ANNUAL REVIEW OF CORPORATIONS LAW

by

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INTRODUCTION

There is little doubt that 2017, as I see it at this time in mid-November as I prepare this overview, has seen relatively minor legislative activity on the part of the government. There have also been relatively few major policy considerations considered by the government other than in relation to problems arising out of the operations of the banking and financial sector. But in September 2017 the extraordinary Banking Executive Accountability Regime Regulations (BEAR regulations) were released for public comment but only seven days allowed for such comment) by the Federal Treasurer. This extraordinary knee-jerk reaction on the part of government to deal in what was hoped would be a conclusive manner with the alleged failure on the part of certain sectors of the financial and banking institutions to behave with the appropriate "culture" expected of senior officers in that area of our economy has caused considerable disquiet. It is likely that this draft "regulation" will be significantly amended in parliamentary debates that will follow in 2018.

The major reforms to be implemented following the implementation of the Murray Report into financial institutions have by and large not yet appeared. We await with interest the major initiatives. These will include a proposal to place the Australian Securities and Investments Commission (ASIC) in a position where it will be able to review the documents issued by relevant companies to the public when funding support or investment is sought by the relevant companies. This is an intriguing initiative suggested by the Murray Report. It will be fascinating to see how ASIC, with a minimum amount of practical experience in this type of activity, may be able to cope with the obligation to review documentation of a high-profile nature.

ASIC has been considerably relieved of some of its more technical obligations as a result of the passage of legislation to allow it to enter into arrangements where cost recovery is a feature of its operations. It is unnecessary to deal in detail with these provisions but they are of a far-reaching nature and reflect the government's support for recommendations in the Murray Report.

There have been relatively few high-profile court cases, other than the three cases against three high-profile trading banks, brought by ASIC. They are briefly discussed in this overview, dealing with the traditional areas of directors' duties, corporate governance, remedies for shareholders (although in this area the courts have been more active than perhaps in the past). However, there have been many pieces of litigation involving corporate collapses, winding up of companies, disqualification of directors and related matters. The use of the infringement notice power by ASIC (and indeed by other regulators under other legislation), has continued to attract attention and other regulators and related fields.

My comments may seem harsh but it is my view that the use of the infringement notice in the future will continue to damage the work undertaken by the regulators. But on the other hand AUSTRAC has certainly played its part in highlighting the assertions by many, including this writer, that corporate compliance is far from adequate in Australia at the current time.

As in previous editions of this overview, I shall deal first with the legislation that has been introduced and considered by Parliament, Bills that are likely to be the subject of vigorous debate in the early part of 2018, and the work of ASIC in particular. A number of important discussion papers have been issued by ASIC. It has taken on a significantly higher profile role in the latter part of this year. The interaction between it and the Australian Prudential Regulation Authority (APRA) in dealing with these matters is also briefly discussed.

The appointment of Mr James Shipton as the new Chairman of ASIC (Greg Medcraft has retired) has also generated some anticipation in the way the regulator will perform in the future. The recent settlement by ASIC of two of its three cases against the major trading banks in relation to alleged market rigging allegations referred to earlier was a significant victory for Mr Medcraft at the time of his term of office coming to an end. It reflects a new era when litigation will be used more often to achieve results rather than relying on the media, politicians and commentators, to hopefully create a different cultural approach. In the second part of this overview I shall consider some recent decisions from our courts and other initiatives in that context (and perhaps do a little bit of crystal ball gazing).

One of the more important initiatives taken by the government has been the release of an exposure draft dealing with the important topic of whistleblowing. This area of the law has been largely overlooked in Australia in terms of dealing with corporate misbehaviour and the ability of individuals and others to ensure that bad behaviour is brought under serious consideration by regulators and others. There is now a real intention being shown by the Federal Government to do something quite creative in this area.

I am happy that the government at this stage has chosen not to introduce a fee reward for whistleblowers along the lines of the US and Canadian initiatives. These prospective initiatives have sparked significant debate and interest in Australia. There is no place, in my respectful view, for this type of approach in dealing with these matters. As the Australian Competition and Consumer Commission (ACCC) will attest, rewards of this kind are not the best way to encourage compliance and good behaviour. Immunity from prosecution may be a far more effective incentive to ensure that compliance becomes a matter of greater importance to companies and those who occupy senior positions in these companies. They will wish to ensure that the laws of the land have been complied with. But this is an issue which is likely to be considered further in 2018.

What is unfortunate, however, is that the Australian States and Territories do not always see eye to eye with the initiatives that the Commonwealth wishes to take in dealing with this important area of our law, and the continued breakdown in ensuring that there is a satisfactory national approach to corporate and other regulation. This failure remains a matter of great disappointment to me and to many others who have commentated in this area of regulation. The fact that the Commonwealth Government has to seek a referral of powers from the States (and Territories) every five years to ensure that we have a comprehensive national regime in the corporate law area is one example of how our federal system of regulation continues to be flawed. This has caused significant costs to the community as well as malfunction in the government's capacity to deal effectively with this area. And now as we go press the government has agreed to establish a Royal Commission on banks and financial services. I have not yet reviewed the terms of reference. I can nevertheless assume they are are far reaching.

I would like to thank Andrew Julian, a paralegal who has spent the last few weeks assisting me in the research involved in writing this overview, and putting together ideas for the chapter in giving me considerable support in undertaking this task. The overview is being written as I end my career as a partner and consultant in major law firms in Australia. I have now taken on a more independent role which will enable me to provide perhaps a cheekier set of observations about the behaviour of our corporate community and those who advise it.

LEGISLATION ENACTED BY THE FEDERAL GOVERNMENT IN 2017

The most significant statutory enactment during 2017 in the corporate law area this year is the *Treasury Laws Amendment (2017 Enterprise Incentives No 2) Act 2017* (the safe harbour legislation).

I have named this legislation the safe harbour legislation because the most significant aspects of this legislation is the inclusion of important provisions aimed at providing a "safe route", or fallback position for directors who are faced with the problem of trying to save companies that are in financial difficulty. This can be achieved even if the directors are unlikely to be able to trade the company's way out of these financial difficulties and do so without fear of losing the benefit of protection against the insolvent trading legislation: s 588G of the *Corporations Act 2001* (the Act). The Prime Minister of Australia, Malcolm Turnbull has favoured an American-type solution (the Chapter X solution in the USA) where in effect all the debts of the insolvent company are forgiven and the company starts anew. That is a dramatic initiative that is never likely to be adopted in Australia. However, the recommendations of the Productivity Commission in its report *Business Set-up, Transfer and Closure* (September 2015) (See the discussion in the 2017 Annual Review of Corporations Law pp xviii to xix) which led to the safe harbour legislation, were an important step forward.

These changes to the Act should enable directors to act more confidently in trying to rescue companies that are close to insolvency or need to be administered in some rescue operation. The proposals as set out in the safe harbour legislation do not contain a set of provisions that are as general as those proposed by the Productivity Commission.

The legislation contains lengthy provisions which aim to allow directors to take a more "aggressive" and hopefully successful action to enable companies to trade themselves out of such financial difficulty. The amendments contained in s 588GA of the Act (a new provision) will soften the impact of s 588G (the insolvent trading provision). In essence, the legislation provides a non-exhaustive list of steps to be taken by directors which should enable the court to determine whether a director should be excused from a prosecution of insolvent trading, where the director took action which could be assessed as reasonably likely to lead to a more successful outcome. In effect the director must prove that he or she took steps to prevent misconduct occurring in the course of the rescue operations; also that the director took steps to keep financial records; the director obtained appropriate advice; the directors informed themselves of the overall financial position that was facing the company at the time; and that the director implemented or began to develop suitable arrangements to ensure that the company would improve its operations in the future. However, additional matters may be brought to the attention of the courts by the directors in their support.

If the director establishes these matters, the court is "instructed" by the relevant new law not to find against the directors for insolvent trading. In my view, the language used to draft the relevant provisions is tortuous. It adopts what is known in the law as a "black letter law approach". It is likely that there will be some difficulty facing the courts in excusing directors in appropriate cases although It is a significant improvement on the current statutory business judgment rule contained in s 180(2) of the Act. It will be fascinating to see how these new provisions will be administered by ASIC, and used by liquidators and others who may otherwise challenge the rescue attempts taken by directors.

