HIGH COURT OF AUSTRALIA

FRENCH CJ,
CRENNAN, KIEFEL, BELL AND GAGELER JJ

MACARTHURCOOK FUND MANAGEMENT LIMITED & ANOR — APPELLANTS

AND

TFML LIMITED — RESPONDENT

MacarthurCook Fund Management Limited v TFML Limited
[2014] HCA 17
14 May 2014
S39/2014

ORDER

1. *Appeal allowed.*

2. *Set aside paragraphs 1 to 4 of the order of the Court of Appeal of the Supreme Court of New South Wales made on 3 September 2013 and, in their place, order that:*

   (a) *paragraphs 2 and 3 of the order of the Supreme Court of New South Wales made on 17 August 2012 be set aside and, in lieu thereof, order judgment for MacarthurCook Fund Management Limited and Sandhurst Trustees Limited against TFML Limited in the sum of $10,809,868 plus pre-judgment interest; and*

   (b) *the appeal be otherwise dismissed.*

3. *Respondent to pay the appellants' costs in this Court and at first instance and on appeal to the Court of Appeal.*

4. *Parties have leave to file written submissions seeking a variation of these orders on or before 4.00 pm on the day 14 days after the publication of these orders.*

On appeal from the Supreme Court of New South Wales

Representation

N C Hutley SC with V A Thomas for the appellants (instructed by Ashurst Australia)

B W Walker SC with M A Izzo for the respondent (instructed by Piper Alderman Lawyers)

CATCHWORDS

MacarthurCook Fund Management Limited v TFML Limited

Corporations – Managed investment schemes – Unlisted unit trust – Members' rights to withdraw from scheme – Where terms of issue of units in trust provided for redemption within stipulated time period – Where units not redeemed within stipulated time period – Whether obligation to redeem units subject to requirements of Pt 5C.6 of *Corporations Act* 2001 (Cth) – Whether redemption of units constitutes withdrawal from scheme within meaning of Pt 5C.6 of *Corporations Act* 2001 (Cth).

Words and phrases – "managed investment schemes", "redemption", "withdrawal".

Corporations Act 2001 (Cth), Pt 5C.6, ss 601GA(4), 601KA.

1 FRENCH CJ, CRENNAN, KIEFEL, BELL AND GAGELER JJ. The issue in this appeal is whether redemption of certain interests in a managed investment scheme constituted withdrawal from that scheme within the meaning of Pt 5C.6 of the *Corporations Act* 2001 (Cth) ("the Act").

The Act

2 Chapter 5C of the Act sets out a regime for the regulation of managed investment schemes. A managed investment scheme can be described, sufficiently for present purposes, as a scheme under which financial contributors ("members") have acquired rights to financial or proprietary benefits ("interests") produced by pooling their contributions but do not have day-to-day control over the operation of the scheme[1].

3 Part 5C.1 requires registration of a managed investment scheme in specified circumstances. One is if the scheme has more than 20 members[2]. Another is if the scheme was promoted by a person in the business of promoting managed investment schemes[3]. To be registered, a managed investment scheme must have a responsible entity and a constitution, as well as a compliance plan[4], which sets out measures the responsible entity is to apply in operating the scheme to ensure compliance with the Act and the constitution[5].

4 Part 5C.2 requires the responsible entity of a registered scheme to be a public company, holding an Australian financial services licence authorising it to operate a managed investment scheme[6], and requires the responsible entity to operate the scheme and perform the functions conferred on it by the constitution and the Act[7]. The responsible entity holds, on trust for members, scheme

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1 Section 9, "managed investment scheme".

2 Section 601ED(1)(a).

3 Section 601ED(1)(b).

4 Sections 601EA(4) and 601EB(1).

5 Section 601HA(1).

6 Section 601FA.

7 Section 601FB(1).

property[8], which includes contributions by members and borrowings by the responsible entity together with property acquired, and income and property derived, from those contributions or borrowings[9]. In exercising its powers and carrying out its duties, the responsible entity is required, amongst other things, to: exercise a reasonable degree of care and diligence[10]; act in the best interests of members[11]; treat members who hold interests of the same class equally and members who hold interests of different classes fairly[12]; ensure that all payments out of the scheme property are made in accordance with the scheme's constitution and the Act[13]; and carry out or comply with any other duty, not inconsistent with the Act, that is conferred on the responsible entity by the constitution[14].

