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1 Introduction

It is fair to say that the year 2015 has not proven to be a very fruitful year in terms of many interesting cases, legislative developments and policy discussions in the area of corporate law. Whilst there has been ongoing debate as to how the government would eventually respond to the Murray Report into the financial systems of Australia (the **Murray Report**), and how the government might deal with the growing number of concerns arising out of corporate collapses highlighted in the Senate Economics References Committee Report into the performance of the Australian Securities and Investments Commission (**ASIC**), on a legislative front the Federal Government seemed almost to be "frozen" in responding to the policy questions that have been raised, initiatives that have been suggested, and important developments that seem to cry out for attention. The embarrassing failure of the government to obtain passage of relevant legislation to remove the Corporations and Markets Advisory Committee (**CAMAC**) "from the books" (the organisation has certainly stopped operating and its staff have been dispersed), has heightened the continued debate on the need for a replacement body to advise the government on policy issues in the corporate law area. Until late in 2015 not much in the way of initiative had been shown by the government but, as is not unusual as the year was coming to a close, important initiatives were taken. So, late in the year, the Honourable Scott Morrison (Federal Treasurer) and the Honourable Kelly O'Dwyer (the Assistant Treasurer) released the Federal Government's response to the Murray Report. This is a high level response and the government has indicated in it that a number of further initiatives and actions need to be taken in the next few months.

As this document was being finalised the government was able to persuade the Labor Party opposition in the Senate to agree to changes to the FoFA legislation (Future of Financial Advice legislation – *Corporations Amendment (Streamlining of Future of Financial Advice) Bill 2014*) which was enacted in the previous Labor Government's term of office, and was subject to significant amendments in the first year of the current government's term of office. However, a number of amendments that the government wished to make to this legislation were opposed by the Labor Party, and the minority senators, on the basis that it watered down the consumer protections in this important legislation dealing with areas that were the subject of significant concern in the Murray Report (which we discuss briefly below) and certain senate inquiries. We discuss this legislation briefly in the next section.

Critical to the way the government will formally respond in detail to the recommendations in the Murray Report (and it is interesting to note that the government has basically adopted the vast

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majority of the Murray Report's recommendations), is a forthcoming report by a three-person committee appointed by the government to review the performance of ASIC. This capability review committee is due to report to the government by the end of December 2015 and it will no doubt make for very interesting reading.

The need to introduce reforms under the insolvency area has been reinvigorated recently. This had been pursued by the previous Labor Government some years ago, and submissions had been made on the second version of the insolvency reform legislation. As we go to press the government has, however, introduced new legislation into the Parliament to reform certain aspects of the insolvency regime (see 3.3.1). These changes will occur during 2016 and we look forward to some systematic and hopefully creative and imaginative responses by the government to deal with a range of issues that have been troubling our economy for some time.

In this review of corporate law cases (and related developments), we will follow the same pattern that we have followed in previous years. We will deal initially with government legislation (there has been relatively few pieces of important legislation), reports on issues of policy (such as the Murray Report and the government response to it), policy recommendations emanating from bodies such as the Productivity Commission (the "Commission"), ASIC, and other bodies, and potential for further developments in the policy area.

In the next section of the Review, we will deal with a range of cases covering them under the following headers:

1. Directors duties and matters relating to corporate governance
2. Shareholders' rights, remedies and related issues
3. Miscellaneous cases

As has been the case in the past, we will not discuss, except in passing, any cases dealing with insolvency, schemes of arrangement and related matters (unless they throw up important questions relating to some fundamental issues at the heart of our corporate regulatory regime). Finally, we will canvass the possible future developments, covering a range of matters, including the potential impact of the High Court's decision in the *CFMEU* case (*Director, Fair Work Building Industry Inspectorate v CFMEU* [2015] HCA 46). The High Court, in the unanimous decision, with three separate judgments, has reversed the decision of the Full Federal Court in *Director, Fair Work Building Industry Inspectorate v CFMEU* [2015] FCAFC 59. In doing so, the High Court has indicated that its decision in *Barbaro v The Queen* (2014) 305 ALR 323 did not apply to civil penalty settlements that had been negotiated by regulators and relevant parties. This reversal of the Full Federal Court decision has come as a welcome relief to major regulators, including ASIC, the competition regulator, and other regulators.

2 Legislative enactments during 2015

As indicated earlier there has been very little by way of specific legislation in the corporate law area. There have been significant pieces of legislation confirming the government's attitude that there is too much regulation and the deregulation legislation that has been enacted (we refer in particular to *Corporations Legislation Amendment (Deregulatory and Other Measures) Act 2015* (Cth)) which sets out very specific areas where the government feels that there are too many rules in place imposing obligations on the corporate sector. However, despite the best wishes of the government in this regard, whilst deregulation may be dealt with in a global and fairly advanced way in these pieces of legislation, there are new pieces of legislation that can be used which create further burdens on corporations in carrying on business and related activities. There are no statutory enactments which deal with particular areas which impact specifically on the duties of directors in the broad sense; however, there are a number of enactments which are aimed at ensuring that the legislation can operate more effectively and efficiently.

The major piece of legislation enacted during 2015 (a welcome piece of legislation from the perspective of company directors and most companies) is the *Corporations Legislation Amendment (Deregulatory and Other Measures) Act 2015* (Cth) which, amongst other things, removed the so called "100 member rule". The previous legislation which had been enacted as a result of pressure

from the States some years ago enabled 100 shareholders (members) of a company to call a general meeting of the corporation by providing notice to the board of directors. Previously the legislation required 5% of shareholders (or numbers related to that threshold) to combine in order to demand the holding of a meeting. The arguments against the 100 member rule were well understood, but because it is necessary to obtain agreement amongst the 6 States (and Territories) as well as the federal Government, legislation to change this legislative regime could not be passed.

In addition to the removal of the 100 member rule, together with the enactment of its replacement 5% rule (as it is generally referred to), the relevant legislation also provided a couple of other interesting changes to the Act. These other changes have included a reduction in the remuneration reporting requirements of directors and an exemption for companies limited by guarantee from the need to retain an auditor. They also clarify the circumstances in which a company's financial year may be less than 12 months.

As indicated earlier, the government has managed to persuade the Labor Party to support (at last) amendments to the Future of Financial Advice Legislation as contained in the *Corporations Amendment (Streamlining of Future of Financial Advice) Bill 2014*. These amendments provide as follows:

- removes the requirement for financial advisors to provide yearly fee disclosure statements to some clients;
- extends the period in which fee disclosure statements must be provided to clients;
- lessens the standard required for financial advisors to satisfy their obligation to act in the best interest of the client by removing the 'catch-all' provision that financial advisors were required to take all steps that at the time were reasonably required as being in the best interests of the client given their circumstances;
- provides additional disclosure in the statement of advice in relation to existing rights of the client and obligations on the advice provider;
- ensures that any client request for further information is in writing and signed by the client;
- requires that the statement of advice is signed by both the provider and the client;
- there are also consequential changes.

It is anticipated this legislation will be enacted early in 2016.

3 Proposed legislative initiatives during 2016

3.1 The Murray Report

The major initiatives that are likely to be the subject of legislation during 2016 will be various amendments (and perhaps new laws) dealing with the government's response to the Murray Report into the Australian Financial System (the **Murray Report**). In addition, it is likely that the government will introduce the insolvency amendments that have been foreshadowed for some time in legislation based on the Commission's Draft Report (May 2015). The final report has been presented to the government in September 2015 and at the time of writing this Review the government has not made the final report available for public comment.

On 20 October 2015 the Honourable Scott Morrison (Federal Treasurer) and the Honourable Kelly O'Dwyer (Minister for Small Business and Assistant Treasurer) published an ambitious set of responses to the even more ambitious Murray Report. We await the more specific responses to relevant portions of the Murray Report which is potentially a far reaching document with significant implications for the Australian business community and for the regulation of aspects of our corporations law. There are also specific recommendations which will be implemented to deal with aspects of the financial and regulated securities regime and the role of bodies such as ASIC, the Australian Prudential & Regulatory Authority (**APRA**) and related bodies.

In this overview of annual developments we can touch on only some aspects of the government initiatives. We believe that these initiatives depend, to a very large extent, on the way the

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government will phase in the recommendations of the ASIC Capability Review Panel (the **Panel**) appointed in September by the government and which was due to report to the government by the end of the year.

That initiative is likely to produce some challenging views from this three-person committee to the ambitious recommendations contained in the Murray Report.

The Murray Report in broad terms covers five significant initiatives, as analysed by Treasurer Morrison and Minister O'Dwyer. They are initiatives that are aimed to:

- strengthen the resilience of the financial system;
- improve the efficiency of the superannuation system;
- stimulate innovation in the financial system;
- support consumers of financial products being treated fairly; and
- strengthen regular capabilities and accountability.

It will not be possible to provide detailed commentary on any of these proposed initiatives until we see the actual language of the draft legislation that is proposed, and the background discussion on these matters. In this brief review note we comment only on two aspects of the Murray Report, namely the comments in relation to the proposition that consumers should be treated fairly and that the regulator should be strengthened and made more accountable.

In this context it is important to remember that the Panel is likely to have significant influence in the way ASIC's powers will be reinvigorated and perhaps progressed. Until that report is made available, (and regrettably from the perspective of this Annual Review it will not be before it appears in print), we can only foreshadow certain potential developments.

It is useful to note, before dealing with two specific areas on which we will provide more detailed commentary, that the governments of the day have already taken many important steps in dealing with the superannuation regime in an attempt to improve on it. Recent decisions to ensure that there are a greater number of independent directors on the boards of superannuation companies is an interesting initiative, and one that has already received a considerable amount of attention in the media and elsewhere. There are many who do not favour this corporate governance approach, rather favouring the appointment of suitably qualified persons, irrespective of the nature of the background and related matters in choosing them.

The question of crowd source equity funding and how it operates remains an area of growing concern for the government. It will impact significantly on the way the government has to progress initiatives in this area. It is unfortunate that CAMAC has not been replaced by an appropriate body – much of the groundwork in this area in the past had been undertaken by CAMAC (and successfully so in our view). The Commission may be the most likely body to be given the task to undertake further work in relation to this and related areas (see section 3.3.2).

How the government will ensure that consumers are better protected and the legislative regime in place will deal more equitably with claims that they may bring, in the event of corporate collapse or similar failures as witnessed during the global financial crisis, presents a major problem area for the government. The Senate Inquiry into the Performance of ASIC published in June 2014 (The Senate Committee into ASIC) highlighted the fact that there have been far too many failures by ASIC in dealing with the difficulties that the relevant industry faced during this period and was not able to provide adequate protection to consumers. The Ministers, in responding to the Murray Report, noted that it was necessary for the government, and the regulators it provided guidance on, to "do more to lift the standards of financial advisers". These orders should lead to the placement of these standards on a professional footing for the first time. In this regard, the government has said it will be entering into detailed consultation with relevant stakeholders and that following such consultation and evaluation the government would:

> Introduce legislation to make the issuers and distributors of financial products accountable for their offerings. This will ensure a stronger customer focus in product design and marketing. The new product design distribution obligation will be principles-based rather than prescriptive and should be viewed as workable by the industry.