The legislation also abolishes the use of *ipso facto* clauses which have been regarded as a critical disincentive to the natural operation of the law of contract. It is very recent legislation and as yet there have been no cases to my knowledge dealing with the operation of the legislation. (However, see Nicholls R and Buchan J, "The Law of Unintended Consequences: The Effects of Voiding Ipso Facto Clauses in Business Format Franchise Agreements" (2017) 45 *ABLR* 433.)

CROWD SOURCED FUNDING LEGISLATION IN PLACE

After a number of years of debate and consideration the Parliament has finally enacted the *Corporations Amendment (Crowd-sourced Funding) Act 2017*. As Commissioner John Price of ASIC has indicated in announcing the commencement of the operation of this legislation on 28 September 2017, the new law:

> provides an opportunity for small to medium-sized businesses to access an alternate source of capital without the regulatory burden of conditional fund raising. [ASIC has issued new guidelines] which will help public companies and crowd funding platform operators comply with their obligations under the [crowd sourced funding] regime while supporting investor confidence.

It is unnecessary to discuss this particular initiative in detail.

ASIC SUPERVISORY COST RECOVERY ACT

This important legislation, which was recommended by the Murray Report, will enable ASIC to carry out many of its functions including the lodgment and registration of documents and maintenance of registers where ASIC provides services currently for a fee. The legislation, while not lengthy, sets out a very significant set of obligations which must be complied with for ASIC to engage in this arrangement with users of its services in a way that will be of considerable assistance to ASIC in allowing it to identify and respond to emerging risks in the financial sector and allocate its costs in line with its regulatory activities so as to reduce cross-subsidisation.

THE BEAR REGULATIONS (THE BANKING EXECUTIVE ACCOUNTABILITY REGIME)

On 22 September 2017, following a considerable amount of agitation for reforms to the law to capture unacceptable behaviour in the financial services and related areas (especially banking), the Treasurer, the Honourable Scott Morrison, released for comment initiatives that had been highlighted in the Budget Papers tabled in Parliament earlier in 2017. However, the BEAR Regulations, as they are referred to, were released to the public for comment for only seven days – an extremely problematic, if I may say so with respect, exercise of power by the government. It is interesting to note that similar regulations in the UK took nearly three years to be settled.

This proposed regime is a culmination of developments following the release of the House of Representatives Standing Committee Report (the Coleman Report) *Economic Review of the Four Major Banks* in September 2016. One of the critical comments in this report, otherwise known as the Coleman Report, was this statement:

> The major banks have a "poor compliance culture" and have repetitively failed to protect the interests of consumers. This is a culture that senior executives have created. It is culture they need to be accountable for.

Following this recommendation from the Coleman Committee, the Federal Government announced in discussion papers in July 2017 that it would be introducing legislation to virtually force the banking and related industries to significantly improve their culture and to provide better protection for the community.

What was regrettably forgotten by the Federal Government, and others who have continually pleaded for stronger penalties and more regulation in this context, is the fact that both ASIC and APRA already have significant powers under various pieces of legislation and regulations administered by those agencies, to ensure that the appropriate culture is adopted by these institutions. The relevant laws, include the Commonwealth Criminal Code of 1995 (the relevant provisions of which were not implemented until 2001), create a statutory requirement for companies and others to adopt a culture of compliance in relation to Commonwealth criminal sanctions. (Regrettably this legislation was not copied by the States and Territories as was anticipated when it came into operation in 2001.) In addition, there are specific provisions in relevant legislation which is how the regulators, especially ASIC and APRA, ensure that appropriate steps are taken to embrace an appropriate culture.

The BEAR Regulations once they become law will introduce a responsibility and accountability framework which goes far beyond the current legislative reach of the provisions in operation. The government has introduced the Treasury Laws Amendment (Banking Executive Accountability and Related Measures) Bill 2017 (the BEAR Bill)) which embraces the reach of the Regulations. But there has been some recognition by the government that perhaps these proposed rules may be too stark.

In essence the BEAR regulations (which will become a statutory set of rules) will impact on organisations described as "authorised deposit-taking institutions" (ADI) or subsidiaries of such organisations (these terms are defined very broadly). Individuals who have actual or effective responsibility for control or management of ADIs, or a subsidiary as governed by the extended definitions, will be accountable if they come within the reach of the proposed regulations.

The aim of the consultation paper, in extending the obligations under the proposed regulations, was to ensure that "individuals who have significant influence over conduct and behaviour, and whose actions could pose risks to the business and its customers" would be made aware of their obligations.

A key feature of the regulation is that it will apply to all ADIs and accountable persons. The reach of the proposed regulations is extremely wide. The ADI must comply and ensure that key personnel, comply with the rules. The reach of the regulations is intended to ensure that an ADI conducts its business (and all accountable persons follow suit) with appropriate policies, integrity, skill, care and diligence. It is hoped that APRA, the

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main regulator, and bodies working with it, can be certain that the organisations involved will be acting reasonably and in an accountable manner. An appropriate risk management program is required to be established by the ADI.

APRA may require an ADI to defer the remuneration payable to the relevant accountable persons for a period of up to four years if there are breaches that occur. In addition APRA may seek penalties against the ADI and against individuals which are quite significant. A $1 million maximum penalty may be sought by APRA in relation to the most serious breaches and there are similar very large penalty fines that may be imposed on others. APRA is to be given far-reaching powers to disqualify accountable persons who engage in conduct which is regarded as serious. In the covering explanatory memorandum it is suggested that any decision taken by APRA to disqualify a person would only be justified in serious cases but there is little guidance as to how this responsible task will be exercised by the regulator. It has also been suggested in the media commentaries that the government will introduce a defence which will be available to accountable persons and to the ADIs, to challenge disqualification orders that might be made by APRA.

The language in the consultation paper suggests that strict liability/reversal of onus of proof approach would be taken in much of the drafting, imposing an obligation on both the ADI and accountable persons to defend themselves from either having to pay fines or facing disqualification which may be sought by the regulator. I have not had the time to review the BEAR Bill in detail.

It is most unfortunate that this type of legislation is being introduced in the manner that the government has chosen to do so. The government's loss of a clear majority in the Parliament as a result of the disqualification of members of Parliament following a decision of the High Court of Australia has led to further moves being generated by some disenchanted members of Parliament fed up with the way in which the banks and financial institutions have behaved. Political pressure has led to the establishment of a Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry on 30 November.

I have not had the opportunity to consider the terms of reference of this Royal Commission but I repeat my view that such a Royal Commission is unnecessary.

The Senate Economics Legislation Committee charged with the task of reviewing the BEAR Bill presented a report to the government on 24 November 2017. The Committee supported the legislation but recommended that the proposed start date of the proposed legislation be delayed to allow APRA and other regulators time to ensure they could deal adequately with the introduction of the legislation. It has not been possible for me to consider other aspects of the Report.

This legislation will no doubt be the subject of detailed debate in the Parliament in 2018.

NEW CHAIRMAN OF ASIC APPOINTED

As this overview chapter is being finalised, the controversial and very high-profile eight-year term of Greg Medcraft, the current Chairman of ASIC, comes to an end. The new Chairman, appointed by the government, James Shipton, will have a very hard act to follow. He has indicated that he will support the initiatives that have been taken recently by ASIC.

It is my view that many of the criticisms made by ASIC and its Chairman about the lack of appropriate culture and the absence of appropriate good behaviour or ethical behaviour on the part of financial institutions and their officers, have been greatly over-emphasised by politicians, the media and many others.

It is my view that it was the failure of ASIC, in particular under the leadership of Greg Medcraft, to bring appropriate litigation in earlier years (certainly the trend has changed now) against persons in high-profile positions in the banking and other organisations where allegations of breaches of the law were being made, that led to a large part of the concern about this problem. There has been far too much talk about alleged breaches of the law, poor culture, and bad practices, rather than taking the matters via court action. The fact that two of the major pieces of litigation against the three trading banks have been settled, on what appear to be very favourable terms as far as ASIC is concerned (in terms of admissions of liability in certain aspects of the behaviour) and the imposition of significant monetary penalties (on a civil basis only of course), is a reflection that something was not quite right in this area of the business environment.

James Shipton, a senior member of the financial and regulatory community in New York and prior to that a lawyer in Australia, will commence as Chairman in early February 2018. Peter Kell, the Deputy Chairman, will be the Acting Chairman of ASIC in the meantime. Mr Shipton has indicated that he intends to adopt a similar approach to that taken by his predecessor. In the last 12 months in particular we have seen an increase in the amount of high-profile litigation being brought in the type of areas where the complaints which have led to the growing demand for a banking Royal Commission and similar demands. In a later part of this review I discuss some of the cases in which significant actions have been brought by ASIC and the results have been less than satisfactory from ASIC's perspective. ASIC has gained some victories but also suffered a significant number of losses in these cases.