5 Part 5C.3 requires the constitution of a registered scheme to be contained in a document that is legally binding between members and the responsible entity[15]. The constitution is required to make adequate provision for the powers of a responsible entity in relation to dealing with scheme property[16]. Within Pt 5C.3, s 601GA(4) provides:

> "If members are to have a right to withdraw from the scheme, the scheme's constitution must:
>
> (a) specify the right; and

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8 Section 601FC(2).

9 Section 9, "scheme property".

10 Section 601FC(1)(b).

11 Section 601FC(1)(c).

12 Section 601FC(1)(d).

13 Section 601FC(1)(k).

14 Section 601FC(1)(m).

15 Section 601GB.

16 Section 601GA(1)(b).

(b) if the right may be exercised while the scheme is liquid (as defined in section 601KA) – set out adequate procedures for making and dealing with withdrawal requests; and

(c) if the right may be exercised while the scheme is not liquid (as defined in section 601KA) – provide for the right to be exercised in accordance with Part 5C.6 and set out any other adequate procedures (consistent with that Part) that are to apply to making and dealing with withdrawal requests.

The right to withdraw, and any provisions in the constitution setting out procedures for making and dealing with withdrawal requests, must be fair to all members."

6 Part 5C.6 is headed "Members' rights to withdraw from a scheme". Within Pt 5C.6, s 601KA provides in relevant part:

"(1) The constitution of a registered scheme may make provision for members to withdraw from the scheme, wholly or partly, at any time while the scheme is liquid (see subsection 601GA(4)).

(2) The constitution of a registered scheme may make provision for members to withdraw from the scheme, wholly or partly, in accordance with this Part while the scheme is not liquid (see subsection 601GA(4)).

(3) The responsible entity must not allow a member to withdraw from the scheme:

(a) if the scheme is liquid – otherwise than in accordance with the scheme's constitution; or

(b) if the scheme is not liquid – otherwise than in accordance with the scheme's constitution and sections 601KB to 601KE.

…

(4) A registered scheme is liquid if liquid assets account for at least 80% of the value of scheme property."

Sections 601KB to 601KE, to which s 601KA(3)(b) refers, set out a procedure by which the responsible entity of a scheme that is not liquid can make an offer to

all members of an opportunity to make withdrawal requests (specifying in the offer the period during which the offer will remain open and the assets that will be used to satisfy withdrawal requests) and by which the responsible entity can then satisfy withdrawal requests members make in response to the offer (proportionately if the money available from the assets is insufficient to satisfy all requests). Contravention of s 601KA(3) is an offence[17].

Facts

7 RFML Ltd ("RFML") was from 2006 until after 2008 the trustee of an unlisted unit trust ("the Trust"). The Trust was a registered scheme. RFML was then the responsible entity of the scheme. TFML Ltd ("TFML") subsequently replaced RFML as the responsible entity and thereby assumed the rights, obligations and liabilities of RFML[18]. RFML was subsequently renamed Zhaofeng Funds Ltd ("Zhaofeng").

8 The constitution of the Trust was contained in a deed which provided that the beneficial interest in the Trust was divided into units, and which was expressed to be binding on unitholders and the trustee. Subject to the terms of issue, each unit conferred on its holder an equal and undivided interest in the assets of the Trust as a whole. The trustee was given power to issue units in different classes subject to rights, obligations and restrictions determined by the trustee.

9 The constitution provided that a unitholder had no right to withdraw from the Trust other than in accordance with specified procedures for making and dealing with withdrawal requests. Those withdrawal procedures applied differently when the Trust was liquid from when it was not. They complemented s 601KA(3)(b) of the Act in providing that a unitholder had no right to withdraw when the Trust was not liquid unless there was a withdrawal offer currently open for acceptance by unitholders. The trustee was given power, whether or not the Trust was liquid, to suspend withdrawals for a period of time if it was not in the best interests of unitholders for withdrawals to be made.

10 The constitution provided that units of a class named "Founder Units", created and issued by the trustee, "may be redeemed at a Withdrawal Price of $1.00 each". The constitution separately provided for the trustee to have

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17 Sections 601KA(3A) and 1311.

