct in contravention of s 1041H of the *Corporations Act.* The Full Court held that damages arising from conduct in contravention of s 1041E of the *Corporations Act* were not apportionable, although they were apportionable to the extent that they were recovered for misleading or deceptive conduct under s 1041H of the *Corporations Act*.

On appeal in *Selig v Wealthsure Pty Ltd* [2015] HCA 18, the High Court unanimously held that the proportionate liability regime in Pt 7.10 Div 2A applies only to claims of misleading and deceptive conduct under s 1041H of the *Corporations Act* and not to other statutory claims, including claims under s 1041E of the *Corporations Act*, although they are based on the same conduct and result in the same loss. The plurality noted (at [26]) that the text of s 1041L(1) restricts the concept of an "apportionable claim" to one based on s 1041H of the *Corporations Act* and observed (at [29]) that the reference to a claim for more than one cause of action under s 1041L(2) did not extend to claims arising from contraventions other than under s 1041H. They held (at [37]) that that concept does not extend to claims on other grounds, even if the same conduct or the same loss is alleged, so that a claim under s 1041E of the *Corporations Act* would not be apportionable, although they noted that common law claims may be subject to apportionment regimes and contributory negligence regimes under State legislation. Gageler J reached the same result. This conclusion is of great importance, particularly in the context of securities class actions, where claims for misleading conduct against auditors and

others may arise where at least the relevant company is insolvent, and can be reformulated as a claim under s 1041E of the *Corporations Act*, if negligence is arguable, so as to avoid apportionment or a reduction for contributory negligence.

Financial services regulation

Future of Financial Advice reforms

Pt 7.7A Div 2, introduced by the *Corporations Amendment (Future of Financial Advice) Act* 2012 (Cth), applies in relation to the provision of personal advice (as defined in s 766B) to a person as a retail client (as defined in s 761G). This Part addresses the concern identified in the Report of the Parliamentary Joint Committee on Corporations and Financial Services, *Inquiry into Financial Products and Services in Australia* (November 2009) that disclosure had not been effective to address conflicts of interest and that Inquiry's recommendation that the *Corporations Act* be amended to explicitly include a duty for financial advisers to place their clients' interests ahead of their own.

A provider of personal advice to a retail client is required to act in the best interests of the client when giving the advice: s 961B(1). Section 961B(2) in turn specifies steps that a provider may take to demonstrate that it has acted in the client's best interests. These steps are directed to the process of providing advice, and reflect "the notion that good processes will improve the quality of advice that is provided" and are intended to set out the minimum steps required to establish that a provider has acted in the best interests of the client.[10] The first of the specified steps is to identify the objectives, financial situation and needs of the client disclosed in the client's instructions: s 961B(2)(a). The specified steps also required an adviser to take any other step that would reasonably be regarded as in the client's best interests (as defined in s 961E), given the client's relevant circumstances (as defined in s 961B(2)(b)): s 961B(2)(g). This requirement was intended to require a provider to take any additional step necessary to demonstrate that it had acted in the best interests of the client and to require that it did anything else that would reasonably be regarded as being in the best interests of the client to do, and applied an objective standard based on the client's relevant circumstances, the provider's relevant expertise and the subject matter of the advice sought.[11] This requirement potentially expanded the scope of s 961B(2) since a step that was not specified in the previous steps set out in the section may nonetheless be reasonably regarded as being in the client's best interests. The present Government sought to narrow the scope of some of these requirements by the Streamlining of Future of Financial Advice Regulations (30 June 2014), which were disallowed by the Senate on 18 November 2014. The legislation is now in effect in its original form. However, ASIC has indicated that it will take a facilitative approach to allow financial services licensees to address the implications of that development in the period to 1 July 2015.[12]

Part 7.7A Div 3, dealing with ongoing fee arrangements, was introduced by the *Corporations Amendment (Future of Financial Advice) Act* 2012 (Cth) and addressed a concern that it was inappropriate that a financial adviser could indefinitely deduct

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[10] Explanatory Memorandum to Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011, [1.23], [1.25].

[11] Explanatory Memorandum to Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011 [1.43]-[1.44].

[12] ASIC 14-307MR Disallowance of FOFA Regulations, 19 November 2014.

ongoing fees from a client's account without providing ongoing advisory services, unless the client took active steps to terminate such an arrangement.[13] The Future of Financial Advice reforms also introduced a requirement that a current fee recipient (as defined) who received fees under an ongoing fee arrangement for providing personal advice to a retail client that would remain in place for longer than 24 months send a written renewal notice (as defined) containing specified information and a fee disclosure statement at two yearly intervals: ss 962K(1), 962L. That requirement was also to be limited by the Streamlining of Future of Financial Advice Regulations (30 June 2014). Those regulations were also disallowed by the Senate and the legislation is now in effect substantially in its original form.