Recognising that considerable consultation will need to take place before the government can clarify in finite detail the way in which to progress these initiatives, the government noted that it is necessary for there to be a better alignment between the practical incentives that should exist in improving the way in which conflict of remuneration packages are disclosed to the public in the various areas such as insurance, stockbroking and mortgage broking. The relevant legislation to be introduced will need to be more innovative to ensure that effective competition in the marketplace can help regulate more efficient and effective behaviour.

The government has signalled in the past that it is determined to ensure that appropriate professional standards are introduced into the relevant marketplace in which our financial advisers operate. ASIC had announced in its commentary on the Murray Report that ASIC expects to be given new powers to ban individuals from managing financial firms in appropriate circumstances. This banning power is one that would be a difficult one to put into full effect because at the end of the process the courts may become, and may need to become, involved in evaluating whether ASIC has properly evaluated the evidence in finalising its banning orders. To ensure that the government responds in a sensible and responsible way to the concerns that may be raised in this area, the nature and level of the consultation to be adopted in this regard will be enhanced. This will ensure a professional approach will be adopted in dealing with the increase and the enforcement tools to be provided to ASIC to handle the regulation of financial services and credit licensing regimes.. ASIC will be given the task of reviewing remuneration arrangements in the mortgage broking industry and related industries and again appropriate consultation on how this is best undertaken will be a welcome initiative.

The Ministerial response further notes that it is the government's wish to consult broadly in the development of any legislation to ensure that innovative disclosure will be a key feature in the development of new financial products. There is a clear determination on the part of government to improve the way management investment schemes are regulated, and this will be seen as a parallel development to the disclosure regime that is being pursued. In this context, the government notes that ASIC is already undertaking more responsibility in relation to this area of regulation. There is little doubt that the customers in the marketplace are keen, and have always been keen, to ensure that there is a more effective and able regulator to ensure that better results can be achieved for the consumers in the case of significant collapses occurring. These collapses have been the incentive for class action cases in the courts supported by considerable litigation funding backing. This area of the law is far too litigious in our view and a greater consensus needs to be reached to deal with these areas. This consensus must be between the legislature, the regulators and the marketplace and consumers alike to deal with these areas.

It is anticipated that the Panel will support the proposition that the government states in its Murray Report response that all of the relevant regulators in this area such as ASIC, APRA and the Payment System Board (amongst others) will have to increase their attention to questions of accountability. They will need to set out more clearly and effectively in their annual performance review documentation, what the relevant performance criteria they intend to achieve will be, and how they intend to ensure that they meet relevant targets that are identified in these documents. It will be fascinating to see how this initiative will be transformed into a clear interplay between the regulators and the marketplace.

Funding of ASIC is a matter that the government recognises is very important and it is a matter that needs to be addressed effectively. That particular view has certainly been expressed by the Senate Committee into ASIC and in other reports that have been made. The funds from the sale of ASIC registration business may assist in enabling ASIC to carry out many of its obligations, but there will be an increase in funds needed. The question of whether increased penalties are needed, and just how the government wishes to proceed in that regard, remains alive. The government has indicated so far that it will provide ASIC and other regulators with the ability to "intervene effectively" in dealing with the production and distribution of financial products documentation and related papers. Such an initiative is particularly relevant insofar as the less-informed members of the investing public are concerned. In the UK the relevant market regulator has the power to join with the participants in the market to ensure that the products that are made available to the public as a

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basis of considering investment opportunities, should be clear, well-written and easy to understand. If necessary, the relevant regulator will have the power and the ability to work with the parties issuing these documents to amend them so they can become more effective. The possibility is that we will see similar powers being vested in ASIC to, as it were, re-draft documentation, and to best ensure that the disclosure regime is in place and matters relating to variation of provisions, can be achieved through class orders and other initiatives. Much work will need to be done on these initiatives.

Whilst ASIC has had experience in negotiating enforceable undertakings that may extract from companies where alleged breaches of the law have occurred, and this power is one that it has exercised with a degree of skill and success, it is unclear as to how effectively that skill can be translated into the ability to draft documents that are issued to the public in the context of new products that will seek funds from the public, whether they are investors who are sophisticated or simply mum and dad consumers.

There is a need for considerable co-operation between the government, ASIC, and other regulators, as well as business and the public to ensure that the relevant regime can work. The UK experience will be important.

The next step will be the production of formal responses to each of the recommendations that the government has agreed to pursue. Draft legislation will be introduced in due course for consultation and finalisation, although in some cases the legislation may move straight to final versions where speed is of greater importance. The amount of work to be done in regard to these developments is significant and the extent to which the UK experience to date has been useful will be carefully monitored by the players that are involved in this particular exercise, to ensure that the government's intentions are carefully and effectively put into operation.

The most significant reform of our corporate securities markets and related activities, initiated by the Murray Report will be one of the more significant challenges that our major regulators will have to face. The amendments to current legislation will be very far reaching and subject to some pressure from third parties for the changes to be introduced to the regime that will take its place in the hierarchy of regulators to be established under the proposed view regime.

Greg Medcraft, the Chairman of ASIC, has called for significantly increased powers to be vested in ASIC. To date ASIC has not sought in too many cases the setting of significant penalties against persons who breach the relevant laws. Indeed ASIC's reluctance to bring appropriate court cases, relying instead on the Infringement Notice regime, has been one of the clear failings on the part of the regulator in our view. The power to issue Infringement Notices vested in ASIC following the government's rejection of the Australian Law Reform Commission's 2003 Report "*Principled Regulation: Federal, Civil and Administrative Penalties in Australia* (ALRC Report 95)" which advised against adopting the regime, has been a disappointment to us. One of our writing team, Bob Baxt, has stated publicly on many occasions that he is unhappy with the powers vested in ASIC and suggested that ASIC uses these powers far too often.

The ability to issue Infringement Notices is a power that has been vested in other regulators as well, and enables the regulators to obtain in certain cases fines from corporations which do not wish to pursue detailed negotiations with the regulator on whether a breach of the law has occurred or not, rather agreeing to pay a penalty which would lead to the discontinuance of the investigation. No guilt is assigned to the agreement on the part of the party; and there is no conviction noted; publicity surrounding the issue of these Infringement Notices is very limited in scope and should not be over extended. We wonder how valuable this infringement power is other than saving companies and regulators a lot of time and expense in dealing with the allegation.

No precedential value is produced by the use of Infringement Notices. They may provide a warning to the community that ASIC is 'on the war path' and will intervene in appropriate circumstances but the long-term benefit from the use of these Infringement Notices is very minimal in our view. There is a greater need for positive and aggressive litigation to be taken by ASIC (and by the regulators) when breaches occur.

3.2 Possible amendment of the Statutory Business Judgment Rule

Whilst the courts dabble with the statutory business judgment rule in relevant cases (for example in *ASIC v Mariner Corporation Ltd* [2015] FCA 589, see 5.1 in this review), the Commission, in responding to a request from the Federal Government of Australia to suggest better solutions for companies facing financial difficulty but not wishing to go into liquidation in various scenarios, in its report *Business Set-up Transfer and Closure* (presented in September 2015 but only made public in December 2015), the Commission has recommended important changes in procedure. Directors trying to rescue companies which are close to insolvency may enter into administrative and related arrangements which should be give them certain protection against the operation of the insolvent trading provisions of the legislation (s 588G of the Act), provided certain steps are taken. The Commission has recommended that during this period of exploring reconstruction and related matters, the directors would retain control of the company but receive independent advice from advisers who are appropriately registered. Furthermore, the Commission recommended that the relevant "defence" or "harbour" will only be available if:

- the directors of a company have made, and documented, a conscious decision to appoint a safe harbour adviser with a view to constructing a plan to turn around the company;
- the adviser was presented with proper books and records upon appointment, and can certify that the company was solvent at the time of appointment;
- the adviser is registered and has at least five years' experience as an insolvency and turnaround practitioner;
- directors are able to demonstrate that they took all reasonable steps to pursue restructuring; and
- the advice must be proximate to a specific circumstance of financial difficulty, and subject to general anti-avoidance provisions to prevent repeated use of safe harbour within a short period.

The Commission further recommended that this "defence" would cover all of the steps being taken in running the business in the restructured form until the conclusion of the particular plan that has been put in place. If the relevant appointed advisors form the opinion that the relevant rescue plan is not possible, or cannot be continued, they will be required to terminate the relevant safe harbour period and advise the directors that "a formal insolvency process" should commence.

(There are other connected recommendations to the operation of this process which is not necessary to discuss in the context of this brief overview).

The proposed legislation is likely to emphasise the need for directors to take "all reasonable steps". This expression has been a matter of some concern to advisers in the corporate law field in previous legislation. It will be interesting to see if the legislation to be introduced retains these words.

Of course, the probable effectiveness of this proposed new rule will depend on the actual drafting to be finalised in the statute intended to be introduced into parliament in early 2016.

In the meantime, the honest and reasonable director defence proposed by the Australian Institute of Company Directors has not been able to be progressed; it is not supported by ASIC and a range of business and legal advisers.

3.3 Other proposed legislative initiatives for finalisation in 2016

3.3.1 Insolvency reforms

Literally as this overview was being finalised the government introduced into the Parliament the long awaited Insolvency Law Reform Bill 2015. This proposed legislation had been mooted by the previous Labor Government. As indicated in the Second Reading speech "the level of confidence in the insolvency industry needs to be improved. Insolvency practitioners received the lowest rating of perceived integrity in the latest survey of ASIC's stakeholders". It is not possible to discuss the very many technical reforms proposed in this Review.

Nevertheless it is important to note the fact that the Assistant Treasurer, the Hon Kelly O'Dwyer, in tabling the Bill, advised that the government was "currently considering the Commission's

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recommendations to ensure that financially distressed businesses are given the best opportunity to restructure, or be wound up efficiently where the business cannot be saved."

It is hoped that this will lead to the introduction of a better safe harbour for directors against the reach of the insolvent trading rules (see s 180(2) of the Act).

3.3.2 Crowd-sourced funding

As part of the government's emphasis on innovation, a legislative priority has been the passing of new laws to not only regulate, but also open up, opportunities for crowd-sourced equity raising. Literally, as this Review was being finalised, the government introduced the Corporations Amendment (Crowd-sourced Funding) Bill 2015 into Parliament with the purpose of making crowd-sourced equity more available, especially to assist start-up companies. Although at this stage it is not possible to enter into a detailed analysis of the proposed new regime, it at least appears that it will be limited to public companies and have a $5 million overall limit and a $10,000 limit per retail investor. This was not in line with the expectations of many in the industry who were arguing for private companies to be able to access crowd-sourced funding, as most start-up companies in need of such equity are private companies.