James Shipton will have a significant task ahead of him together with the continuing Commissioners, Peter Kell, Cathie Armour and John Price, to ensure that ASIC's recent successes should continue as well as the considerable support for active and strong action by the regulators in the context of this area of the financial and other business sector. Recent successes in the cases against the ANZ Bank and the National Australia Bank (see discussion under "Bank bill swap rates action") will no doubt provide ASIC and its Commissioners with much encouragement in continuing to adopt a policy of enforcement where appropriate.

In this context, it is very interesting to read the ASIC Enforcement Report that is published every six months. It reflects a strong approach by ASIC in dealing with the regulatory environment. I have just confirmed that ASIC continues to use the infringement notice regime too regularly in dealing with these matters.

THE PROPOSED WHISTLEBLOWING REFORMS

In October 2017, the Honourable Kelly O'Dwyer, Minister for Revenue and Financial Services released for comment by the community an Exposure Draft of the *Treasury Laws Amendment (Whistleblowers) Bill 2017* (the Whistleblowers Bill). It is hoped to have this considered in Parliament early in 2018 and to establish appropriate whistleblower protection that has been recommended by the Parliamentary Joint Committee (PJC) on Corporations and Financial Services. That far-reaching report, referred to as "Whistleblower Protections", has recommended, not unanimously in terms of the specific proposals, but in a way that suggests that there is common support for the introduction of a comprehensive regime, a new set of rules to deal with the regulation of whistleblowing and related matters.

The PJC proposals covered a much wider variety of matters, including the wish of the majority of the committee which favoured the introduction of a reward system for whistleblowers. This was based in part on developments occurring in the USA and Ontario, Canada. It also proposed a comprehensive protection for whistleblowers, with the establishment of a "Whistleblower Protection Authority". The question of whether a reward should be provided for in the second stage of the whistleblowing legislation to be introduced will be considered by the government next year.

The existing whistleblowing protections currently in place in Australian legislation environment are to be found in the Act, and in a range of other legislation such as the *Banking Act 1969*, the *Insurance Act 1973*, the *Life Insurance Act 1995*, and the *Superannuation Industry (Supervision) Act 1993*. There are also provisions in place in our income tax regime. In the Exposure Draft released for discussion and comment, the government has not agreed to adopt the comprehensive approach suggested by the PJC referred to earlier. The Exposure Draft concentrates on a number of reforms to be contained in amendments to the Act, and with some overflow provisions also to be introduced as amendments to the *Taxation Administration Act 1953*. There will be consequential amendments to the other pieces of legislation referred to earlier.

A major aim of the Exposure Draft is to consolidate the existing protections by expanding the class of individuals that will have available to them appropriate protection if they act as whistleblowers in seeking how to tackle and deal effectively with breaches of the law. The Exposure Draft also proposes to broaden the type of information that the whistleblowers bring to the attention of the regulators, where this particular act of whistleblowing will be protected by ensuring that the whistleblowers will not be prosecuted and cannot be sued effectively by those affected by their reporting. Also proposed is a wide provision to govern the type of misconduct that is the subject of the possible protection under the whistleblowing regime. There will be included in the legislation specific provisions to protect the anonymity of the relevant whistleblower as well as the information that they provide. Under this legislation a significant onus will be placed on organisations (mainly corporations, such as large proprietary companies as well as public companies), to put in place their own whistleblowing policies. This approach parallels the current policy of the government to change in the Criminal Code of 1995 (effective from 2001) which calls for the putting in place of satisfactory procedures to ensure a culture of compliance. Justice French, in the Federal Court, noted in *Re Chemeq* (2006) 24 ACLC 806; 58 ACSR 169; [2006] FCA 936 such compliance policies and programs, must not only be inserted into company corporate management regimes, but kept up to date and refreshed on a regular basis.

The provisions under the current regime administered by the Commissioner of Taxation rely on anonymous reports being made to the Australian Taxation Office enabling it to obtain information from whistleblowers. But no protection in law is specifically guaranteed under this proposal. The proposed legislation will amend the *Taxation Administration Act 1953* to provide a regime that will provide the same protection that will exist in other areas of the law.

There is little doubt that this is an important step. It will be fascinating to see how quickly the government will proceed with the bringing on for debate and in consideration of the very comprehensive provisions contained in the Whistleblowers Bill.

I am assuming that many amendments will be made to the proposals in the Exposure Draft. For example, the Law Council of Australia has already proposed the inclusion of further protection for whistleblowers and the elimination of certain overbearing powers that will be vested in regulators if the Whistleblowers Bill goes through in its current Exposure Draft form. A particular concern raised in commentary so far is that bodies such as ASIC and similar regulators should not be able to interfere with fundamental liberties and protections that need to be contained in this legislation where persons decide to act as whistleblowers.

In my view, while this Exposure Draft was a welcome initiative, it would have been better, as has been suggested by the PJC, for whistleblowing to be dealt with across the board. The further legislation to be introduced in 2018 will no doubt recognise that this major initiative is being adopted in a two- or three-stage approach. The significant improvement to the way regulation occurs in this country if we have an effective whistleblowing regime will be the introduction of a broader definition by Australian organisations of the need for compliance with appropriate regimes within the organisations, which will not only include whistleblower protection, but also a range of other matters as enunciated in the Criminal Code.

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After reviewing submissions on the Exposure Draft, on 7 December 2017 the government introduced the *Treasury Laws Amendment (Enhancing Whistleblower Protections) Bill 2017* into the Senate. I have not had the opportunity to review the Bill.

ASIC REPORTS AND INITIATIVES

NEW CHAIRMAN OF ASIC APPOINTED

As noted earlier, James Shipton will become the Chairman of ASIC from February 2018. Mr Shipton has had a distinguished career in law, merchant banking and related activities. He has indicated that he will follow the leads provided by ASIC under the chairmanship of Greg Medcraft. It will be interesting to see how effective he will be in continuing with the aggressive activity adopted by ASIC in the last 12 months or so, in particular pursuing breaches by high-level officers in the banking and financial and related organisations where the appropriate "culture" has not been adopted by those organisations.

ASIC'S MAJOR INITIATIVES IN 2018

The most important task facing ASIC in 2018 will be to implement the government's very aggressive reform agenda illustrated by the introduction of the BEAR Regulations referred to earlier. It will also pursue the various recommendations made by parliamentary committees on how the power of ASIC should be exercised. In that context. Most important for ASIC will be to put into effect the reforms contained in the Murray Report on Financial Institutions supported by the government.

It has taken a considerable time for the government to respond to the recommendations and to introduce appropriate legislation to empower ASIC in different ways to deal with some of the difficulties that were highlighted in the report. In a number of cases these issues are linked to the problems with the governance of financial and related institutions over the last two to three years. At the time of writing there have been no statutory amendments introduced into parliament to deal with the particular recommendations of the Report, other than those relating to cost recovery which ASIC should be pursuing. For example, the important changes to the way in which ASIC was to become a self-funding organisation have been appropriately implemented through the *ASIC Supervisory Cost Recovery Levy Act 2017*.

The significant powers that ASIC will enjoy, assuming that the proposals in the report are implemented, will include the ability to help formulate the way in which documentation that is issued by corporations and organisations in raising funds and investment in their organisations, can be monitored and directly influenced by ASIC. The recommendations of the report (recommendation 22) into this particular area were briefly these:

- to provide ASIC with the power to intervene where there is a risk of significant detriment to a class of consumers; and
- to provide ASIC with the power to require or impose amendments to marketing and disclosure material, warnings to customers or terminology changes, restrictions on the distribution of products, and bans on products.

These proposed powers will enable ASIC to be proactive in its regulation of the market as opposed to merely reacting to breaches, and are recommended with the qualification that the power is to be used sparingly and with a high level of accountability on ASIC's behalf.

EXTENDING THE POWERS OF ASIC

On 19 October 2016, the Minister for Revenue and Financial Services, the Honourable Kelly O'Dwyer, appointed a taskforce to review the enforcement regime of ASIC. A position paper published on 6 September 2016 suggested that ASIC should be able to take action to ban senior managers from managing financial services in the business sector. The government has pursued this recommendation as can be seen in the BEAR Bill, discussed briefly above.