18 Section 601FS(1).

power to "redeem" the units of any unitholder who failed to pay a debt due to the trustee or who, having acquired more than 15% of the units on issue, failed to comply with a notice to divest.

11 In October 2006 and December 2007, RFML sought to raise funds by an open-ended public offer of ordinary units in the Trust at an issue price of $1.00 each. MacarthurCook Fund Management Ltd ("MacarthurCook") agreed with RFML to underwrite the public offer by subscribing for 10 million fully paid Founder Units at an issue price of $1.00 each. The terms of the underwriting were provided in two Facility Agreements, Facility Agreement Tranche 1 ("FAT 1") and Facility Agreement Tranche 2 ("FAT 2"), each dated 27 October 2006. FAT 1 and FAT 2 each provided for MacarthurCook to subscribe for a tranche of five million Founder Units by 1 November 2006 to be redeemed by RFML out of moneys raised in the public offering. If the Founder Units were not redeemed by 31 October 2007, RFML in its personal capacity was obliged to purchase them from MacarthurCook. In accordance with FAT 1 and FAT 2, RFML issued 10 million Founder Units to MacarthurCook. On 1 April 2007, RFML and MacarthurCook entered into a Unit Conversion Agreement by which the first tranche of five million Founder Units, issued in accordance with FAT 1, were converted to ordinary units in the Trust.

12 RFML and MacarthurCook subsequently entered into three further Facility Agreements. The first of them, Facility Agreement Tranche 3 ("FAT 3"), entered into on 1 November 2007, provided for the termination of FAT 2 on 31 October 2007, for RFML to retain the $5 million subscription price for the second tranche of five million Founder Units, issued in accordance with FAT 2, and for RFML in consideration to issue to MacarthurCook five million fully paid "Subscription Units" at an issue price of $1.00 each. The other two, Facility Agreement Tranche 4 ("FAT 4") and Facility Agreement Tranche 5 ("FAT 5"), entered into on 3 December 2007, each provided for MacarthurCook to pay $5 million for a further tranche of five million Subscription Units at an issue price of $1.00 each.

13 In accordance with FAT 3, FAT 4 and FAT 5, RFML issued a total of 15 million Subscription Units to MacarthurCook. The Subscription Units were held by Sandhurst Trustees Ltd ("Sandhurst") as custodian and agent for MacarthurCook. The Subscription Units were constituted as a separate class of units of which MacarthurCook was the only holder. The terms of issue of the Subscription Units were set out in each Facility Agreement.

14 One of the terms of issue of the Subscription Units, set out in a provision of each of FAT 3, FAT 4 and FAT 5, was to the following effect:

> "Subject to compliance with any requirements under the Corporations Act and the Constitution, during the Subscription Period, Subscription Units held by MacarthurCook must be redeemed by [RFML] for their Issue Price, using funds received by the Trust as a result of accepted applications under the [public offer], such redemptions commencing six months from the Subscription Date."

Each Facility Agreement defined "the Subscription Period" to be a period of 12 months from "the Subscription Date", which was 1 November 2007 for FAT 3 and 3 December 2007 for FAT 4 and FAT 5.

15 By 29 September 2008, the Trust had received funds totalling $12,347,079 as a result of accepted applications under the public offer, but RFML had not redeemed any of the Subscription Units. RFML on that date gave notice that it had suspended all "withdrawals" from the Trust until further notice. The suspension remained in place until after the expiration of the Subscription Period for each of FAT 4 and FAT 5 on 3 December 2008.

16 At 29 September 2008 and throughout the period of suspension, the scheme was not liquid within the meaning of that term as defined in s 601KA(4) of the Act.

Proceedings

17 MacarthurCook and Sandhurst brought proceedings in the Supreme Court of New South Wales against TFML and Zhaofeng. They claimed, amongst other things, damages from TFML for breach of contract by RFML arising from RFML's failure to redeem Subscription Units in accordance with the relevant term of their issue.