4 ASIC's Initiatives and Reports

The past year has been a very active one for ASIC. It has, as usual, published a variety of reports and consultation papers. In these a number of recommendations have been made and initiatives announced. Its Enforcement Report is impressive; ASIC has commenced many cases in courts and tribunals. The impact of these numerous initiatives will become more apparent over the coming year, as some of the reports will be transformed into concrete legislative and regulatory amendments, and no doubt ASIC hopes some of its investigations will result in major pronouncements from the courts. In this section we discuss some of the more significant initiatives and reports. The former Assistant Treasurer Josh Frydenberg released the consultation paper "Proposed Industry Funding Model for the Australian Securities and Investments Commission" (28 August 2015) (the Consultation Paper) in which the government sought to review the way in which ASIC is funded. The concept of an industry funding model for ASIC was also raised in the Murray Report. It was foreshadowing a model pursuant to which those sections/persons in the community who use ASIC's services will be asked to pay for them, thus helping to fund ASIC's operations. Current thinking involves a combination of annual levies on industry participants as well as fees paid for the use of ASIC's services such as document compliance reviews, licence applications and applications for registration. Submissions in response to the Consultation Paper closed on 9 October 2015. It will be interesting to see what changes the government proposes to the way in which ASIC is funded in response to the Consultation Paper and submissions.

ASIC will further seek to improve its bottom line by adopting a new policy to regularly invoke its currently seldom-used power under the *Australian Securities and Investments Commission Act 2001* (Cth) to recover the costs of its investigations from those who it has investigated. This policy was announced in ASIC Information Sheet 204 "Recovery of Investigation Expenses and Costs". If pursued vigorously it will see ASIC rely on the power in s 91 of the ASIC Act to issue an order requiring a person who has been convicted of an offence, or whom a judgment has been made against, to pay the cost of ASIC's investigation. ASIC's costs can include the remuneration of its staff involved in the investigation and ASIC therefore has the potential to recover a considerable amount of money through this policy. In considering whether to issue a cost recovery order, ASIC proposes that it will consider a range of factors such as the impecuniosity of the person, the hardship caused to the person, the amount recoverable under the order, the extent of ASIC's success in the proceeding, the effect of the contravention on the victim and the level of cooperation by the defendant. As the policy will only apply to investigations commenced after the policy's announcement on 29 July, and as issuing a costs order requires a successful court judgment as a prerequisite, it will likely be some time until we see the full effect of this policy take hold.

On 27 July, the then Assistant Treasurer Josh Frydenberg appointed "a review panel into ASIC's ability to meet its future challenges" (the "Panel"). The Panel is comprised of Karen Chester (Productivity Commissioner), David Galbally AM QC (prominent lawyer) and Mark Gray (business person and industrialist). The Panel has examined how efficiently and effectively ASIC

operates to meet its strategic objectives, including an "identification and analysis of immediate and forward looking priorities and risks" including the operation of the financial system. The wide-ranging review was proposed to cover everything from how ASIC allocates resources through to the current capabilities of its staff. The Panel has sought further submissions and has specifically requested that these should be forward looking so as to best be able to help ASIC meet future challenges. Many recommendations in this area have already been made by the Murray Report (see 3.1 "The Murray Report"). As noted earlier, it is expected the government will consider the Panel's recommendations in conjunction with the Murray Report recommendations when formulating legislative responses.

ASIC's Strategic Focus for the next four years in its Corporate Plan was released on 31 August 2015. It provides a useful insight into what ASIC's focus areas will be; it is especially useful when read in conjunction with the ASIC proposal to evaluate "culture and incentives" as important "drivers" ASIC will focus on over the coming year. This will be particularly relevant in relation to financial products and services markets – the main focus of the Murray Report. Greg Medcraft, the Chairman of ASIC has placed considerable emphasis on the role of "culture" in assessing directors' duties (see also section 5.5). This could be one of the most significant areas of development in the corporate law, especially if ASIC is successful in having the government extend the operation of the Criminal Code to have it adopted for civil provisions of the Act, especially in the context of the regulation of the financial services and related sectors. This will primarily involve focusing on the quality of the advice and advisors.

The Corporate Plan also identifies cyber-attacks and digital disruption as important areas for ASIC to focus on over the coming years, as well as the effects of globalisation. ASIC will continue to work in cooperation with other regulators from G20 countries to deal with these issues. The impact of digital disruption and financial crime was also raised in the Parliamentary Joint Committee on Law Enforcement's Inquiry into financial related crime which recommended a review of ASIC's technology to ensure it is capable of meeting such future challenges. It further recommended that ASIC develop stronger connections with the private sector as a way to better detect and prevent financial crime.

The release at the end of August 2015 of ASIC's six-monthly enforcement report ("report") covering the period of 1 January-30 June 2015 revealed that, during that period, 323 enforcement outcomes occurred. This number includes criminal, civil and administrative actions as well as negotiated outcomes. Included were 82 criminal charges against 10 individuals and the disqualification of 19 directors. In line with ASIC's previously mentioned focus on improving the financial services industry, ASIC banned 25 individuals from future participation in the industry. Interestingly, the number represents a decrease from the 348 enforcement outcomes ASIC recorded in the preceding period, covering the last six months of 2014.

As well as highlighting ASIC's enforcement actions over the previous six months, the report also highlights ASIC's enforcement priorities over that period and also going forward and unsurprisingly, 'culture' features prominently. This is expected as it is in line with numerous comments made by ASIC's Chairman Greg Medcraft and we can expect to see developments in this area over the coming year. Interestingly, the report takes its definition of 'culture' from the Criminal Code and ASIC has certainly made previous calls for the provisions in the Criminal Code relating to culture to be incorporated into civil provisions.

The report indicates, that so far, ASIC's work in the area of "culture" has been largely confined to working with companies to achieve refunds for consumers where systematic failures in a company have led to poor consumer outcomes. Many of the examples provided in this context involve some of Australia's largest banks providing multi-million dollar refunds to consumers. The other two areas highlighted as enforcement priorities were retail margin FX trading and phoenix activity. This is also unsurprising given the high-risk nature of retail margin FX trading and well-documented problems of phoenix activity, especially in the construction industry. Looking forward to the next six-month period, the report also highlights that ASIC is currently pursuing 48 criminal enforcement actions and 29 civil enforcement actions, and these are relatively evenly divided between market integrity, corporate governance and financial services areas.

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5 Leading cases in 2016

5.1 Director's duties of care – some new "sunlight"

There has been a considerable amount of interest in the subject of directors' duty of care since the High Court of Australia's decision in the James Hardie litigation (*ASIC v Hellicar* (2012) 247 CLR 345). It is clear that the community expects a higher standard of care and diligence from directors than perhaps was the case in the previous generation. Whilst ASIC has not been as spectacularly successful in any cases at the same level of importance as the James Hardie litigation, and indeed has suffered some serious losses, it has nevertheless succeeded in obtaining important judgments against directors where issues raised relate more to specific areas in which the relevant directors have not addressed their obligations as well as has been expected.

For example, in *ASIC v Australian Property Custodian Holdings Ltd (Receivers and Managers appointed) (in liq) (Controllers appointed) (No 3)* [2013] FCA 1342, ASIC was able to obtain judgment against all the directors of the relevant companies associated with the major investment initiative inspired by the plans of William Lewski. Significant penalties (both financial and disqualification) were imposed. At the time of writing, an appeal on all counts is being considered by the Full Federal Court. Justice Murphy in his judgments in both cases (the second case is *Australian Securities and Investments Commission (ASIC) v Australian Property Custodian Holdings Ltd (recs and mgrs apptd) (in liq)* (2014) 322 ALR 45) indicated there is an expectation in the community that directors will reach a certain standard in their obligations to comply with the law, whether they are specific general duties, such as the duties of care and diligence, or with more specific duties such as those which relate to disclosure to the market and related matters.

The case concerned the Australian Property Custodian Holdings Ltd (APCHL) which collapsed in 2010 owing $550 million to its investors. APCHL acted as the former trustee and manager of the failed nursing home organisation, Prime Retirement and Aged Care Property Trust (Prime Trust) which owned a number of nursing homes. ASIC commenced proceedings against the former APCHL directors for breaching their directors' duties under the Act, challenging a board decision of Prime Trust which amended the constitution and introduced a controversial "listing fee" to be paid, which resulted in $33 million being paid to APCHL as well as entities associated with Mr Lewski in order to list APCHL on the ASX. The directors failed to seek members approval for this amendment. These decisions are currently on appeal in the Full Federal Court.

Despite minor successes, however, ASIC did not succeed in what we regard as a major case which saw an ASIC prosecution, namely *ASIC v Mariner Corporation Ltd* (2015) 106 ACSR 343. It concerned a proposed takeover offer by the Mariner Corporation (driven by its CEO Darren Olney-Fraser and two directors Donald Christie and Matthew Fletcher), who ASIC alleged did not comply with a number of provisions of the Act including provisions relating to partial takeovers and how these should proceed. ASIC sued the directors and the corporation for making what it alleged was a reckless takeover bid for Austock Corporation Ltd (in breach of s 631(2)(b) of the Act), as well as claims that they engaged in misleading or deceptive conduct by inadequate disclosure in breach of s 1041H of the Act. Of most interest to us, ASIC also alleged that the directors had breached their duty of care and diligence by committing either or both of the statutory breaches referred to earlier, or otherwise causing the company to breach the law by not progressing with the takeover offer in an appropriate fashion, basing their action on s 180(1) of the Act.

All allegations by ASIC were dismissed by Beach J. In doing so, he made a number of significant contributions to the law relating to directors' duties and the statutory business judgement rule (s 180(2) of the Act).

Early in his judgment Beach J made a significant contribution on the nature of the duties of care expected of company directors through his evaluation of the standards against which a court should assess the alleged breaches of duty which may be levelled at directors of companies either by ASIC or by civil litigants. Taking into account the background and experience of the relevant directors facing the charges, he noted:

> It is necessary to bear [the director's experience] in mind when assessing the case of a regulator second guessing such judgment calls with the benefit of hindsight, using a largely paper-based

> analysis and viewing the events from a timeframe perspective divorced from the reality of the speed at which the events occurred in real time. Second, in looking at the transaction in question, it is important to adopt an ex-ante perspective where one is not just looking at the potential risks and downsides but also the potential benefits. That was the directors' framework at the relevant time and that is necessarily the framework within which s 180 must be analysed. A retrospective analysis of a transaction which did not proceed has the tendency to overlook that dimension (2015) FCA at para 13.