The position paper contained a further suggestion that the banning powers currently enjoyed by ASIC could be improved upon by enhancing the power of ASIC to assess and address the way in which managers and senior persons in relevant organisations were dealing with the questions of corporate culture and appropriate behaviour. At the time of writing this particular part of the overview the final position of the government on this proposal had not been formalised.

The Taskforce also proposed that ASIC should have the power, if a course of action was being pursued under to s 920A of the Act, to ban a person from:

1 performing special functions in the financial services business including the management of a financial services business;

2 performing any function in a financial services business; and

3 ensuring that ASIC enjoyed similar powers in respect of the regulation of credit activities of companies.

In the view of the Taskforce, such an enhancement of powers would ensure greater flexibility in the use of the banning powers. The Taskforce believed that ASIC should be empowered to move to have a person banned from fulfilling a particular position within an organisation (for example as a senior manager or even a manager) in relation to all financial services organisations. Currently, where non-financial services are involved in the relevant activities, ASIC cannot issue a banning order in the context of financial services.

The Taskforce did not foreshadow or replicate the proposals contained in the BEAR Regulations as drafted, but rather proposed that the banning power should be triggered where ASIC has reason to believe that the person is:

1 not a fit and proper person to provide a relevant financial service or services or to perform the role of an officer or senior manager in a financial services business; and/or
2 inadequately trained, or is not competent, to provide a financial service or financial services or to perform the role of officer or senior manager in a financial services business.

The Taskforce also proposed that the banning order could be extended to officers, partners, or trustees who had been found to have been involved on more than one occasion, in the financial services or credible licensee, where that organisation had been the subject of a report by the Australian Financial Complaints Authority regarding the failure to comply with the ruling by that authority, or where the corporation had been wound up and a liquidator had lodged the report under the provisions of the Act about the relevant corporation's inability to pay its debts as and when they fell due.

In addition the Taskforce also proposed that ASIC should have the power to ban an individual who had been involved in a financial services or credit licensee organisation, if the person had breached any duties under ss 180–183 of the Act. In effect, the extent of the new banning power would be to enable ASIC to focus on the relevant individual's fitness, capacity and competence to ensure that a relevant financial services was performed by a senior person instead of introducing new obligations or duties. Whilst this new power would be limited to "officers" and "senior managers" (as these terms are defined in the current legislation), they nevertheless would extend significantly the ability of ASIC to move quickly to regulate behaviour of senior persons in appropriate circumstances.

As noted above, it is my view that the BEAR Bill as proposed by the government has gone too far. Until we have seen appropriate litigation involving our courts' consideration on the use of the banning powers, and challenges brought against the issue of banning orders by ASIC is not sufficient to trigger the legal operation of such banning orders.

We should not be extending greater powers than the power to recommend such banning orders, subject to challenge in an appropriate court environment, where the onus is on the government or the regulator to establish that a breach of law has occurred, rather than requiring the person against whom the banning order is being recommended, to prove his or her innocence. The use of the reversal of onus of proof or the strict liability regimes that are contained in many of these initiatives are unacceptable and should be removed from our statute books, except in extreme cases of terrorism or wartime activities being present.

FURTHER EXTENSION OF ASIC'S OVERSIGHT OF BANKING AND OTHER FINANCIAL AND RELATED MATTERS

As noted elsewhere in this overview, ASIC has been criticised for its failure to pursue alleged breaches of the laws by directors and senior officers of companies, and its failure to pursue appropriate measures to tackle some of the problems that have affected the operation of the economy in this particular area, and the many corporate collapses that have occurred. It has been the subject of reports from parliamentary committees and its conduct commented on by judges in various cases. So it is interesting to note that the regulator has now set out on a very positive and aggressive program of reviewing operations and creating opportunities for implementation of measures to provide better protection against similar collapses occurring in the future.

The most important document that ASIC continues to produce on a regular basis now is a review of enforcement outcomes through all the relevant periods under consideration. In the most recent report available, REP 536, *ASIC enforcement outcomes: January to June 2017*, ASIC describes the role it has taken in a range of activities and initiatives. There were a number of investigations conducted by ASIC into financial and related organisations and court proceedings of a minor nature in the context of some of the more significant litigation against the three of the major trading banks for alleged market rigging activities discussed elsewhere. (See New Chairman of ASIC appointed.)

ASIC has continued to focus on culture and incentives in the financial sector in particular, as well as in other markets. It is now very heavily involved in looking at threats as a result of cyber invasion and the problems associated with general market integrity and corporate governance questions. There is little doubt that ASIC has become more vigorous in enforcing the law. ASIC has obtained important enforceable undertakings from Westpac Banking Corporation, the Australian and New Zealand Banking Group Ltd and Macquarie Bank Ltd in relation to wholesale foreign exchange businesses which it was alleged had been conducted by the relevant banks between January 2008 and June 2013, in a way which had disclosed a number of potential breaches of the law.

Another major report issued by ASIC in the recent six-month period is report REP 539 *ASIC Regulation of Corporate Finance: January to June 2017*. The purpose of this report is to provide greater transparency about the role that ASIC plays in the regulation of corporations and corporate transactions in Australia and highlights and discusses key statistical information and observations that ASIC reaches in reviewing its regulation of fundraising, mergers and acquisitions, corporate governance and other general corporate finance activities. The commentary included and the models that ASIC discusses in the report provide a useful backdrop to the way in which ASIC will embrace the recommendations of the Murray Report into Financial Institutions.

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There are many other matters that ASIC has commented on in numerous reports and documents published on its website from time to time illustrating the activities undertaken by this organisation. When these are reviewed together with the actions being taken by APRA, particularly in relation to the current focus in litigation and reporting into the affairs of the Commonwealth Bank of Australia, it is perhaps not surprising that a Royal Commission into banking has been established.

But I do not believe this is the most effective way of changing the "culture" seen as desirable by many in Canberra. Laws framed in such sweeping and general terms will be closely scrutinised in important cases and the unwillingness of our courts to give weight to legislation that is not drafted along traditional black letter law formulas can only lead to frustration, delay and significant legal costs.

ASIC – PROPOSAL TO REFORM THE LAWS RELATING TO PHOENIX ACTIVITIES

A major problem area for ASIC, and for governments generally in trying to eliminate fraudulent and illegal activities in the markets, is the ability to control the operation of so-called phoenix activity situations which have increased in number and intensity and have been the subject of a number of reports and recommendations for reform.

The most significant of these is the report entitled *Phoenix Activity: Recommendations on Detection, Disruption and Enforcement* by Professors Helen Anderson, Ian Ramsay and Michelle Welsh, and Mr Jasper Hedges (Melbourne University, February 2017), which made significant recommendations to combat illegal phoenix activities. Such activity is broadly defined as "the misuse of the corporate form to exploit the privilege of limited liability". In the Treasury consultation paper *Combatting illegal phoenixing*, it is stated that "whilst the scale of illegal phoenixing ranges from the opportunistic to the systemic, its common characteristic is that when a company is unable to pay its debts, its controlling directors act in a manner which [creditors may have] access to the entity's assets to meet the unpaid debts".

The main reform measure proposed was to define phoenix offences in a way to ensure that the legislation prohibits the transfer of property from one company to another company if the main purpose of the relevant transfer was to prevent, hinder or delay the way in which that property could become available for division amongst the creditors of the company from whom the property was being transferred. This would mean in fact that the particular offence in the context of the Corporations Act would operate in a similar manner to the way s 121(2) of the *Bankruptcy Act 1966* of the Commonwealth operates. That section provides that the main purpose in making a transfer of property will be taken to be a purpose that is proscribed, if "it can reasonably be inferred from all the circumstances that, at the time of the transfer, the transferor was, or was about to become, insolvent".

Whilst some presumptions of insolvency will apply, such transactions can generally be regarded as void against the liquidator or persons in a similar position. Where the offence occurs, creditors and liquidators including ASIC would be in the line to sue for compensation in respect of the loss caused by the relevant conduct, the subject of the transfer of property. The remedy can be sought against all those persons who are knowingly involved in the conduct of the particular activity in accordance with the operation of s 79 of the Act.

Defences are available under s 121(4) of the Bankruptcy Act and these defences would be replicated in the Corporations Act to ensure there was no overreaching in the impact of this prohibition.

LEADING CASES

INTRODUCTION

The year 2017 has not been marked by many spectacular and far-reaching decisions from our courts in the areas of corporate law, especially in the areas of directors' duties, corporate governance, remedies for shareholders and related matters. There have been some decisions which have been high-profile in other ways (such as the three major cases brought by ASIC against the three major trading banks with two of them being settled which have been discussed elsewhere below), and a range of cases by ASIC seeking penalties against directors, officers, securities markets operators where allegations of breaches of the law have been pursued. I will deal only with what I regard as high-profile or important cases.