Part 7.7A Div 4, dealing with conflicted remuneration, was introduced by the *Corporations Amendment (Further Future of Financial Advice Measures) Act* 2012 also following the Report of the Parliamentary Joint Committee on Corporations and Financial Services. Broadly, these provisions apply where personal advice is provided to a retail client and prohibit initial or upfront commissions (such as an advice fee charged as a percentage of the initial investment built into the price of the product by arrangement between the product provider and adviser), trail commissions (such as a commission charged as a percentage of the investment and built into the price of the product) and payments based on volume or sales targets (such as a volume bonus or fee rebates and volume-based payments). These provisions were significantly narrowed by exceptions made by the regulations, and were to be further narrowed by additional exemptions introduced by the Streamlining of Future of Financial Advice Regulations, which were then disallowed by the Senate as noted above.

Further scope for reform

The Senate Economics Committee published a detailed report of its inquiry into ASIC's performance in 2014, making numerous recommendations, and the Commonwealth Government has issued its response to that report. The Government noted or accepted, in whole or in part, many of the recommendations made by that report (including, for example, in relation to treatment of whistleblowers and reports by insolvency practitioners), generally noting that ASIC was already addressing the relevant issues. Other matters, including a recommendation for a national examination for advisers, were the subject of review by industry working groups and the Government broadly accepted a proposal for an enhanced public register of financial advisers, which has now been implemented. The Government noted that a range of the wider recommendations made by that report would be considered in its response to the report of the Financial Services Inquiry ("FSI"), including recommendations for increased penalties and alternatives to court action in respect of financial services licensees' failure to comply with breach reporting requirements; a review of penalties under the *Corporations Act* and other legislation administered by ASIC; for the extension of banning orders to directors, managers and persons in a position of influence over financial services licensees; for an expanded power for ASIC to suspend financial planners and advisers; for the introduction of a "user pays" model for funding of ASIC's activities; for the expansion of ASIC's "regulatory toolkit" to prevent marketing of "unsafe products", particularly to retail investors; and clarification of the definitions of retail and wholesale investors.

The broad review of the financial system by the Financial Services Inquiry also

[13] See ASIC Regulatory Guide 245 *Fee Disclosure Statements.*

published its recommendations in its Final Report in December 2014, which address wider issues as to the stability of the financial system and the structure of retirement savings, and also issues as to protection of consumers of financial products and regulatory structure. Matters of particular interest to this audience in that report will include a recommendation of consultation on amendments to the external administration regime to provide additional flexibility for businesses in financial difficulty. This recommendation may encourage the recurrent dialogue as to whether Australia should adopt corporate reorganisation mechanisms modelled on the US regime. The FSI Final Report also expresses support for reform of the managed investment scheme regime, including addressing illiquid schemes and the risk of freezing of investors' funds, best illustrated in respect of difficulties with agricultural investment schemes.

The FSI Final Report also identifies a concern that retail investors may purchase complex structured products that they do not understand or which involve unsuitable risks, without understanding relevant disclosures, and recommends the introduction of a "targeted and principles-based product design and distribution obligation". That obligation would be imposed on product issuers and distributors in relation to the design and distribution of all products other than credit products, not only "complex" products, and would require identification of the type of consumer for which the product would be suitable and appropriate means of distribution. The FSI Final Report also recommended the introduction of a product intervention power which ASIC could exercise where there is a "risk of significant consumer detriment" to a class of consumers, even if there was no existing or suspected breach of the law, and which would permit ASIC to require amendment to marketing or disclosure materials, warnings to consumers, restrictions on distribution or the banning of financial products, up to a maximum of 12 months, and subject to judicial review.[14] Submissions to the Government in respect of the proposals for a product design and distribution obligation and product intervention power have, not surprisingly, been divided. For example, the Law Council of Australia has expressed concern that ASIC is not well qualified to exercise a product intervention power and that such a power risks constraining innovation and increasing costs. On the other hand, two senior academic commentators, in responding to an inquiry from ASIC's Consumer Advisory Panel, expressed broad support for the product intervention power, and pointed to the existence of broadly similar powers in the United Kingdom and the European Union.

The FSI Final Report is also cautiously supportive of "crowd funding" for debt and equity and, over time, other forms of financing, contemplating the raising of small amounts from relatively large number as of investors. The FSI Final Report also recommended improving standards of financial advice by lifting competency and increasing transparency in respect of financial advice. The FSI Final Report expressed the view that Australia's regulatory architecture did not need major change, but noted that ASIC's funding arrangements and enforcement tools had significant weaknesses. That Report also recommended that the criminal and civil penalties available to ASIC be substantially increased so as to act as a "credible deterrent" for larger firms and recommended that ASIC be able to seek

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[14] For commentary, see J Bulling& G Palmieri, "Australian regulators move to increase accountability of financial product issuers and distributors" (2015) *Butterworths Corporations Law Bulletin* [156].

disgorgement of profits.

The Government has undertaken a consultation process in respect of that report, which has now closed, and the final outcome of that Report remains an open question. The Commonwealth Finance Minister indicated, in mid-June, that the Government's response to the FSI Final Report was still several months away.