After reviewing the relevant facts and related issues, and making it clear that he was not impressed with the case that ASIC had brought, Justice Beach warned against an approach to this area of the law that was "too bold". He added at para 444 the following important quote from Brereton J's judgment in *ASIC v Maxwell* [2006] NSWSC 1052 at [104]:

> There are cases in which it will be a contravention of [director's] duties owed to the company, for directors to authorise or permit the company to commit contraventions of provisions of the [Act]. Relevant jeopardy to the interests of the company may be found in the actual or potential exposure of the company to several penalties or other liability under the Act, and it may no doubt be a breach of the relevant duty for a director to embark on or authorise a course which attracts the risk of that exposure, at least if the risk is clear and the countervailing's potential benefits insignificant. But it is a mistake to think that ss 180, 181 and 182 [of the Act] are concerned with any general obligation owed by directors at large to conduct the affairs of the company in accordance with law generally or the Corporations Act in particular; they are not. They are concerned with duties owed to the company …

He concluded his approach to this evaluation of the duties of directors with a significant recognition of entrepreneurialism on the part of directors:

> Further, relevant to the question of breach of duty is the balance between, on the one hand, the foreseeable risk of harm to the company flowing from the contravention and, on the other hand, the potential benefits that could reasonably be expected to have accrued to the company from that conduct.
>
> Not only must the Court consider the nature and magnitude of the foreseeable risk of harm and degree of probability of its occurrence, along with the expense, difficulty and inconvenience of taking alleviating action, but the Court must balance the foreseeable risk of harm against the potential benefits that could reasonably be expected to accrue from the conduct in question.
>
> After all, one expects management including the directors to take calculated risks. The very nature of commercial activity necessarily involves uncertainty and risk taking. The pursuit of an activity that might entail a foreseeable risk of harm does not of itself establish a contravention of s 180. Moreover, a failed activity pursued by the directors which causes loss to the company does not of itself establish a contravention of s 180. [450-452]

In conclusion, Justice Beach ruled that he would have applied the statutory business judgment rule (s 180(2) of the Act) in this case if it was necessary to do so. In a short passage in his judgment he considered the application of the business judgment rule by considering the way the directors had assessed the takeover and the way it should proceed. In his view the directors had acted in good faith and the directors had done everything that was commercially reasonably sensible in the context of the proposed takeover offer. He further observed by way of dicta that he would have applied s 180(2) of the Act if for some reason he ruled that they had acted in breach of their duty. They would have been relieved of any liability under the Act in the circumstances but it was unnecessary for him to make a ruling on that score – in other words the application of the statutory business judgment rule was not relevant in the circumstances (and in that context this case can be compared to the decision in *ASIC v Rich* (2009) 236 FLR 1, the judgment of Austin J).

5.2 Directors obligations to act in good faith and in the best interests of the company reaffirmed

The courts have had a series of cases argued before them on the extent to which the courts can investigate the way in which companies have been managed and the continued failure, on the part of some directors, to act in the interests of the company rather than their own interests.

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The recent decision in *Thomas v Arthur Hughes Pty Ltd* is discussed as an illustration of this matter.

In previous issues of the Annual Review we have highlighted decisions in the various courts, and most significantly in the New South Wales Supreme Court, in which the courts have provided relief to shareholders (or other directors) in closely held companies when directors who controlled a significant position within the company acted in a way to prioritise their own interest (or interests linked to theirs) in preference to other shareholders. The decision in *Re Ledir Enterprises Pty Ltd* [2013] NSWSC 1332 was discussed in the 2014 Annual Review of Cases (see "4.4 Oppression Remedy (ss 232 and 233 of the Act)").

White J in the recent decision of the New South Wales Supreme Court in *Thomas v Arthur Hughes Pty Ltd* [2015] NSWSC 1027, faced a similar difficult question to determine a family dispute involving family owned companies. In this case, Mr and Mrs Lewis were the shareholders of a company Anne Lewis Pty Ltd (the company). Mr Lewis held the majority of shares and a friend of his was appointed as a director shortly before he died. After his death the friend sought specialised tax advice to ensure that the planning involving the breakup of the company's assets would be most tax effective. Mrs Lewis worked with a colleague of her late husband and one of her sons to enter into a series of transactions which would see the assets of the relevant company pass to a series of new companies and trusts. A second son of the Lewis', who was opposed to the arrangements that had been put in place, brought an action to have the company wound up.

Once the company was placed into liquidation the liquidator sought to undo the transactions that had seen the transfer of the company's assets. The liquidator argued that this should occur because the transactions prioritised the interests of Mrs Lewis and did not follow the interests of the late Mr Lewis which had been set out in his will. The late Mr Lewis had instructed that Mrs Lewis should only be entitled to the annual net income from the estate and that the residual property should be divided amongst their children. As Mr Lewis was a shareholder of the company, his will represented the interests of the company and therefore, by transferring the company's assets to the series of companies and trusts, Mrs Lewis was said to not be acting in the best interests of the company, but rather in her own best interest. The liquidator challenging the arrangements argued that these estate planning arrangements were not in the best interests of the company and argued that the directors were not acting in good faith and in the best interests of the company. White J referred with approval to comments of Justice Black in *Re Ledir Enterprises* in assessing whether directors were acting in the best interests of the corporation. He adopted a subjective approach – the proper purpose would not be considered relevant if the directors were exercising their powers in order to obtain some private advantage. In the view of White J, Mrs Lewis had breached both her statutory and fiduciary duties as she had acted neither in the best interests of the company, nor taken any note of her husband's will. White J did not find dishonesty in her behaviour, he ruled that Mrs Lewis had not subjectively considered the transactions to be in the best interests of the company.

Interestingly in this case the court also dealt with the question of accessorial liability of directors duties. The relevant son who was involved in the planning, was held to have knowingly assisted Mrs Lewis in the breach of duties that she had committed and he was required to pay equitable compensation.

(See also section 5.7 for a discussion of the broader application of the question of accessorial liability.)

In another interesting decision in which the courts took a similar severe view of the obligations of directors and the need to behave with appropriate attention to the interests of the company rather than to personal interests that they might have otherwise favoured, namely *Re Ikon Group Ltd* [2015] NSWSC 980, Brereton J maintained what we believe is a standard approach in dealing with requests that the court reassess the way in which the directors of the company had acted – that the court would need a reasonably strong case to interfere with the way in which the board had carried out its decisions.

The key features of this case involving the Ikon Group concerned a joint venture agreement between the company Ikon Group Ltd (**Ikon**) and the similarly named but different organisation, Ikon Financial Group Ltd (**Ikon F**). The joint venture concerned foreign exchange trading. A third company within the broad group of companies, Ikon Australia Pty Ltd (**Ikon A**), which is a subsidiary of Ikon International Hong Kong PCL, the major corporation in the joint venture, carried on a minor role in the activities of the relevant broad consortium, operating what can generally be described as a "front office" in Australia. It received instructions from various areas. The back office of the organisation was used to process client instructions which would then be forwarded to Ikon F to process. Ikon and Ikon F, the parties to the current joint venture, were respectively both the sole director and the sole shareholder of the relevant companies. Disputes arose between them in relation to the hedging arrangements between Ikon A and Ikon F which led to the owner of Ikon F expressing an intention to exit the joint venture agreement. Two new directors were apparently appointed to Ikon A by the owner of Ikon F and an existing director of Ikon A was removed.

Initial proceedings to deal with the particular dispute were initiated. Ikon sought a declaration that the appointment of the new directors to Ikon A was invalid. It also argued that the removal of the existing directors of the Ikon was void.

In this case, Brereton J agreed that s 1324 of the Act could provide a remedy to any person whose shares are affected by an alleged breach of duty, and they may seek an injunction or some other order to pursue that particular argument. The reason for the injunction being sought in this case was the allegation that the joint venture agreement contained a clause requiring the parties to refer any disputes to arbitration; the joint venture agreement could then not be relied on in order to institute court proceedings. Brereton J held that the section had been triggered – the very touchstone of the section "is a contravention, passed or threatened, of the [Act]" [at 22]. The case could only proceed if there was in fact a potential breach of one of the director's duties under ss 180–183 of the legislation.

It was suggested that the relevant breach of duty was the failure of the existing directors to ensure that the company complied with its obligations to third parties (namely to the major holding company). Brereton J noted at para 27: "I accept the directors may contravene their duties to act in good faith in the interest of the company, and to act with the requisite degree of care, skill and diligence, if they were to facilitate breaches by the company of obligations owed to third parties, such as clients, in circumstances where doing so would be calculated to expose the company to liabilities and thus jeopardise the position of the company". He ruled, however, that no such circumstances existed here; there was no wilful failure on the part of the directors in carrying out the particular next steps; rather there was a breakdown in the consideration of relevant information from one group of directors to another and there was no suggestion that the court should second guess commercial decisions made by the directors in this case. In conclusion, Brereton J ruled that there was not a sufficiently justifiable case to support a breach of the Act and Brereton J concluded these were matters "in which the courts would be very reluctant to interfere" and therefore the seeking of interlocutory relief was refused.

At the time of writing the litigation was stayed and the dispute referred to arbitration in line with the contractual dispute resolution clause governing the joint venture.

5.3 Courts tough on directors seeking to benefit themselves at the expense of their company

Linked to these cases in terms of liability of directors is a case where directors tried to benefit themselves to the detriment of the company by, for example, voting themselves a very generous retirement package. The courts will, generally speaking, come down very heavily against the directors retaining payments that they receive as a result of such arrangements.

The Full Federal Court of Australia in *Renshaw v Queensland Mining Corporation Ltd* [2014] FCAFC 172 ruled that where directors had organised the arrangements with a company's management so that they could receive generous retirement packages when it suited them (which they proceeded to trigger as a result of certain events that occurred in the company), the directors would not be able to maintain those benefits. In the court's view the relevant provisions in the

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legislation, dealing with this type of conduct, were aimed at "bringing transparency to, and shine daylight onto, transactions commonly called 'golden handshakes' that involve expenditure of the company's money in connection with the cessation of employment or services relationship with a senior office holder or employee" (at para 29). The court felt that words used in legislation to catch conduct that was "in connection with" the so-called malfeasance, and the benefits gained by directors, was intended 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 context of [the legislation] thus informs and suggests a broad construction of the reach of the expression 'in connection with' when used in [relevant legislation]" (at para 30).

This line of interpretation is similar to other cases in which the courts have emphasised that the directors duty of good faith will be interpreted quite strictly by the courts.

5.4 To whom do directors owe their duties – are we on the praecipes of a new legal agenda?

Had the High Court of Australia been given the opportunity to review the Western Australian Court of Appeal decision in the Bell Group case (*Westpac Banking Corporation v Bell Group Ltd (in liq) (No 3)* (2012) 89 ACSR 1), and to focus on the question of whether directors owed a legal duty to creditors at large rather than owing a duty to the company which may involve considering the interests of creditors (as was clearly suggested in the minority judgment in the Bell Group case and supported in a recent lecture by former High Court Justice Ken Hayne ("Directors" Duties and a Company's Creditors' (Speech delivered at the 2014 Harold Ford Memorial Lecture, The University of Melbourne, 19/08/2014), we might by now have had an answer to this growing problem. Instead, at the end of November 2015 the Governance Institute of Australia will be holding a five-day conference which will focus on that particular question amongst others.

The question is really quite a simple one. The courts have said, on more than one occasion, that directors would be foolish if, when their companies were faced with financial difficulties, on the praecipes, so to speak, the directors did not take into account the interests of creditors. But, the High Court in cases such as *Spies v R* (2000) 173 ALR 529, and judges in various other cases (including the equivalent of the High Court of Australia in Canada – Supreme Court of Canada (see *BCE Inc v 1976 Debentureholders* [2008] 3 SCR 560), have made it clear that the obligation in law is to the company, which means the shareholders.