DUTIES OF DIRECTORS

Perhaps the most significant, although for reasons that will become apparent this should not be so, from my perspective, are the decisions of Robson J (now retired from the Supreme Court of Victoria) in *ASIC v Flugge* [2017] VSC 117. I shall discuss in detail only the penalty decision. The decision on whether there had been breaches of the Act, discussed very briefly in the 2017 overview (at p xvii), required Robson J to rule on whether Flugge, who was the Executive Chairman of the Australian Wheat Board (AWB), had breached his duties to act with care and diligence (s 180(1) of the Act). Whilst he held that there had beev a breach of s 180(1) of the Act, the judge ruled against ASIC in relation to ancillary claims that he had also breached his duty to act in good faith in the best interests of the company (pursuant to s 181 of the Act). These claims were made in relation to dealings that had been conducted between AWB and the Government of Iraq in relation to the "Oil-For-Food" program. This program had been criticised by the United Nations and various international sanctions had been imposed against Iraq.

This decision has been the subject of much criticism in the legal community for various reasons. It is appropriate to comment, however, on the question of penalties. It is useful to remind readers I wish to commence this comment by noting that the collapse of AWB, and the subsequent Royal Commission into the activities of the AWB delivered by Justice Cole (*Inquiry into certain Australian companies in relation to the UN Oil-For Food Programme*, 2006), and a number of prosecutions brought by ASIC, as well as other actions brought in relation to the activities of AWB, have been a particular highlight in the Australian corporate law scene and in the evaluation of the duties of directors. The penalty decision of Robson J staggered many sections of the community because of the very low penalties imposed by Robson J against Flugge. Some say that hard cases make bad law and there is little doubt that the litigation involving Flugge (and his co-defendant Geary), which lasted many days, producing hundreds of pages in the judgments of Robson J, is a classic example of a hard case.

The decision of the judge to impose a modest monetary penalty of $50,000 and disqualification being considered as largely irrelevant in the context of the man's age and the fact that he had retired from all positions of a similar nature, have resulted in considerable debate in the legal and business communities. In a note that is to be published in the *Company & Securities Law Journal* in 2018, Tim Bednall, a senior lawyer and partner of a major law firm, criticises the litigation brought by ASIC as a case which ASIC pursued against the director, to make him responsible in the eyes of the community for reprehensible conduct by others, without the law requiring ASIC to prove any dishonesty or crime or liability.

There is considerable debate as to whether s 180 of the Act is in need of significant "repair" or replacement, because it permits the court to impose civil penalties and disqualification for a breach of the duty of care. Only directors and officers are liable for prosecution in relation to a breach of the section and it has been used in circumstances where perhaps a different approach might well have been considered relevant by the court in dealing with corporate collapses. This is particularly relevant, it has been argued, where a significant sum of money is lost and ASIC believes that the persons who should be made directly responsible to make proper compensation. Surely class actions provide an alternative course of action to seek retribution many would argue.

Section 180 of the Act Act has been in place for a number of years in one form or another and there are interesting and important judgments in which directors and senior officers who have been responsible for the activities of the company which have led to significant losses, have been penalised. In last year's Annual Review I discussed the decision of Edelman J in *Australian Securities and Investments Commission v Cassimatis* [2016] FCA 1023.[1] The relevant allegations made against the directors of Storm Ltd concerned breaches of s 180(1) of the Act. It was alleged the directors had not done enough to ensure that the investment activities that the directors invited members of the public to engage in were not sufficiently reviewed and researched to ensure that success rather than the disastrous financial consequences would follow. The Court agreed with these assertions by ASIC.

1 See Corporations Legislation 2017, Annual Review pp xxvi–xxviii.

I have highlighted the fact that the recently retired Chairman of ASIC (Greg Medcraft) has sought (with the support of his organisation) significant increase in penalties for breaches of the Act. The government is currently seeking further views from the community on proposed increases in penalties and other changes to the law relating to penalties to be imposed. In contrast to the *Competition and Consumer Act 2010*, the Act does not carry with it a range of very significant default regimes dealing with "bad behaviour" on the part of directors in the context of traditional company law activities. Where semi-criminal conduct is engaged in (such as insider trading and manipulation of the market and related matters), there is an opportunity for ASIC to seek criminal and related penalties. ASIC has certainly not been shy in using its powers in relation to those provisions to pursue remedies.

My final comment on the Flugge case is that it brings to an end a very sad chapter in the history of ASIC's administration of corporate law. It is my view that ASIC should have pursued more difficult cases in relation to the collapse of AWB, as well as other financial disasters. Had such action been brought and considered by the courts, we might have seen some significant commentary to assist in the reformulation of the current penalty regime.

ACCESSORIAL LIABILITY OF DIRECTORS

One of the more interesting questions surrounding the potential liability of directors for breaches of the law, especially the fundamental duties imposed upon them by virtue of ss 180–184, the possibility that litigation may be brought against relevant directors (and other officers in appropriate cases) is whether the parties can rely on the accessorial liability provisions of the Act, and the companion common law rules that may apply. In particular, in the case of *Gore v Australian Securities and Investments Commission* (2017) 249 FCR 167; [2017] FCAFC 13 the Full Federal Court confirmed the ruling that accessorial liability had been proved by ASIC against the defendants in relation to the breaches relied upon by ASIC with respect to the relevant claims. It is unnecessary for our purposes to delve into the nature of the particular contraventions except to note that this brings the Full Federal Court to support the decision of Rares J in finding that accessorial liability had been established. ASIC had successfully proved that Mrs Gore knew of material in each of the

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allegations concerned and thus could be adjudged liable under the relevant provision. The existence of this added ground upon which the regulators and other parties may rely in appropriate cases will be important in future litigation.

FOFA LEGISLATION AND THE DUTY OF DIRECTORS AND SENIOR OFFICERS TO CONSIDER THE BEST INTERESTS OF CONSUMERS AND BORROWERS

Other interesting cases in relation to directors' duties have been concerned with activities involving management investment schemes and the inability or failure of directors and companies to conduct the businesses of management investment schemes in a way to ensure that the interests of investors and borrowers who sought to make a "quick dollar" or a better return on their investment, might have been the subject of proper consideration.

When the Coalition Government was elected in 2013 it sought to amend the FOFA legislation to remove some of the statute provisions included in the specific legislation championed by the former Labor Government to require directors to act with appropriate attention to the interests of consumers and borrowers in relation to significant loans and advances being made to them. The so-called "best interests provisions" contained in the FOFA legislation had been challenged by the Liberal/National opposition when Labor pushed for their introduction. This challenge failed when attempts to repeal the legislation were defeated by a combined Labor-Green and cross-benches opposition.

There have now been some interesting decisions in the courts dealing with aspects of the FOFA legislation. These actions confirm the question of whether the companies advancing sums or entering into arrangements with members of the public which will expose the relevant borrowers and investors to obligations in the documents which have not been fully explained to them in the circumstances have a remedy. The relevant provisions in the FOFA legislation (see now ss 961B, 961G and 961J of the Act plus some ancillary provisions) require the relevant company making funds available to ensure that the company and its representatives comply with the provisions and to ensure that the relevant borrowers were made fully aware of their obligations.

In *Australian Securities and Investments Commission v Wealth & Risk Management Pty Ltd* [2017] FCA 477, Moshinsky J ordered that the company providing funds to borrowers should be stopped from continuing to rely on their rights under the documentation. He ruled that the representatives had failed "to take reasonable steps to ensure that its representatives complied [with provisions in the Act] ss 961B, 961G and 961J" (at [5]). The aim of the provisions was to ensure that relevant information is made available to consumers to enable them to appreciate more fully the nature of the obligations that were imposed upon them under the documentation.

In *Australian Securities and Investments Commission v NSG Services Pty Ltd* (2017) 35 ACLC 17-005; [2017] FCA 345 Moshinsky J was asked to deal with the obligations that were imposed on the lenders, and other providers of finance, to ensure that they did consider whether the best interests of the relevant borrower were taken into consideration. Injunctions were issued in that case and final orders were eventually made. Before reviewing the conduct and compliance protocol of the defendant company, Moshinsky J emphasised the significance of the FOFA amending provisions in the context of a number of corporate collapses "including of the Storm Financial and Opes Prime Groups" (see para [14] of his judgment). He discussed the key provisions of the FOFA legislation and in the absence of any other judicial commentary emphasised that, in line with other provisions of the Act such as s 912A, it was important for relevant companies to "take reasonable steps to ensure that its representatives comply with the financial services laws" (see [31]).