18 The primary judge, Hammerschlag J, held that s 601KA(3)(b) of the Act applied to prevent RFML from redeeming the Subscription Units other than in accordance with the constitution of the Trust and ss 601KB to 601KE[19]. The primary judge found that RFML had sufficiently complied with the requirements of the constitution and of ss 601KB to 601KE by entering into FAT 3, FAT 4 and FAT 5 or that (if it had not) RFML was in breach of an express or implied obligation to do what was necessary within its power to comply with those

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19 *MacarthurCook Fund Management Ltd v Zhaofeng Funds Ltd* (2012) 30 ACLC ¶12-042 at 585-586 [66]-[71].

requirements[20]. The primary judge determined that MacarthurCook was entitled to damages against TFML on this claim in the amount of $10,809,868. That amount was calculated by taking the $12,347,079 which RFML had received as a result of accepted applications, and which MacarthurCook and Sandhurst in turn would have received from RFML for redemption of 12,347,079 Subscription Units, and then subtracting $1,537,211, which was found to be the value of those 12,347,079 Subscription Units then still held by MacarthurCook[21].

19 The Court of Appeal concluded that the primary judge was correct to hold that s 601KA(3)(b) applied[22]. Meagher JA, with whom McColl and Macfarlan JJA agreed, said that, within Pt 5C.6, "'withdrawing' describes exiting the collective investment scheme during its continued operation by receiving a payment of money out of the scheme funds in exchange for the extinguishment of the interest held in the scheme"[23]. The Court of Appeal concluded, however, that the primary judge was wrong to find that RFML had complied with the requirements of the constitution and of ss 601KB to 601KE by entering into FAT 3, FAT 4 and FAT 5[24]. Given that the relevant term of issue of the Subscription Units expressed RFML's obligation to redeem to be subject to compliance with any requirements of the Act, the consequence of the Court of Appeal concluding that s 601KA(3)(b) applied, but had not been complied with, was that RFML did not breach that term in failing to redeem[25]. The Court of

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20 *MacarthurCook Fund Management Ltd v Zhaofeng Funds Ltd* (2012) 30 ACLC ¶12-042 at 586-589 [78]-[100].

21 *MacarthurCook Fund Management Ltd v Zhaofeng Funds Ltd* (2012) 30 ACLC ¶12-042 at 584 [52]-[53], 589 [106].

22 *TFML Ltd v MacarthurCook Fund Management Ltd* (2013) 31 ACLC ¶13-046 at 576-579 [24]-[38].

23 *TFML Ltd v MacarthurCook Fund Management Ltd* (2013) 31 ACLC ¶13-046 at 577 [28].

24 *TFML Ltd v MacarthurCook Fund Management Ltd* (2013) 31 ACLC ¶13-046 at 579-580 [39]-[45].

25 *TFML Ltd v MacarthurCook Fund Management Ltd* (2013) 31 ACLC ¶13-046 at 580-581 [46]-[47].

Appeal went on to conclude that, contrary to the further finding of the primary judge, RFML was not in breach of any further relevant obligation[26].

Appeal

20 MacarthurCook and Sandhurst argue in their appeal to this Court that the Court of Appeal erred in concluding that RFML did not breach its obligation to redeem. That is because, they argue, the Court of Appeal erred in holding that s 601KA(3)(b) applied to redemption of the Subscription Units. They argue that redemption of the Subscription Units by RFML was not withdrawal by MacarthurCook from the Trust within the meaning of Pt 5C.6.

21 TFML supports the reasoning of the Court of Appeal. TFML also seeks to argue that RFML was not in breach of its obligation to redeem the Subscription Units, even if s 601KA(3)(b) did not apply. That is because, TFML argues, to have redeemed the Subscription Units in the circumstances which existed after 29 September 2008 would have breached RFML's duty to act in the best interests of unitholders. That alternative argument was not put to the Supreme Court. Indeed, the primary judge specifically recorded that it was "not suggested that redemption was not, or that the responsible entity had come to the view that redemption was not, in the interests of members"[27]. As it relies on a contestable, and contested, view of the facts, the alternative argument cannot now be raised in this Court.

Resolution

22 Part 5C.6, in combination with s 601GA(4), has a number of features which bear on the meaning of "withdraw" in Pt 5C.6 of the Act. The first is that a member can have no "right to withdraw", other than a right that is specified in the constitution[28]. The second is that, where a right to withdraw is specified in the constitution, the constitution must also specify "adequate procedures" by which that right "may be exercised"[29]. The third is that adequate procedures will

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26 *TFML Ltd v MacarthurCook Fund Management Ltd* (2013) 31 ACLC ¶13-046 at 581-583 [49]-[62].