Directors will obviously try to ensure that all persons who may be affected by important decisions to be reached by directors when companies face financial difficulties will be taken into account, but the obligation that the directors must keep at the forefront is the shareholders. Even the changes to the UK *Companies Act 2006*, in s 172, whilst legally allowing directors to take into account the interests of stakeholders such as creditors, have not changed the fundamental principle: ie the duty directors owed to the company (ie the shareholders).

In other words, it is unlikely that stakeholders will be able to sue directors if they do not take into account other stakeholder interests unless they can rely on s 1324 of the Act which provides a remedy, at the discretion of the judge hearing the case, in favour of any person whose interests are affected by breach of statutory duty. Therefore, if the directors are alleged to have breached a duty that can be linked to a breach of s 181 of the Act (or another section of the Act) the relevant interested persons may be able to claim a remedy pursuant to s 1324 of the Act. So far no court has awarded damages to stakeholders (nor indeed the shareholders) for damages relying on s 1324(10) of the Act which clearly provides for such remedy to be ordered in specific cases where harm has been shown to have occurred as a result of the alleged failure on the part of directors to act properly.

There is a growing movement, amongst lawyers as well as business people, for the law to be softened and to permit greater flexibility in the way in which directors and senior managers conduct the affairs of companies. Indeed the ASX Corporate Governance Council has various rules in relation to corporate social responsibility and related matters (now in their third edition). They make it clear that they welcome such an approach by company directors and other managers.

The Act provides, in certain sections, a very clear direction to directors of companies that they must take into account outside interests. Environmental interests are clearly provided for in this context by specific provisions in the statute, such as s 299 of the Act. Indeed, that was the basis on which the Australasian Centre for Corporate Responsibility relied on its action in the case *Australasian Centre for Corporate Responsibility v Commonwealth Bank of Australia* [2015] FCA 785 (discussed in section 6.2) which was argued in the Federal Court (and although Davies J ruled against the application, that decision is now on appeal to be argued in the Full Federal Court in February).

Whilst the listing requirements of the ASX also have a part to play in that they are given legal backing pursuant to s 793C of the Act, the relevant ASX rule applicable here are limited in scope and operation. There have been many calls for a broader extension of the obligations that directors of companies should be forced to comply with in recognising community interests. But, it is still a far cry from the days when company directors argued that they could expend the corporate funds in providing a proper safeguard for employees of companies when companies were facing insolvency. Whilst such action may be relevant in certain circumstances, it may also amount to a breach of the law if the action is not evaluated as being in the best interests of the company.

One major problem with what we would describe as "wishy-washy rules" in dealing with these matters is that it places the company director, and pity the poor non-executive company director, in an impossible situation as to how he or she must act in dealing with attempts to rescue the company. The potential liability directors face in merely trying to rescue the company by considering the narrow interests of the company, may see them ending up facing very expensive and lengthy litigation under the insolvent trading regime. (But see section 3.2 for possible extension of the SBJR).

5.5 The relevance of corporate culture in assessing directors' duties – ASIC makes a *stake*

Linked to the question of to whom the duties of directors are owed is one of the more interesting initiatives undertaken by the Chairman of ASIC, Greg Medcraft, in seeking reviews of the relevant legislation, and the possible enhancement of the powers of ASIC is to seek a significant increase in the penalties that the courts may award where breaches of the law occur. He has suggested in many speeches and submissions that the penalty regime contained in the legislation does not provide a sufficient disincentive to directors who flirt with potential areas of misbehaviour. That particular proposition is one that is very difficult to support when we do not have enough litigation brought by ASIC in which it tests the ability of the current legislation to be administered by the court in an effective way.

A more recent and more ambitious statement made by the Chairman of ASIC, which he has modified somewhat, is a suggestion that provisions be included in the Act which will in effect embrace the requirements set out in the Commonwealth *Criminal Code Act 1995* (Cth) (the Criminal Code) under which companies are required to put into effect appropriate risk management regimes to ensure that they embrace a proper culture of compliance. There have been very few cases in which the Criminal Code has been specifically tested in the context of the duties owed by directors to the company. Justice Keane, when Chief Justice of the Full Federal Court, accepted ASIC's claim that the chief executive officer of the Fortescue Metals Group had breached s 180(1) of the Act in *ASIC v Fortescue Metals Group Limited* (2011) 190 FCR 364, on the basis that he had allowed the company to breach the continuous disclosure requirements of the Act by the company engaging in alleged, misleading and deceptive conduct, suggesting that courts are likely to be willing to impose stricter liability on directors in appropriate cases (in this case ASIC was pursuing the disqualification of the CEO). Pursuant to the suggestion made by Greg Medcraft, what would be required would be to include in the Act specific provisions which provide that if the alleged breach of duty involved an absence of appropriate risk management and review by the directors of the relevant activities of the company, it might result in criminal sanctions being sought against the directors for a breach of the relevant legislation. The drafting would have to be extremely carefully prepared in order to ensure that the legislation did not impose a ridiculous level of liability in extreme circumstances.

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(See the forthcoming article by Colvin and Argent "Corporate and personal liability for 'culture' in corporations" due to be published in the February 2016 CSLJ. The article deals with the broader issues surrounding the possible inclusion of a reliance on a culture as far as legislation is concerned.)

5.6 Directors liability for general breaches of the law, including miscellaneous provisions of the Corporations Act

With the culture of compliance, as introduced by the Criminal Code, now very much in the limelight, there is a growing tendency for regulators and others to try to lump together alleged breaches of the law by directors and link them to the primary duties of directors to act with care and diligence, in good faith and related duties under the Act. The most recent example of this process, was attempted by ASIC in the decision *ASIC v Mariner Corporation Ltd* [2015] FCA 589, which we discuss above in dealing with duties of care and diligence. In this case, Beach J dismissed an attempt by ASIC to lumber the directors of the Mariner Corporation with a range of general breaches of the law connected with the discontinued takeover offer by the Mariner Corporation of Austock Corporation Limited. As noted earlier in discussing the duties of care, ASIC had alleged that the directors had breached not only s 180(1) of the Act, but also two other provisions of the Act: one relating to the requirement to maintain appropriate disclosure (s 1041H of the Act) and the other relating to the conduct of takeovers (s 639(2)(b) not complying with certain takeover rules that were in place).

Beach J, in dismissing all of the allegations against the directors, also dismissed the approach taken by ASIC to embrace this broader compilation of obligations on the part of directors where other contraventions were relevant. His Honour followed the decision of Brereton J in *ASIC v Maxwell* [2006] NSWSC 1052, and noted (at [444] of the *Mariner* case quoting from *Maxwell* at [104]) a very meaningful "rule of thumb":

> There are cases in which it will be a contravention of their duties, owed to the company, for directors to authorise or permit the company to commit contraventions of provisions of the Corporations Act. Relevant jeopardy to the interests of the company may be found in the actual or potential exposure of the company to civil penalties or other liability under the Act, and it may no doubt be a breach of a relevant duty for a director to embark on or authorise a course which attracts the risk of that exposure, at least if the risk is clear and the countervailing potential benefits insignificant. But it is a mistake to think that ss 180, 181 and 182 [of the Act] are concerned with any general obligation owed by directors at large to conduct the affairs of the company in accordance with law generally or the Corporations Act in particular; they are not. They are concerned with duties owed to the company. (at [444], quoting *Maxwell* at [104])

As indicated in section 5.1, he also dismissed the allegations that the directors had acted in breach of their duty of care and diligence.

See also the article by Hanrahan and Bednall, ″Officers' liability for mandatory corporate disclosure″, (2013) 31 C&SLJ 474.

5.7 Accessorial liability given greater weight in a series of cases

The question of when accessorial liability might be pursued either by the regulator (most likely ASIC or the Australian Competition and Consumer Commission) or by civil litigants, has certainly been highlighted in some recent decisions. By way of background, it is useful to note that s 79 of the Act contains the accessorial liability provisions. Under this section a director or officer may be liable where he or she has aided, abetted, counselled or procured the committing of an offence by their relevant company. Even without this provision, directors and officers may be made liable as a result of the application of s 11.2(1) of the Criminal Code. Under this provision a person may commit an offence if that person "aids, abets, counsels or procures the commission of [that] offence by another person". To be guilty under subs (1), it must be shown that the person's conduct actually did, on the facts, aid, abet, counsel or procure the commission of the offence; that the offence was committed by the other person (subs (2)); and that the person intended for their conduct to have this outcome (subs (3)).

Two interesting decisions are worthy of brief comment. Reeves J in *Australian Competition and Consumer Commission v Davies* [2015] FCA 1017 discusses the potentially wide application of s 79 and related matters. *Re Waterfront Investments Group Pty Ltd (in liq)* [2015] NSWSC 18 indicates that the equivalent section of the common law rules may apply in the context of corporate law scenarios.

The facts in the *Davies* case are these. Davies was the sole shareholder and director of Natural Food Vending Pty Ltd (NFV). The Australian Competition and Consumer Commission (ACCC) used its power under s 155 of the *Trade Practices Act 1974* (Cth) (TPA) (now s 155 of the *Competition and Consumer Act 2010* (Cth)) to issue a notice to NFV to provide certain documents. Prior to the deadline in the notice, Davies placed the company into voluntary administration but failed to disclose the notice to the administrator (although this was disputed and Reeves J was not required to make a final finding as to this fact). It was alleged that the company breached s 155 of the TPA, and the ACCC brought proceedings against Davies under s 11.2 of the Criminal Code for being accessorily liable to NFV's breach.

Justice Reeves ruled that Davies took no steps to make NFV comply with the terms of the notice. Instead, Davies instructed an administrator to liquidate the company without informing that administrator of the ACCC notice or giving the administrator any instructions in relation to complying with the notice. In that context Reeves J ruled that Davies, through his omission in not-complying with the notice, aided, abetted, counselled or procured the offence by NFV and on the evidence his conduct showed that he intended to do so. This meant he was guilty of commissioning the offence by NFV, and was guilty of that offence himself.

During the course of his judgment, Reeves J made some interesting observations of the difficulties that arise when a director, who may control the relevant company, but who is a separate person from that company, exposes himself/herself to potential liability.

His Honour noted the various sections contained in Pt 2.5 of the Criminal Code attribute the conduct and intention of a company's "high managerial agents", which include directors and officers, to the company. However, his Honour then noted (at [33]):

> Notwithstanding these provisions, it is important to record that, for the purposes of s 11.2 of the Criminal Code, a corporate body and its directors are still treated as separate legal persons with the consequence that a director can aid and abet the commission of an offence by the company.