His assessment of the performance of the company and relevant representatives (which was covered in some detail) illustrated that the relevant provisions introduced into the Act by the FOFA amendments had not been complied with (in particular s 961L of the Act), and that appropriate orders were warranted in relation to the improvement of compliance and training and a number of declarations were made.

The decision has received considerable attention in the financial media.

In an interesting civil case in which more general claims are being made against directors and officers, similar obligations to those "captured" by the FOFA requirements, but framed in a different fashion, were held by the Full Federal Court to be imposed on the officers of the relevant company. In *Life Plan Australia Friendly Society Ltd v Ancient Order of Foresters in Victoria Friendly Society Ltd* (2017) 250 FCR 1; 120 ACSR 421; [2017] FCAFC 74 the Full Court of the Federal Court comprising Allsop CJ, Middleton and Davies JJ, agreed that the board of directors of the Foresters organisation was in breach of duties under ss 181, 182 and 183 of the Act. The Full Federal Court held that the relevant officers could be held to have known that the breaches of the Act were occurring. The decision of the trial judge was overturned and liability imposed on the defendant, Ancient Order of Foresters. The trial judge had erred in ruling that there was no cause or connection between the relevant breaches of the fiduciary duty and the profits that had been attained by the Foresters organisation was a mistake and that the linkage had been established and warranted an account of profits against the officers of the Ancient Order of Foresters. The Full Federal Court discussed a number of related cases, but not cases relating to FOFA (see [58]) in which similar issues had been discussed, an order to support its ruling. The court also held that s 79 of the Act (accessorial liability) had been established as the relevant officers of the organisation were knowingly concerned with breaches of the Act in relation to the activities under consideration.

In addition ASIC is currently continuing its prosecution of a case against the Westpac Banking Corporation alleging that it and its senior officers had not complied with the provisions in the FOFA legislation in relation to a significant transaction but details of this litigation are not generally available. However Westpac has stated that it will be strongly opposing the ASIC allegations.

CONTINUOUS DISCLOSURE REQUIREMENTS

The continuous disclosure provisions of the Act are also the subject of interesting decisions. One of the more important decisions is the judgment of Siopis J in *Australian Securities and Investments Commission v Padbury Mining Ltd* (2016) 116 ACSR 208; [2016] FCA 990. It was agreed in this case that certain parties had been in breach of the continuous disclosure requirements\. ASIC and the relevant parties sought a ruling from the Federal Court on the question of penalties. Siopis J was receptive to the way in which the parties who decided to settlethe case had summarised the relevant breaches, and calculation of the penalties, based on the alleged breaches of the law. It is encouraging to see cases being "settled" in this fashion.

COMPLIANCE WITH THE LAW REGARDED AS A VERY SIGNIFICANT FACTOR

In another interesting decision, *Australia Securities and Investments Commission v Sino Australia Oil and Gas Ltd* (2016) 118 ACSR 43; [2016] FCA 1488, Davies J, who had earlier ruled in the case of *Australia Securities and Investments Commission v Sino Australia Oil and Gas Ltd (in liq)* (2016) 115 ACSR 437; [2016] FCA 934that the company had been in breach of various provisions in theAct, added to this ruling with a stern warning on the need of directors to ensure that compliance with the law was observed. The company's managing director, Mr Shao was personally liable, had not behaved appropriately in complying with the law and following the culture of compliance. The pecuniary penalties awarded against the company and against Mr Shao were significant. Shao was disqualified from managing a corporation for a period of 20 years. The fact that he did not understand English, did not speak English, and did not fulfill the obligations required of the company under the continuous disclosure regime, were very significant. In the course of this judgment Davies J commented on the importance of the culture of compliance to be followed by companies in Australia and referred with approval to the obiter dicta of French J in *ASIC v Chemeq Ltd* (2006) 58 ACSR 149.

SHADOW AND DE FACTO DIRECTORS

The continued investigation into the affairs of Queensland Nickel Pty Ltd (QN), which is currently being administered by the liquidator pursuant to actions by creditors against the company, has raised for possible consideration (more likely than not) of the question of when a relevant person might be considered to be treated as a shadow director. When the court will determine that a person who is heavily and financially involved in supporting a corporation should be treated as a shadow director by the courts has become quite significant. It has been made clear by ASIC that it believes that Clive Palmer, a principal shareholder in QN who has advanced considerable sums of money to the company over the years, might well be classified as a shadow director. However, at this stage attempts to bring Palmer into the Australian jurisdiction so that he can be examined by the liquidator and ASIC have failed and the issue remains very much at large.

The potential of Clive Palmer being labelled as a shadow director will have wait until we have more detailed information provided by a court decision. The liquidator has been anxious to ensure that Clive Palmer will be brought within the jurisdiction of the court. Palmer has in turn challenged the validity of the summonses that have been issued against him and the validity of the court proceedings brought against him, his relatives, and those involved in the administration of the company. These challenges have been considered by the High Court of Australia. It decided in *Palmer v Ayers; Ferguson v Ayers* (2017) 259 CLR 478; [2017] HCA 5 that the relevant proceedings and summonses issued were constitutionally valid and that it is appropriate for Palmer to bring himself within the jurisdiction of the courts. Palmer has continued to resist this attempt by the liquidator and others, and in light of the fact that a number of other examinations have yet to be made of various persons involved with QN, these questions remains at large.

The Victorian Supreme Court has also had the opportunity to consider the factors that should be taken into account to determine whether a person is a shadow director. In *Re Akron Roads Pty Ltd (in liq) (No 3)* (2016) 117 ACSR 513; [2016] VSC 657 (Akron Roads) Robson J provided an interesting decision which illustrates the significance of the shadow director cases that have been decided recently. It may be relevant in the eventual consideration of whether Palmer is a shadow director.

The facts of this case are straightforward. The liquidators of the company Akron Roads sought damages pursuant to s 588M(2) of the Act against a management consultancy firm Crewe Sharp Pty Ltd (Crewe Sharp) and the Chief Executive Officer of Akron Roads, Crewe. The allegations were that the debts incurred were incurred whilst insolvent.

Mr Crewe had been formally appointed as a director and CEO of Akron Roads as part of Crewe Sharp's management consultancy service. The liquidators alleged that Crewe Sharp was a shadow director for the purposes of the Act. Akron Roads claimed that its directors regularly followed the instructions of Crewe Sharp despite the fact that the company was insolvent. An insurance policy in favour of the relevant defendant, a professional indemnity policy, was relied on by the liquidator as the basis for seeking the remedies under the relevant provisions of the Act. The insurance company, however, disputed its liability to indemnify Crewe Sharp on the basis that the management company was not a director of Akron Roads.

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In his decision, Robson J relied on two cases, *Buzzle Operations Pty Ltd (in liq) v Apple Computer Australia Pty Ltd* (2010) 238 FLR 384 (*Buzzle*)[1] and an English case, *Re Hydrodam (Corby) Ltd* [1994] 2 BCLC 180 (*Hydrodam*) to assist his decision.

1 For a discussion of the judgment of the Court of Appeal in *Buzzle Operations Pty Ltd (in liq) v Apple Computer Australia Pty Ltd* (2011) 250 FLR 242; 277 ALR 189; 82 ACSR 703; [2011] NSWCA 109, see Professor Robert Baxt, *Corporations Legislation 2012* (Thomson Reuters, 2012), pp xxvii–xxix.

In his judgment (at [271]), Robson J noted the following:

> To establish that a defendant is a shadow director of a company it is necessary to prove:
>
> (1) who are the directors of the company, whether de facto or de jure;
>
> (2) that the defendant gave instructions or expressed wishes to those directors on how to act in relation to the company or that he was one of the persons who did so;
>
> (3) that those directors acted in accordance with such instructions or wishes; and
>
> (4) that they were accustomed so to act.

The relevant defendants challenged the conclusions that the judge was leading towards. Robson J noted that while Crewe Sharp was receiving a fee to enable Akron Roads to employ Crewe Sharp, there had been no legal authority to support this conclusion. The defendants argued that this connection was by way of inference only. However, Robson J outlined Crewe's duties which were managerial. He knew what his role as CEO consisted of and he did not require board approval for his actions. Robson J concluded that there was no evidence to suggest that the actions taken by Crewe were being taken at the direction of the company or that the board was accustomed to act pursuant to the directions or wishes of Crewe (see [315]). However, his Honour refused to rule that an adviser to the company should not necessarily be treated as a shadow director (merely because the directors follow his or her advice, particularly when the adviser has been retained to give advice (see [319])). He concluded that Crewe Sharp was not a shadow director of Akron Roads.