27 *MacarthurCook Fund Management Ltd v Zhaofeng Funds Ltd* (2012) 30 ACLC ¶12-042 at 588 [98].

28 Section 601GA(4)(a).

29 Section 601GA(4)(b) and (c). See also s 601KA(1) and (2).

always involve the member making a "withdrawal request"[30]. The fourth is that, if the scheme is not liquid, the responsible entity cannot "allow" a member to withdraw, other than in accordance with additional statutory procedures designed to ensure that all members with rights to withdraw have the same practical opportunity to make withdrawal requests and to have those withdrawal requests satisfied[31].

23 Those features indicate that a right to withdraw within the ambit of Pt 5C.6 is not limited to a right of a nature which would require the existence of a correlative obligation. They also indicate that the withdrawal by a member that is regulated by Pt 5C.6 of the Act involves some act of volition on the part of the member.

24 Those indications are reinforced by the legislative purpose of Pt 5C.6, as revealed by its legislative history. Chapter 5C was introduced into the Act in 1998[32], following extensive consideration by the Australian Government of a joint report of the Australian Law Reform Commission and the Companies and Securities Advisory Committee published in 1993 on the non-superannuation segment of the managed investments industry ("the Review")[33]. The background to the Review was the loss of investor confidence after the collapse and closure of many property trusts in the late 1980s following a severe decline in commercial property values[34]. The evident purpose of Pt 5C.6 was to address problems identified in Ch 7 of the Review, entitled "Withdrawing from a collective investment scheme". The chapter was concerned with "how investors leave collective investment schemes" and "whether modifications to exit mechanisms" then permitted by the applicable corporations legislation were

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30 Section 601GA(4)(b) and (c).

31 Section 601KA(3)(b) and ss 601KB to 601KE.

32 *Managed Investments Act* 1998 (Cth).

33 Australian Law Reform Commission and The Companies and Securities Advisory Committee, *Collective Investments: Other People's Money*, Report No 65, (1993). See Australia, House of Representatives, *Parliamentary Debates* (Hansard), 3 December 1997 at 11928.

34 *Westfield Management Ltd v AMP Capital Property Nominees Ltd* (2012) 247 CLR 129 at 136 [11]; [2012] HCA 54.

"necessary to improve the efficiency and enhance the stability of collective investment schemes"[35].

25 Chapter 7 of the Review identified two ways in which an investor might have then been permitted to "withdraw his or her investment from a collective investment scheme", other than by selling his or her interests or by terminating the scheme and liquidating its assets. One was "redemption", which involved the investor "redeeming his or her interests from the scheme" and being "paid out of scheme funds, if necessary by liquidating some of the scheme assets". The other was "buy back", which involved the investor requiring the manager of the scheme to buy the investor's interests by paying the investor from its own funds, but which often resulted in practice in the manager itself going on to redeem those interests from the scheme[36].

26 Chapter 7 of the Review recorded that, while "[i]nvestor confidence in collective investment schemes is likely to fall, and individual investors may suffer, if investors are unable to withdraw their funds in accordance with their expectations … inappropriate or unworkable exit rules may create false or unrealistic expectations in investors as to their ability to liquidate their investments"[37]. The Review continued[38]:

> "The departure of investors from a collective investment scheme invested only in liquid assets rarely causes commercial instability. The scheme is able to pay out investors either directly (redemptions) or indirectly (buy backs by the scheme manager with a subsequent redemption of acquired interests) because its assets are liquid. The departure of investors from wholly or partly illiquid collective investment schemes, on the other hand, can lead to instability. This is because the scheme operator and the scheme itself may not have enough liquid funds readily available to pay out these persons. If more investors are entitled to leave the scheme than can be paid out from available liquid assets, the operator will need to sell assets of the scheme quickly. This can cause disruption in financial markets."

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35 Review at 61 [7.1].

36 Review at 61 [7.2].

37 Review at 62 [7.3].

38 Review at 62 [7.4].

27 The Review expressed the view that managers of illiquid investment schemes "simply cannot act as banker to the scheme's investors"[39]. The Review recommended legislated procedures, designed to ensure investors are treated equally, to govern the manner in which the manager of an illiquid scheme should be permitted either to buy back existing interests from investors[40] or to "make redemption offers"[41].