In *Waterfront*, referred to earlier, there were a number of claims brought against certain directors as a result of the collapse of a major enterprise involving investments on the NSW Central Coast. In particular Black J, in the New South Wales Supreme Court, had to consider the application of s 79 of the Act which as we have noted above can result in the imposition of accessorial liability. The plaintiff in the case argued that each of those persons associated with the sole director were persons who were "knowingly concerned and involved in those breaches within the meaning of s 79 of the [Act] or were accessories for the purposes of the second limb of [the decision in *Barnes v Addy* (1874) LR 9 Ch App 244]" (at [124]).

Justice Black held that certain persons were liable but his comments on accessorial liability are particularly interesting:

> A finding of knowing concern requires that the relevant person is an intentional participant in the contravention, the requisite intention being established if the person has knowledge of the essential elements of the contravention [quoting certain cases the details of which it is unnecessary to set out here]. That finding also at least requires [that the relevant director] was in fact "concerned" in the contravention, in that he … had a practical involvement in the acts or omissions constituting the contravention [again, quoting at length from a number of cases]. (at [125])

His Honour discussed a number of cases, including *Farah Constructions Pty Ltd v Say-Dee Pty Ltd* (2007) 230 CLR 89. Black J noted that in that case the High Court emphasised that its earlier decisions established the requirement that "any breach of trust or breach of fiduciary duty relied on

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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 [126]).

Finally, Black J noted that "a third party which is the corporate creature or alter ego of a fiduciary who acted in breach of duty can also be held to be knowingly involved in that breach without the need to separately establish dishonesty on its part" (at [126]).

Ultimately, his Honour held that it was inappropriate for him to make orders against certain persons and companies associated with the relevant director as there had been insufficient evidence produced to establish what the loss or damage was in the relevant circumstances.

5.8 Courts continue to take a generous view of directors' indemnity arrangements

Sections 199A and 199B of the Act contain very strict rules governing when a company may or may not provide payment to indemnify directors and officers for breaches of the law. In the middle of the previous decade, the now defunct Corporations and Markets Advisory Committee (CAMAC) identified that directors had been facing increasing difficulty in obtaining appropriate indemnity insurance (in its 2004 report titled Directors and Officers Insurance). At almost the same time the High Court of Australia provided directors and officers with some comfort by giving a generous interpretation of the relevant provisions in the Act (*Wilkie v Gordian Runoff Ltd* (2005) 221 CLR 522 and *Rich v CGU Insurance Ltd* (2005) 79 ALJR 856). This view was later enforced by the Full Federal Court in *Rickus v Motor Trades Association of Australia Superannuation Fund Pty Ltd* [2010] FCAFC 16.

This year, the Victorian Court of Appeal, in *Note Printing Australia Ltd v Leckenby* [2015] VSCA 105, took a similar approach to determining whether a director who had been charged with criminal offences was able to rely on his indemnity agreement with the company to have his defence funded by the company. In this case, Leckenby, who was the chief executive officer of Note Printing Australia Pty Ltd (NPAL), had a deed of indemnity with the company which contained the following clause:

> To the fullest extent permitted by law, NPAL hereby indemnifies [Leckenby] against each and every liability for legal costs and expense [he] may incur or for which [he] may become liable in defending an action for a liability incurred as such an officer of NPAL unless such costs and expenses are incurred: …
>
> (b) in defending or resisting criminal proceedings in which [he] is found guilty;

Leckenby had been the subject of criminal proceedings in relation to alleged bribery charges against him. The charges had not yet been heard in court, however Leckenby had begun hiring a legal team for his defence. He requested that NPAL reimburse his costs, which the company refused on the grounds that it would be illegal for it to do so.

In the Court of Appeal, NPAL had argued that the payment is barred by s 199A of the Act as such payments would be tantamount to indemnifying someone for costs that would be illegal. Justice Tate, with whom Whelan and Ferguson JJA agreed, found that s 199A(3)(b) of the Act, and the relevant clause "clearly precludes Leckenby having an entitlement to be indemnified by NPAL against legal costs he has incurred if he is found guilty" (at [23]). However, as was pointed out by Sifris J in the first instance decision, the clause was essentially an agreement by the company to provide an advance to Leckenby so that he could conduct his legal proceedings in a satisfactory way (see Annual Review 2015 "5.11 A Director's insurance and indemnity (Leckenby)").

Appeal Justice Tate took a businesslike approach to interpreting the clause, confirming "the need for a businesslike approach to be adopted in the interpretation of a commercial contract". Her Honour continued in the same paragraph: "It would be apparent to a reasonable person in the position of NPAL and Leckenby, at the time of entering into the Deed, that, in the eventuality of a criminal prosecution, unless there was an agreement for ongoing legal costs to be paid prior to verdict, Leckenby could incur significant liability for those costs in a manner that could be potentially compromising of his defence" (at [66]). This approach confirmed that taken in the earlier cases mentioned above, and continues to show that the court is willing to promote directors'

and officers' rights to enforce indemnity clauses against their companies to enable them to have the best legal defence in a particular case, despite the strict rules set out by the Act in this area.

6 Shareholders rights, remedies and related issues

6.1 An overview

In this section of the Annual Review we discuss very briefly the major interesting cases that have been decided during the year dealing with the rights of shareholders (especially in the context of statutory and common law actions) and certain related matters with respect to shareholder's responsibilities and the potential developments. In this context we note again that this is not a comprehensive overview of all aspects of this area of the law. We do not discuss the very many cases that are heard each year where shareholders (and others who are more likely to be creditors) seek to set aside the winding up of companies as a result of the failure of the company to meet claims for payment of debts (see section 7.5).

6.2 Ability of shareholders to require discussion of matters at annual general meetings

Of growing interest in Australia is the impact being made in corporate governance and the way companies are being influenced by hedge funds and other minority interests using the proxy rules that are available under the legislation to have their say at meetings. The extent to which the courts will allow shareholders to, as it were, interfere with the way in which the directors choose to manage the relevant corporation, is well illustrated by the decision in *Australasian Centre for Corporate Responsibility v Commonwealth Bank of Australia* [2015] FCA 785 (CBA).

The traditional rule in corporate law that once the corporate constitution (the old memorandum and articles of association) is in place, the powers of the companies are vested in the board of directors, was the subject of that case. Justice Davies had to consider the ability of a pro-conservation group, the Australasian Centre for Corporate Responsibility (the Centre) which sought orders from the court to force the board of directors of the Commonwealth Bank of Australia to list for discussion, resolutions in relation to providing details of financial support being provided by the bank to certain organisations. In CBA, the main question for consideration was the extent to which the Centre could force the board of directors to list on the agenda of the banks Annual General Meeting a report that would set out:

- the quantum of greenhouse gas emissions that the bank was responsible for financing, calculated in accordance with guidance provided by the greenhouse gas protocol;
- information about the current levels and nature of risks to the bank from the amount of "unburnable carbon" that was generated; and
- the current approach adopted by the bank to mitigate those risks.

The Centre also asked that its representatives, and other shareholders, should be given an opportunity to express their concern about the absence of information in the report that had so far been provided to shareholders.

The request was denied by the directors of the bank and as indicated the Centre sought declarations from the court. It also sought a further declaration that the bank should provide more information about the relevant resolutions so that matters could be considered more usefully.

In her judgment, Davies J considered not only the impact of ss 249N, 250R and 250S of the Act, but some general common law principles. These cases discussed the divisions of powers between the directors and members, and the possibility that ratifying breaches of duties might occur. It was suggested by the Centre that *Winthrop Investments v Winns* [1975] 2 NSWLR 666, and other similar decisions, enabled shareholders to ratify breaches of directors' duties should the directors be held to be in breach of their duties if they agreed to such a request from the Centre.

In her judgment, Davies J relied heavily on the NSW Supreme Court's decision in *National Roads & Motorists' Association v Parker* (1986) 6 NSWLR 517 (*Parker*). At para 24 of her judgment she outlined the legal position that she held applied in this case: "The general meeting cannot by

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resolution express the members' opinions as to how the board should exercise powers exclusively vested in it by the constitution of the company [in the Parker decision, the articles of association ie the constitution placed the control of management of the business and affairs of the company in the board]. The articles also made provision for the procedure to be followed in the election of the board … and the [the conduct of the relevant meetings]."

Davies J also relied on (as had McLelland J in *Parker*) earlier English authority such as *John Shaw & Sons (Salford Ltd) v Shaw* [1935] 2 KB 113 to support the supposition that members would not be able to override the board's powers in running the meeting unless there were clear provisions in the articles to do so. In the current case, counsel for the Centre relied on US authorities such as *Auer v Dressel* (1954) 306 NY 427 which contained dicta that suggested that the courts could be more generous in assessing the power of the shareholders to be given greater opportunity to decide matters in a corporate environment.

Recently, in the New South Wales Supreme Court, White J in *Re Molopo Energy Ltd* (2014) 294 FLR 13 (*Molopo*) confirmed the view that it would be most unusual for members to be given the power to generate decision-making which was normally in the hands of the directors.

The decision of Davies J has been taken on appeal to the Full Federal Court. But in the meantime Beach J in *Aveo Group Ltd v State Street Australia Ltd* [2015] FCA 1019, in considering a number of matters surrounding the management of the relevant company and the division of powers between the members and the board, relied heavily on the decision in Davies J in the *CBA* case and earlier cases to which she had referred. Beach J also relied on a number of other cases in which questions surrounding the way in which powers in the board should be evaluated.

Whilst the decision of White J in the *Molopo* case may have gone further than was necessary in considering the specific facts of that particular situation, and whilst there have been decisions in which the courts have provided some flexibility to shareholders in pursuing matters that might be seen to be within the prerogative of the board of directors (see for example the decision of the Full Federal Court of Australia in *Capricornia Credit Union Ltd v ASIC* (2007) 159 FCR 69 in which flexibility was allowed in the way in which these matters are to be evaluated), it will be surprising to see the Full Federal Court, or indeed the High Court, move away from the central theme of the earlier cases referred to by Davies J (and others) in evaluating the powers of the members and the board.

6.3 Statutory derivative actions

There have been no very high profile decisions in this area of the law but there have been some interesting ones in which the courts have continued to emphasise that there are a number of criteria that have to be established by shareholders who wish to bring a derivative (or representative) action against the company and the directors based on s 236 of the legislation. Section 237 of the legislation sets out the criteria that must be established and, in various overviews of the law in this area in the last few years, we have highlighted the tendency for the courts to be a little more sympathetic to shareholders than perhaps was the case in the earlier years in which this statutory procedure was introduced to the legislation to overcome the decision in *Foss v Harbottle* (1843) 2 Hare 461.

Two cases in South Australia saw the courts reach different conclusions on whether relevant shareholders should be allowed to continue with their litigation. In *Argus Group Pty Ltd v Litigation Lending Services Ltd* [2014] SASC 181 the relevant plaintiffs, who held a minority interest in Litigation Lending Services Ltd (Litigation Lending), brought proceedings which were in effect seeking remedies against the majority directors and the majority shareholders of Litigation Lending. In the view of Gray J, since the requirements in s 237(2) were all satisfied, the plaintiffs should be granted leave under s 237 to represent Litigation Lending in its primary action against the majority shareholder and directors.