The decision is a useful one and shows that the courts may be willing in appropriate circumstances to extend the application of the shadow director principles so strongly supported in the *Buzzle* case referred to earlier and will play a significant part should an action be brought against Palmer in due course.

Another decision dealing with de facto directors, is that of Barrett J in *Re ACN 092 745 330* [2017] NSWSC 241. This case arose from the consideration of the evidence that persons who wish to claim that the relevant person in charge of the company was a de facto director was in fact acting with the relevant authority even though there was no formal recognition of his position in the company.

In considering the legal principles in assessing whether a Mr Battaglia was a de facto officer of the relevant company (by virtue of the broad definition of director in s 9 of the Act), Barrett J examined the circumstances under which Battaglia dealt with financial and related matters involving the company. In concluding that the liquidator had not established that the facts were sufficiently strong to determine that Battaglia was a de facto director, Barrett J relied in part on the Full Federal Court decision in *Grimaldi v Chameleon Mining NL (No 2)* (2012) 200 FCR 296; [2012] FCAFC 6. He noted that in order to establish a finding of de facto director a person had to be shown to have "assumed or performed functions which only a de jure [or de facto] director or board can properly perform or which are the sole responsibility of the director or the board" (see [110]). He referred to the facts in some detail to reach the conclusion that it was not possible for him to decide that the facts supported the finding of a de factor directorship. He also relied on the decision of Black J in the New South Wales Supreme Court in *Re Swan Services Pty Ltd* [2016] NSWSC 1724 to support his conclusions. The case turned significantly on the facts. (He also referred with approval to the decision in *Crowe-Maxwell v Frost* (2016) 91 NSWLR 414.)

THE STEPPING STONES THEORY IN EVALUATING DIRECTORS' DUTIES

One of the most interesting debates at the moment in relation to the question of whether the duties imposed on directors are too harsh or perhaps need to be made more far-reaching is the relevance of the so-called "stepping stones" theory in evaluating whether directors can be prosecuted by ASIC (or sued by others in civil litigation). The question here is whether the provisions of the Act, or some other law, can be used as a "stepping stone" by ASIC (or by civil parties in an appropriate case) in litigation against directors or others, including cases seeking the imposition of penalties or appropriate damages for breaches. Arguably the first high-profile case dealing with this issue is that of *Australian Securities and Investments Commission v Fortescue Metals Group Pty Ltd* (2011) 190 FCR 364; [2011] FCAFC 19. In that case Keane CJ in the Full Federal Court felt that it was appropriate for ASIC, in bringing proceedings against Andrew Forrest, the CEO of Fortescue Metals alleging a breach of the continuous disclosure rules in the Act and the director's duties of care and diligence, to rely on the fact that Forrest had overseen the failure of the company to comply with the continuous disclosure provisions. He was supported by the Full Court. The decision of the Full Federal Court was hotly debated and the High Court overturned the Full Federal Court's ruling of whether there had been a breach of the continuous disclosure regime meant that the rulings by Keane CJ were no longer relevant.[1]

1 For a discussion of the High Court of Australia decision in *Forrest v Australian Securities and Investments Commission* (2012) 247 CLR 486; 86 ALJR 1183; [2012] HCA 39), see Professor Robert Baxt, *Corporations Legislation 2013* (Thomson Reuters, 2013), pp xxix–xxx.

In the recent decision of Edelman J in *Australian Securities and Investments Commission v Cassimatis* (referred to under Duties of directors), his Honour dismissed the reliance on the "stepping stones" theory in evaluating the otherwise successful action brought by ASIC against the directors of the Storm organisation. This has led to further considerable debate. The Federal Government has requested the Commonwealth Treasury to review ASIC's consideration of this matter. In its enforcement review taskforce paper (*ASIC Enforcement Review: Position and Consultation Paper 6 – ASIC's power to ban senior officials in the financial sector*) the particular question of extent to which the "stepping stones" theory can be applied has once again been raised. It will be interesting to see where this debate ends.

BANK BILL SWAP RATES ACTION

The so-called Bank Bill Swap Reference Rate case (*Australian Securities and Investments Commission v National Australia Bank Ltd* [2017] FCA 1338, referred to earlier, which had been vigorously conducted by ASIC against three of the major trading banks in Australia, namely the National Australia Bank Ltd (NAB), the Australian and New Zealand Banking Group Ltd (ANZ), and the Westpac Banking Corporation Ltd (Westpac), has resulted in considerable media discussion, political comment and legal arguments as to the importance of these cases. Apart from the case against Westpac, which is now the subject of a hearing by Beach J, a "settlement" has been reached between ASIC and NAB and ANZ.

The litigation was based on an allegation by ASIC that there had been breaches by the relevant banks of specific provisions of the *Australian Securities and Investments Commission Act 2001* (Cth) (the ASIC Act), namely ss 12(3)(b) and 12(3)(c) which deal with the allegation that the banks were engaged in conduct that, in general terms, might be described as unconscionable. After many days of debate between the parties in the relevant cases, and much agitation as to whether the cases would go to full trial (which meant that the retiring Chairman of ASIC, Greg Medcraft, would not obtain a verdict in these important initiatives on ASIC's part during his term as Chairman), the pressure was on the parties to reach a settlement. Within days of Mr Medcraft's retirement, the parties in the cases involving the NAB and ANZ agreed to take to the court settlements which in essence led to a ruling that the banks had engaged in conduct which was unconscionable, in breach of the relevant provisions of the ASIC Act referred to earlier. Agreement was reached that the banks would pay penalties of $10 million each. Relevant orders were made by Jagot J in approving the settlement arrangements, on 10 November 2017, awarding costs in favour of ASIC against the two banks.

What is of particular interest for me, and of significant interest to commentators and others who are fascinated by the nature of the litigation that has been brought, the allegations made against the banks in this and related activities, were Jagot J's very powerful obiter dicta in comments describing the behaviour of the two banks.

At paragraph 112 of her judgment, she noted that:

> 112. Each of NAB and ANZ has admitted to unethical and dishonest conduct, It is difficult to convey the seriousness of what the offences involved. Knowing the function of the [relevant banks' swap rates] in the Australian financial system and that it was relied upon as an independently established benchmark throughout the system, employees of NAB and ANZ deliberately sought to manipulate the benchmark to advantage their employer (and their own performance) over counterparties who have no means of protecting themselves from the effects of such manipulation, and had a right to expect that NAB and ANZ would deal with them fairly, honestly and in good faith.
>
> 113. From the perspective of the counterparties, the conduct involved great departures from basic standards of commercial decency, honesty and fairness.
>
> 114. From the broader perspective of the Australian financial system, a system which depends on public and institutional trust in its integrity, the conduct is even worse.

Perhaps what is even more fundamental, in the approach of Jagot J to the description of the activities that enabled her to agree with the penalties of $10 million against each of the two banks being awarded, were these comments about the explicit culture that the community, the politicians and no doubt the regulators, would expect of organisations such as the banks. She noted at paragraph [115] of the judgment that any employee who was performing functions in the banking organisations, which would amount to the commission of manipulating practices over a period of time displayed:

> fundamental failings in the culture, training, governance and regulatory systems of both NAB and ANZ. The public should be shocked, dismayed and indeed disgusted that conduct of this kind could have occurred. The conduct involved attempts to corrupt a fundamental component of the entire Australian financial system for a mere short-term commercial advantage. The conduct involved a repeated failure to fulfil what would generally be perceived as the most basic standards of honesty, fairness and commercial decency, let alone the standards that would properly be expected of these two banks. The conduct tends to undermine public confidence in the entirety of the Australian financial system.

It will be interesting to see how the third case is finally dealt with by Beach J. It would not surprise if the case is settled, although it may well be that we will see a different result in this litigation to the agreed penalties that have been discussed and settled between the parties in the litigation involving NAB and ANZ.