28 Part 5C.6 operates in combination with s 601GA(4) to address problems of the nature identified in Ch 7 of the Review: problems associated with investors exercising choice to exit a scheme, particularly when the scheme is not liquid; not problems associated with investors exiting a scheme otherwise than through the exercise of choice, even when the scheme is not liquid; much less problems associated with the performance of duties and exercise of powers by responsible entities.

29 The meaning which best fits the structure and purpose of Pt 5C.6 operating in combination with s 601GA(4) of the Act is that a member withdraws from a registered scheme if the member acts so as to result in the responsible entity returning the whole or some part of the member's contribution. A member does not withdraw from a scheme merely by reason of the responsible entity exercising a power compulsorily to redeem the interest of a member (examples of which were those powers conferred by the constitution of the Trust to redeem the units of any unitholder who failed to pay a debt due to the trustee or who, having acquired more than 15% of the units on issue, failed to comply with a notice to divest). Similarly, a member does not withdraw from a scheme merely by reason of the responsible entity performing an obligation to redeem which arises under the terms of issue of a class of interests if that obligation is required by those terms to be performed independently of any act on the part of the member. The reason in each of those cases is the same: it is because the redemption occurs without volition on the part of the member.

30 TFML argues that there is no difference between an agreement which provides for redemption at a stipulated time (or during a stipulated period), and an agreement which empowers a member to call for redemption at the time of the

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39 Review at 63 [7.5].

40 Review at 65-66 [7.12].

41 Review at 69-70 [7.21].

member's choosing. Each is the product of volition on the part of a member, and each carries risks if redemption is required when a scheme is not liquid.

31 There is a real difference between the creation of a separate contractual obligation for a responsible entity to redeem an interest, and the creation of an obligation for the responsible entity to redeem as part of the terms of issue of that interest. TFML's argument postulates the former. The latter is what occurred in the present case, the terms of issue of the Subscription Units being set out in each Facility Agreement. The volition necessary for there to be withdrawal by a member is not to be found merely in the choice to become a member by subscribing for units on the terms on which they are issued. That is so even if those terms were the subject of prior agreement between the responsible entity and the putative member. Nor is the volition relevant to withdrawal by a member to be found merely in the choice of the member either to sue or not to sue to enforce the terms of issue.

32 As already explained, the responsible entity of a scheme must always exercise a reasonable degree of care and diligence, must always act in the best interests of members, must always treat members who hold interests of the same class equally and members who hold interests of different classes fairly, and must ensure that all payments out of the scheme property are made in accordance with the scheme's constitution and the Act. The responsible entity is not placed by Pt 5C.6 under any further obligation in the performance by the responsible entity of an obligation to redeem arising under the terms of issue of a class of interests.

33 For these reasons, the argument of MacarthurCook and Sandhurst is to be accepted: redemption of the Subscription Units by RFML in the performance of the obligation imposed on it by the relevant term of the issue of the Subscription Units did not constitute withdrawal by MacarthurCook from the Trust within the meaning of Pt 5C.6, with the consequence that s 601KA(3)(b) had no application. The appeal is therefore to be allowed.

Orders

34 The parties were agreed as to the form of orders in the event the appeal was allowed. The agreed form of orders, however, included orders which would vary orders made by the Court of Appeal against Zhaofeng. As Zhaofeng is not a party to the appeal, those orders cannot be made. In the circumstances, the appropriate orders are:

1. Appeal allowed.

2. Set aside paragraphs 1 to 4 of the order of the Court of Appeal of the Supreme Court of New South Wales made on 3 September 2013 and, in their place, order that:

   (a) paragraphs 2 and 3 of the order of the Supreme Court of New South Wales made on 17 August 2012 be set aside and, in lieu thereof, order judgment for MacarthurCook Fund Management Limited and Sandhurst Trustees Limited against TFML Limited in the sum of $10,809,868 plus pre-judgment interest; and

   (b) the appeal be otherwise dismissed.

3. Respondent to pay the appellants' costs in this Court and at first instance and on appeal to the Court of Appeal.

4. Parties have leave to file written submissions seeking a variation of these orders on or before 4.00 pm on the day 14 days after the publication of these orders.