In contrast in *Michalakas v Powell* [2014] SASCFC 132, the Full Federal Court dealt with a more complex scenario. The applicant, Michalakas, was appointed as a director of Garden Estate Hackam Pty Ltd (Garden E) by her husband, who was also a director of the company. The husband

had been declared bankrupt after Garden E entered into a loan agreement with Angas Securities Ltd (Angas) and failed to meet the repayment schedule. The applicant then sought leave to bring a statutory derivative action against Angas. In this case the court had to consider two of the requirements in s 237 in a little detail. The first was whether there was a serious question to be considered by the court and the second question was whether it would be in the best interests of the company for leave to be granted to Michalakas to continue with the action. The Full Court of the South Australian Supreme Court held that the first requirement had not been met because the applicant's claims lacked evidentiary proof. With respect to the second requirement, the court found that the applicant's offer to provide an indemnity had been made too late in the proceedings. In the circumstances, the application was held to be correctly refused.

Finally, in *Huang v Wang* [2015] NSWSC 510, an application by Huang for permission to commence a statutory derivative action was denied by Black J. In his view, the particular litigation would not be in the best interests of the company. Several factors were considered by Black J in reaching this conclusion. He regarded the prospects for success in litigation as very slight and that the costs that would be incurred would be detrimental to the position of the company. In his view if it had been successful the benefits would not have justified the costs of litigation.

There have been other cases dealing with these issues. Often cases involving reliance on the statutory derivative action procedures also involved questions of oppression which the court may find more relevant when considering the dispute in question.

6.4 Oppression cases

Perhaps the most interesting and important decision in relation to the oppression remedy during 2015 is s 232 of the Act in the decision in *Corbett v Corbett Court Pty Ltd* [2015] FCA 1176. This decision of Farrell J illustrates that to evaluate whether oppression has been established in an action under this particular provision it is necessary to look at the matter objectively. The facts of the case are relatively detailed and we set them out to illustrate this particular issue. Corbett Court Pty Ltd (the company) had been founded by the parents of eight children who were all offered shares in the company. John, one of the children was offered 42 shares in the company while the other siblings shared an additional 42 shares (holding six shares each). Following the death of the father, John was the sole director of the company and he later appointed his wife to the board. The company owned and operated a small shopping centre and at the time of the dispute John was trying to entice the Target Group of Companies to take a major tenancy in the relevant centre. To do so, the company entered into a period of expensive building development, but regrettably for the company's sake it was unable to retain the Target Group as a tenant. In due course the company faced certain liquidation.

John had tried to bring his brothers and sisters together to arrange for an equity raising but failed to achieve this with his brothers and sisters refusing to support John's initiative. Farrell J noted during the course of the judgment that there was animosity and mistrust between the siblings, especially towards John and his wife.

The two directors then issued 100,000 shares of $1 each to themselves, thus raising $100,000 of the $1 million required for the company to capture the Target Group tenancy. This had the effect of diluting the other shareholders' interest from approximately 7% to 0.005995%. Paul, one of the siblings, brought proceedings, including a claim under s 232 of the Act.

Farrell J was critical of the behaviour of Paul and the other siblings, but she nevertheless ruled in favour of the s 232 of the action. The evidence in the case indicated that Paul had on previous occasions tried to convince the company's creditors to call on loans which would have placed the company into liquidation. Paul had also made unsupported claims of promises his father had made with regards to the structure of the company and that the shareholdings would never change. Farrell J described the attitudes of Paul and the other siblings as "commercially naïve and self-serving" – they simply wanted the company to be an avenue for them to make money but they did not wish to provide further funds to the company.

Farrell J held that oppression had been established on two basic grounds. In the first place she ruled that the other shareholders (siblings) were never given any independent opinion, when the initial

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share issues were proposed by John, as to whether they were a suitable way to raise funds in the circumstances. Thus, even though none of the shareholders even responded to these proposals, they still did not have all the facts and information to be able to make informed decisions about further investing in the company if they had so chosen.

Secondly, her Honour emphasised that the test was objective:

> The test of unfairness requires an objective assessment of the conduct in question with regard to the particular context in which the conduct occurs. Conduct will be oppressive if that conduct is unfair according to ordinary standards of reasonableness and fair dealing (at [128]).

She added:

> Determining whether conduct is oppressive involves an objective assessment of whether the impugned conduct is so unfair that reasonable directors who consider the matter would not have thought it fair to make the decision having balanced the importance of furthering the corporate objective on one hand and the disadvantage, disability or burden which would be imposed on the member or members on the other (at [130]).

In conclusion, she pointed out that the outcome of the share issue was to dilute the holdings of the other shareholders. Whilst the $100,000 that had been raised was a relevantly small part of the over $1 million required, it was nevertheless only helping John and his wife. She also noted that whilst there was no evidence to show that John believed that the proposals he put forward would be other than in the interests of the company, due to the objective nature of the test required to be applied in interpreting s 232 of the Act, it was irrelevant for this matter to be considered in the decision. The circumstances as such supported a conclusion that oppression had occurred and thus a finding was made in support of the applicant.

Other interesting cases on oppression during the year included Patterson v Humphrey (2014) 291 FLR 246 – a case involving two equal shareholders in the relevant company. Justice Le Miere ruled that the failure of Humphrey and his partner to allow the Pattersons access to directors meetings and material amounted to oppression. In *Falkingham v Peninsula Kingswood Country Golf Club Ltd* [2015] VSCA 30, a member of the relevant golf club sought oppression relief with respect to a proposed merger between the Peninsula Golf Club and the Kingswood Golf Club. The Victorian Court of Appeal upheld the ruling of Robson J that oppression had been established even though the members of the board of the relevant golf clubs had acted honestly and believed that the merger was in the best interests of the relevant club. The Victorian Court of Appeal also held that Robson J did not err in exercising his discretion to deny the relief sought.

Finally, in the very recent case of *Australian Institute of Fitness Pty Ltd v Australian Institute of Fitness (Vic/Tas) Pty Ltd (No 3)* [2015] NSWSC 1639 the Victorian and Tasmanian branch of the Australian Institute of Fitness against the main body sought relief under the oppression remedy. The Victorian/Tasmanian section of the Institute, a minority shareholder in the Institute, alleged that there was oppression in the way in which the business of the organisation was conducted. Sackar J noted that he had to assess the matter on an objective basis. The mere fact that there was a disagreement between different interests did not amount to oppression. In his view the evidence did not support a movement for relief under the oppression remedy.

6.5 Conclusion

In the early years following the introduction of the statutory derivative action, and the reliance on the oppression remedy, plaintiffs/applicants were largely unsuccessful, or found it very difficult to sustain arguments in favour of the remedies that they sought (there seemed to be a reluctance on the part of judges to interfere in what one leading judge has described as “basically family disputes”). More recently, the courts have been far more sympathetic to these claims and the results more innovative in the way in which the courts have evaluated the relevant evidence and the remedies to be awarded.

7 Miscellaneous cases

7.1 Important High Court judgment on settlements between regulators and defendants – the CFMEU case

As this Annual Review was to be sent to the printers, the High Court of Australia handed down its important decision in *Construction, Forestry, Mining and Energy Union v Director, Fair Work Building Industry Inspectorate* [2015] HCA 46. This was an appeal from the decision of the Full Federal Court in the case, *Director, Fair Work Building Industry Inspectorate v CFMEU* [2015] FCAFC 59. In that decision, the Full Federal Court believed that civil litigation settlements between regulators and defendants were equally affected by the decision of the High Court of Australia in the case of *Barbaro v The Queen* (2014) 88 ALJR 372. Pursuant to that decision there were certain restrictions placed on the courts in approving settlement agreements between regulators and defendants, in which penalties (both criminal and civil) were settled by the courts. In the area of corporate law and competition law, the principles enunciated by the Full Federal Court in *NW Frozen Foods Pty Ltd v ACCC* (1996) 71 FCR 285, had given a very strong green light for the use of the settlement procedures to be pursued by regulators without much fear of interference from the courts. Nevertheless, as the Full Federal Court noted in the *CFMEU* decision, there were certain constraints which led it to believe that the practice had been adopted most liberally by the Federal Courts and that it should be significantly qualified.

Urgent special leave was obtained to appeal the decision from the Full Federal Court. The High Court handed down its decision on the 9th December 2015. Three separate judgments were delivered by the High Court in which it disagreed with the Full Federal Court, especially in the context of the application of the *Barbaro* decision. In each of the three separate judgments, the judges reflected on the need for the flexibility of these arrangements which had been put into practice for some years by various regulators before the Full Federal Court which reduced significantly the costs and time involved in resolving potential litigation. The position of the High Court was well-summarised by the joint judgment which made the following statements:

> More generally, it is entirely consistent with the nature of civil proceedings for a court to make orders by consent and to approve a compromise of proceedings on terms proposed by the parties, provided the court is persuaded that what is proposed is appropriate. [57]
>
> Once it is understood that civil penalties are not retributive, but like most other civil remedies essentially deterrent or compensatory and therefore protective, there is nothing odd or exceptionable about a court approving an agreed settlement of a civil proceeding which involves the public interest; provided of course that the court is persuaded that the settlement is appropriate. [59]

The decision is one that has been warmly received by regulators, and by practitioners alike (as well as their clients), as it will simplify the work of the regulators in dealing with matters where, for various reasons, it is more expeditious and reasonable for the matters to be settled rather than being pursued by the court. However, it is our view, that care will need to be taken by the courts in simply approving arrangements brought to the court for settlement. Courts should look very critically at the nature of the penalties being struck as a signal to the community on the importance of the particular matter that is being pursued by the relevant regulator. The warnings issued by Justice Weinberg in the Victorian Court of Appeal in the *Ingleby*. case (*ASIC v Ingleby* [2013] VSCA 49) should be heeded.

7.2 Shareholders, creditors and investors can rely on “fraud on the market” remedy – Full Federal Court

Where shareholders or other investors buy securities (shares or other securities in the company) and allegedly suffer loss as a result of the failure on the part of the issuer of those securities to inform the market fully, or otherwise engage in misleading or deceptive conduct, the remedies that are available to those investors range from relying on misleading or deceptive conduct provisions in legislation, to common law remedies of a general nature, as well as the increased reliance on the so-called fraud on the market remedy that has been so popular in the United States. The recent

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decision in the Full Federal Court in *Caason Investments Pty Ltd v Cao* [2015] FCAFC 94 (Caason) whilst only dealing with interlocutory matters, contains some very significant guidance for future litigation in situations where significant losses have been suffered in the failure of financial and other companies seeking funds from investors in the market place.