REMEDIES BASED ON OPPRESSION AND OTHER RIGHTS OF SHAREHOLDERS

In previous editions of this Annual Review, I have emphasised that the courts have become more generous in assessing the value to shareholders (members) of remedies provided in the Act where there is alleged

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aggressive or unfair conduct, amongst other complaints, taken by more powerful shareholders, or by directors in appropriate cases. Perhaps the most interesting development in this context has been the increased reliance on the oppression remedy (contained in s 232 and relevant provisions of the Act) by the courts in recent years. This remedy, which was introduced into the legislation some years ago, enables the shareholders (members) to bring proceedings against other members of the company (not against the directors as directors but as members) where there is oppressive, and unfair prejudicial and related conduct that is established by the complainant in the appropriate cases.

While courts had been somewhat hesitant in granting remedies to members on the basis that they do not want to make judgment on how directors are running their company, particularly in instances involving restructuring, we are now seeing increased success in claims for oppression and derivative actions. In a time where directors' duties and resulting penalties continue to be on the agenda for governments and regulators, recent decisions have continued to surprise practitioners and others in the willingness of the courts to provide remedies of a more conclusive context leading to questions of whether the company vehicle should be allowed to continue to operate.

The recent decision of Sifris J in the Victorian Supreme Court, in *Exton v Exton* (2017) 118 ACSR 411; [2017] VSC 14 (*Exton*) is an interesting example of the oppression remedy being available to shareholders in a closely held company, where there is a genuine opportunity for the courts to evaluate the behaviour on the part of the more powerful shareholder (who is usually a director), against shareholders who perhaps have a minority shareholding and who do not exercise the relevant power to conduct the affairs of the company.

The facts in this case involved an action by Exton, who was a director and member of the company, as well as being the brother of the defendant, and who had petitioned the court to order the defendant to sell their shares in the company on the basis of their alleged oppressive conduct, or alternatively, to order the winding up of the company.

The court held that three unauthorised transactions which were conducted within the company by the majority shareholders which affected the position of the plaintiff. Unusually, in this case, one of the central questions for the court to consider was whether the oppression remedy continued to be available if the conduct had ceased at the time the proceedings were considered by the court. Generally speaking the oppression remedy is intended to bring to an end to oppressive conduct by majority members. This would effectively end the alleged oppressive conduct.

Sifris J, in considering this matter, relied on other decisions in noting (at [34]) that the remedy would be "enlivened if the conduct occurs at any time and notwithstanding that it may have ceased at the time of trial". He referred with approval to the judgment of Giles J in the first instance hearing in the case of *Campbell v Backoffice Investments Pty Ltd* (2008) 88 ACSR 359. It should be noted that the High Court eventually approved the decision reached by Giles J (although on a variety of grounds). In his judgment Giles J noted (at [132]) that "claimed relief founded on conduct which is no longer continuing may be refused, but will not always be refused".

It was also noted by Sifris J that the defendant's attempt to rectify the situation by replacing the funds that the defendant had expended did not in any way remove the ability of the plaintiff to make the claim that the relevant action was oppressive.

The decision turned on whether the remedy should be provided by the Court where the conduct was no longer operating to the detriment of the plaintiff. Sifris J noted that cessation of the oppressive conduct had to be considered on the basis of whether it was of "relevance in determining whether and to what extent orders should be made. There may be no need or utility for any remedy. Any remedy will depend on the particular circumstances of the case" (at [34]).

This provides members with the opportunity to hold majority members accountable for any conduct that may be oppressive, regardless of whether it is ongoing. Members should be put on notice that merely rectifying conduct subsequent to the breach will not save them or the company from the array of remedies that courts may order against them.

The decision also confirmed a reluctance on the part of the courts to wind up companies. The Court refused to entertain the plaintiff's claim that it was "just and equitable" to do so pursuant to s 461(1)(k) of the Act and declined to make orders to wind up Exton. Sifris J reaffirmed the courts' position that winding up a company should be ordered as a last resort and only if "some other remedy" was unavailable. His Honour expanded on this and concluded that the broad application of s 467(4) of the Act meant that courts were not limited to considering purely legal remedies, and subsequently ordered the defendant sell their shares to the plaintiff at a price determined by the Court.

The question of whether the courts will wind up a company, even though it is a last resort remedy, was also considered at some length, by Bond J of the Supreme Court of Queensland in *Allways Resources Holdings Pty Ltd v Samgris Resources Pty Ltd* (2017) 121 ACSR 1; [2017] QSC 74. There were a number of interesting features of this decision (a very lengthy one of well over 100 pages). Bond J noted that the winding up order that was being sought could be used in situations where companies were members of the body the subject of the alleged oppressive conduct. He also noted that where the working relationship between the minority shareholders and the majority investor in the relevant company had broken down, in such a way that the main company was no longer able to operate effectively in the manner intended, the courts may have no option but to order a winding up in appropriate circumstances. That was the position that Bond J found himself in and the winding up order was made.

He observed that, where the complaining shareholders were being disadvantaged in such a way that they could no longer obtain the benefits of working together with the other shareholders in running the relevant company, the court would be more willing to order a winding up order or some similar remedy. The evidence canvassed in his lengthy judgment was in his view powerful. It supported the remedy ordering that the company be wound up because the "quasi partnership" that was at the centre of the relevant dispute had been undermined so that it was no longer achieving the purposes of its establishment.

Amongst other cases relying on the oppression remedy during the year, but one where the remedy failed, was the decision of Jagot J in *RBC Investor Services Australia Nominees Pty Ltd v Brickworks Ltd* [2017] FCA 756. In this case the petitioner failed in its claim under the oppression remedy. Instead the Court ruled in favour of what turned out to be parallel or joint behaviour by the two majority shareholders in the relevant company at a time when a restructuring of the company was being considered. Jagot J agreed that a strong case had been made by the complainants that their rights had been affected in a way that made it difficult for their interests to be properly evaluated and considered by the company. She also agreed that the minority shareholders' interests may have been harmed by the fact that the decisions of the two majority shareholders in the relevant company were pursuing interests that did not favour the interests of the minority shareholder. But in her view what the majority shareholders were supporting in the relevant restructure was defensible.

Her language in dismissing the claims and upholding the decisions of the board of directors in relation to the relevant rearrangement that was being considered will no doubt be influential in similar cases where there are very significantly large parcels of shares being held, but where strong board decisions need to be taken. At paragraph [42] of the judgment she noted that the issues had to be considered by noting that:

> [T]he role of the court is not to step into the shoes of the directors and unilaterally decide what it thinks to be in the best interests of the company as a whole. The courts recognise that it is the responsibility of the directors to weigh the competing considerations with which they will be routinely confronted and determine what is in the best interests of the company.

The decision has been criticised by some in the business sector but, in the context of the particular company, the decision has generally been applauded. The decision also confirmed the unwillingness of courts to interfere with the decisions taken by directors in their management of companies, especially companies whose shareholders are major corporations themselves and the unwillingness of the court to second guess the decisions of directors absent any allegation of breaches of duty.

CONCLUSIONS

There is little doubt that the last 12 to18 months have been a very dramatic time in the corporate law "scene". This is not because of the high profile cases considering the failure of directors and others associated with huge corporate losses, as perhaps been a pattern over the last two to three years in my view. Rather the concerted attention being given to the need to ensure that the culture of behaviour in banking, financial and other larger organisations has been an unreasonable focus of attention.

The retiring Chairman of ASIC, Greg Medcraft, was no doubt pleased to oversee the decision by the NAB and the ANZ in the litigation that is still continuing against Westpac. The quite extraordinary language of Jagot J in describing the failure of the two banks to display an appropriate approach to compliance with the law in relation to the allegations pursued by ASIC (discussed briefly above) may be seen as a further ″call to action" on top of the rather draconian BEAR regulatory proposals which are now the subject of legislation to be considered by the Australian Parliament in the new year.

In my view it was unnecessary for the BEAR legislation to be framed in the way that it is. Our current laws already contain clear directions in my view on how the relevant organisations and their senior officers should behave. Had ASIC (and perhaps other relevant regulators) been more willing to litigate rather than continue to claim the law was not tough enough to deal with allegations of breaches of the law, we may have seen some clear signals on the appropriate culture to be displayed. Whether our courts will be willing to rule that breaches of the law have occurred if allegations about culture alone are pleaded will be an interesting challenge to see unfold.

I hope ASIC and our other major regulators will be willing to take appropriate cases to our courts to test the very wide range of relevant laws that are already in our statute books but in the meantime the report of the Royal Commission into banks and financial services announced on 30 November 2017, with a report due in February 2019, will most probably provide a further range of legislative and related changes.

In the meantime I hope James Shipton will have a successful term as the new Chairman of ASIC.