In an earlier decision of the Full Federal Court, *ABN AMRO Bank NV v Bathurst Regional Council* (2014) 224 FCR 1, the Full Federal Court upheld applications by investors in ABN AMRO Bank NV which had made financial products available to local councils and other investors, on the basis that information provided about the securities and their likely success was misleading. The relevant evidence that was critical in this case, relied on by the investors, was that the ABN AMRO NV Bank had obtained a AAA rating from Standard & Poors Credit Rating Agency, which was in fact misleading, and which was a key factor in investors trusting the safety of the relevant offering. A key issue in the appeal in this case was the reliance by third parties on the credit rating supplied. It was noted by the Court that there was no need to prove reliance on the relevant credit rating to prove causation of the loss. In the short statement the Full Federal Court noted that "there is no bright line principle that it is insufficient for a plaintiff to prove that some other person relied on the alleged misleading conduct and that the person's reliance led to the plaintiff suffering loss" (at [1375]).

In a later case of *Grant-Taylor v Babcock & Brown Ltd (in liq)* (2015) 322 ALR 723, Perram J in the Federal Court concluded that "While reliance is a sufficient condition for establishing causation it is not a necessary one" (at para 219). The shareholders in that case ultimately did not succeed in the relevant litigation but reasons for their failure did not relate to causation (see also an interesting article by Danielle McFarlane "Significant Judicial Guidance on the application of the continuous disclosure obligations" (2015) 33 C&SLJ 287 for a discussion of this interesting initiative more generally being relied on in the courts).

The *Caason* case was a representative proceeding with the plaintiffs/appellants buying shares in company Arasor International over a lengthy period. The litigation was based on s 1041H of the Act (misleading and deceptive conduct) and s 79(1) of the Act that provides a remedy where there are misleading or deceptive statements. The plaintiffs' pleadings were struck out on the basis that the case had not been properly structured. The focus on the appeal was whether market-based causation was an arguable basis for the plaintiffs to rely on in the courts. The majority judges (Gilmore and Foster JJ) ruled that there was nothing to prevent a market-based causation argument being run although they did not state whether it would be successful. In a more interesting and far-reaching judgment Edelman J addressed at some length the viability of the market-based causation argument being relied on in the case. At para 155 of his judgment he notes that it was "at least 'arguable' that as a technique of causation without reliance market-based causation was not unusual. A common example of causation that may arise is cases that involve misleading conduct by one trader which leads to customers being diverted from another trader".

7.3 Courts continue to provide broad interpretation of anti-avoidance provisions in the Act

A number of provisions in the legislation enable the courts to set aside transactions entered into by directors of companies in which they tend to favour themselves, or specific creditors, against the interests of others, including other shareholders and creditors. The Commissioner of Taxation is particularly concerned about the ability to unwind these types of transactions where significant tax liabilities have not been met by the company which has gone into liquidation. The sections cover a range of specific scenarios (relying on a strict black letter law interpretation of the relevant provisions from it by and large, although there are some exceptions to this approach). Three cases during the last 12 months centre on the interpretation of the relevant provisions, whilst the High Court of Australia has provided some interesting comment on technical questions in relation to obtaining relief from the operations of the sections.

In the Federal Court in *Super Art Australia Pty Ltd v Foden* [2014] FCA 1168, the Federal Court had little difficulty in penetrating the arrangements that had been put in place by the relevant directors to create speculative transactions which appeared to favour the directors. The court ruled

that s 588FF of the Act could be applied to set aside the relevant transactions and require repayment by the directors of the relevant payments.

In the Western Australian Court of Appeal in the decision of *Weaver vs Harburn* (2014) WASCA 227, the court, in reviewing the decision of Master Sanderson in the Supreme Court of Western Australia, once again took a very strict approach in reviewing these provisions. The relevant arrangements involved the sole director of a corporation channelling corporate funds through a wholly owned subsidiary so that his wife could purchase a boat. The liquidators of the company, once it went into liquidation, sought to recover these payments from the director's wife. Master Sanderson in the Supreme Court rejected the claim of the liquidator, ruling that there were relevant matters that dispelled the potential operations of various sections of the legislation.

The Court of Appeal disagreed with this assessment. In focussing on the financial health of the relevant companies in the group, the court ruled that while the financial condition of the relevant company was not an element of unreasonable behaviour on the part of the relevant director, the wider context of the company's position did not prevent the court from looking at these relevant matters. President McLure noted, in words that may prove to be useful in later cases dealing with similar scenarios, that the:

> relevance and/or weight to be given to the fact, or risk, of insolvency depends on the facts. Indeed a director-related transaction entered into when the company was insolvent would, without more, be caught by s 588FE(4). Further, a transaction may, like an unfair loan, be so objectively unreasonable that the financial position of the company at the time of entry into the transaction is not relevant. In other circumstances, the transaction may be unreasonable solely or primarily because of the financial condition of the company at the time of the transaction (at [93]).

A third case that can be considered together with the previous two decisions is the New South Wales Court of Appeal's powerful decision in *Fletcher v Anderson* (2014) 292 FLR 269. This case involved the impact of s 588FF(3)(b) and associated provisions of the Act. They concerned the activities of the Octavia group of companies which have certainly been keeping our courts very busy.

Certain payments had been made by the Octavia group of companies to the Commissioner of Taxation as a result of numerous claims being lodged against relevant companies within the group. Later, when the relevant companies were placed into liquidation some of these payments were challenged as being in breach of s 588FF of the Act. This challenge was on the basis that the payments made to the Commissioner were "insolvent transactions" within the meaning of s 588FC and unfair preferences were governed by s 588FA of the Act. There were also allegations made against individual directors. The liquidators sought indemnification from them for the payments made to the Commissioner of Taxation.

As a result of the decision of the New South Wales Court of Appeal, not only were the transactions involving the Commissioner of Taxation set aside, but the court also reviewed decisions made against the individual directors of the company to indemnify the company. The decision of the Court of Appeal to read s 588FGA of the Act (under which it is possible to seek indemnity from individual directors), effectively operates to impose additional layers of liability on company directors where fraudulent transactions are involved.

The reach of sections such as the insolvent trading provisions (s 588G of the Act), together with these other provisions that are now the subject of these interesting decisions, makes it clear that there are critical questions that need to be addressed in dealing with insolvency matters. As we have noted elsewhere in this Annual Review, the Insolvency Law Reform Bill is under consideration by the current government, and it is hoped that the legislation, which will deal with some of these matters if not directly at least indirectly, will be able to be actively and effectively pursued.

Two other cases worthy of note are – *Grant Samuel Corporate Finance Pty Ltd v Fletcher* [2015] HCA 8, and *Fortress Credit Corporation (Australia) II Pty Ltd v Fletcher* [2015] HCA 10. In both decisions the High Court considered the power of the court under s 588FF(3)(a) and s 588FF(3)(b) to extend the period under which orders under s 588FF(1) could be voided on the basis that they

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were caught by fraud or other relevant circumstances. In each case, an extended period of time was sought to obtain a relevant order under the relevant section. These were clearly technical questions of interpretation which the High Court reached different conclusions on whether an extension of time could have been granted or not. They reflect the significant attention to detail in dealing with the application of statutory provisions that will need to be applied in obtaining relief with respect to these remedies.

7.4 Can proportionate liability be relied on in misleading or deceptive conduct litigation?

The High Court of Australia in the decision of *Selig v Wealthsure Pty Ltd* (2015) 89 ALJR 572, overturned the Full Federal Court ruling in which apportionment in relation to a claim for misleading or deceptive conduct could be the basis of the relevant litigation. The High Court held that apportionment would only apply if the claim was purely for misleading or deceptive conduct. It would not apply to other related aspects of a claim in which the causes of action based on non-disclosure and related conduct would have been pleaded. Briefly, in this case the Seligs had invested $450,000 in a company on the advice of Wealthsure Pty Ltd through its authorised representative. They were caught up in a "ponzi scheme" and sought damages from their financial advisors not only for misleading or deceptive conduct but also other arguments based on non-disclosure. At first instances the Federal Court ruled that Wealthsure was highly liable for the loss suffered by the Seligs notwithstanding the fact that other parties had been involved in providing advice which had contributed to the loss. Lander J held the apportionment liability provisions could only apply to breaches of s 1041H of the Act. The Full Federal Court reversed his decision holding that where a claim for misleading or deceptive conduct was brought, and these are connected to other causes of action, the courts may nevertheless apportion liability between other causes of action and various defendants.

In the view of the High Court (two separate judgments were delivered but they reached the same result) held that the ability to apportion liability in the circumstances should only apply to claims for misleading or deceptive conduct and only in the context of the provision of financial products and services. The court ruled that an overriding matter in interpreting the relevant statutory regime was that the expression "apportionable claim", as used in the relevant legislation, could only be linked to misleading or deceptive conduct. It is argued that this will be a significant blow to insurance companies and others that may otherwise use this considerably popular argument to minimise their liability for significant losses where these losses occur and be able to spread the losses amongst other defendants. Whether legislation is considered relevant to diminish the trust of these decisions, and other decisions in which significantly greater risks now lay before financial services providers, it will be an interesting question for the government to consider in due course.

7.5 Ability of creditors to challenge the strict liability regime for winding up of companies which fail to meet statutory demands

Perhaps the most effective method that creditors may adopt in winding up companies that do not meet their debts, or become financially embarrassed, is to provide a statutory demand to the company for the payment of the relevant debt within 21 days pursuant to the operation of s 459E of the Act. There is no doubt that the most numerous company liquidations that we see in Australia are as a result of the automatic application of these provisions. Under the relevant statutory provisions surrounding the use of the service of the statutory demand, as one would expect, there are provisions that enable companies to avoid the consequences of the failure to meet the statutory demand in certain very limited circumstances. An application must be made to the court under s 458G of the Act. This must be done within 21 days of the relevant statute of demand being issued.

Since the High Court decision in *David Grant & Co Pty Ltd v Westpac Banking Corporation* (1995) 184 CLR 265, our courts have been very unwilling to extend the time for compliance with a statutory demand, unless a very strong case has been made out. The courts have also been unwilling to set aside the winding up order that has been made where exceptional circumstances exist. An interesting case this year, in which the strictness of the law was given a very strict interpretation with respect to attempts to set aside a failure to meet a statutory demand, is the decision in *Adhesive Pro Pty Ltd v Blackrock Supplies Pty Ltd* [2015] ACTSC 268, a decision of the Supreme Court of the Australian Capital Territory. In this particular case, Mossop AJ refused to

provide relief to the applicant where the 21 day statutory period had not been complied with due to delays at the Supreme Court Registry. The plaintiffs still sought to serve an unapproved copy of the relevant documents within the statutory period. However, Mossop AJ held that this was not within the definition of 'filed' and 'served' as required by the Act. In his view the relevant documents must have been processed and recorded by the Registrar. He also ruled that the relevant documents in this case had not been served as they did not contain a clear notification of certain details as to the return date with respect to the company's response to the relevant documents. That notification could only be affixed in his view, by the Registrar.

It was clear from this decision, and indeed on other decisions (and there are numerous decisions that were made this year) that a very strict regime is applied by the courts in dealing with this area of the law

8 Conclusions

Whilst the year 2015 will certainly not be regarded as a year in which many major legislative decisions were finalised and acted upon, it has produced a wealth of important recommendations, reports and initiatives, which, providing things progress as planned, will make 2016 a very exciting year to think and write about.

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