HIGH COURT OF AUSTRALIA

KIEFEL CJ,
BELL, GAGELER, KEANE AND EDELMAN JJ

Matter No M79/2018

AUSTRALIAN SECURITIES & INVESTMENTS COMMISSION — APPELLANT

AND

WILLIAM LIONEL LEWSKI & ANOR — RESPONDENTS

Matter No M80/2018

AUSTRALIAN SECURITIES & INVESTMENTS COMMISSION — APPELLANT

AND

MICHAEL RICHARD LEWIS WOOLDRIDGE & ANOR — RESPONDENTS

Matter No M81/2018

AUSTRALIAN SECURITIES & INVESTMENTS COMMISSION — APPELLANT

AND

MARK FREDERICK BUTLER & ANOR — RESPONDENTS

Matter No M82/2018

AUSTRALIAN SECURITIES & INVESTMENTS COMMISSION — APPELLANT

AND

KIM SAMUEL JAQUES & ANOR — RESPONDENTS

Matter No M83/2018

AUSTRALIAN SECURITIES & INVESTMENTS COMMISSION — APPELLANT

AND

PETER CLARKE & ANOR — RESPONDENTS

Australian Securities & Investments Commission v Lewski
Australian Securities & Investments Commission v Wooldridge
Australian Securities & Investments Commission v Butler
Australian Securities & Investments Commission v Jaques
Australian Securities & Investments Commission v Clarke
[2018] HCA 63
13 December 2018
M79/2018, M80/2018, M81/2018, M82/2018 & M83/2018

ORDER

Matters M79, M80, M81 and M82 of 2018

1. Appeal allowed in part.

2. Set aside orders 2 to 6 of the orders of the Full Court of the Federal Court of Australia made on 1 November 2017 and in their place order that:

(a) the appeal be allowed in part;

(b) declarations 13, 21, 29, 37, 40, 41, 42, 43, 44, 45, 46, and 47 of the declarations and orders 1.1 to 1.4 and 2.1 to 2.5 of the orders made by the primary judge in proceeding VID 594 of 2012 ("Trial Proceeding") dated 2 December 2014 be set aside;

(c) order 3 of the orders made in the Trial Proceeding be set aside and in its place order that the second to fifth defendants pay the plaintiff's (namely, ASIC's) costs of and incidental to the proceeding; and

(d) the first respondent (namely, ASIC) pay the appellant's costs of and in connection with the dispute as to the form of orders.

3. *Remit the matter to the Full Court of the Federal Court for determination of penalty and disqualification orders, costs, and the cross-appeal to that Court.*

4. *The first respondent pay the appellant's costs of the appeal to this Court.*

Matter M83 of 2018

1. *Appeal allowed in part.*

2. *Set aside the orders of the Full Court of the Federal Court of Australia made on 1 November 2017 and in their place order that:*

   (a) *the appeal be allowed in part;*

   (b) *declarations 40 to 47 and order 2.5 of the orders made by the primary judge in proceeding VID 594 of 2012 ("Trial Proceeding") dated 2 December 2014 be set aside and in lieu thereof order that the plaintiff's claim in paragraphs 6 to 19 of its originating process dated 21 August 2012 in the Trial Proceeding in so far as it is made against the sixth defendant be dismissed; and*

   (c) *the first respondent (namely, ASIC) pay the costs of the appellant (namely, Mr Clarke) in the Trial Proceeding and in the Full Court of the Federal Court, including reserved costs.*

3. *There be no order as to the costs of the appeal to this Court.*

On appeal from the Federal Court of Australia

Representation

J T Gleeson SC and R D Strong with C van Proctor for the appellant in all matters (instructed by Australian Securities and Investments Commission)

B W Walker SC with M S Osborne QC and J P Tomlinson for the first respondent in M79/2018 (instructed by SBA Law)

N C Hutley SC with R G Craig for the first respondent in M80/2018, M81/2018 and M82/2018 (instructed by SBA Law, Millens and DLA Piper Australia)

Submitting appearance for the first respondent in M83/2018

Submitting appearance for the second respondent in all matters

CATCHWORDS

Australian Securities & Investments Commission v Lewski
Australian Securities & Investments Commission v Wooldridge
Australian Securities & Investments Commission v Butler
Australian Securities & Investments Commission v Jaques
Australian Securities & Investments Commission v Clarke

Companies – Managed investment schemes – Officers – Duties – Where each first respondent director of second respondent responsible entity of managed investment scheme – Where four directors resolved to amend scheme's constitution to introduce new fees payable to responsible entity out of scheme's assets – Where all five directors resolved to lodge and lodged amended constitution with Australian Securities & Investments Commission ("ASIC") – Where all five directors resolved to pay fees and caused payments to be made – Where ASIC alleged contraventions of *Corporations Act 2001* (Cth) by responsible entity and directors – Where proceedings alleging contraventions in relation to amendment resolution time-barred – Whether amendments to constitution adversely affected members' rights – Whether Full Court erred in holding amendments valid from lodgement until set aside – Whether Full Court erred in holding no breaches of duty occurred because of honest belief that constitution validly amended – Whether Full Court erred in holding directors not involved in contravention of s 208 of *Corporations Act* by responsible entity.

Words and phrases – "adversely affect", "breach of duty", "essential element of the contravention", "financial benefit", "honest belief", "improper use of a position", "interests", "interim validity", "invalid", "involved in a contravention", "listing fee payments", "lodgement", "loyalty", "member approval", "members' rights".

Corporations Act 2001 (Cth), Pt 5C.3, ss 9, 79, 136, 208, 209(2), 229, 601FC, 601FD, 601GA(2), 601GC, 601LC, 1317K, 1318, 1322.

KIEFEL CJ, BELL, GAGELER, KEANE AND EDELMAN JJ.

Introduction

1 On 22 August 2006, a meeting was held of the board of directors ("the Board") of Australian Property Custodian Holdings Ltd ("APCHL"), the responsible entity of a managed investment scheme. At an earlier meeting, on 19 July 2006, the Board had approved a Deed of Variation that made amendments to the constitution of the scheme. The Deed of Variation had not taken effect because it had not been lodged with the Australian Securities and Investments Commission ("ASIC"). The Board resolved to lodge the amended constitution with ASIC. If the amendments were valid, their effect would have been to introduce, without any corresponding benefit to the members of the scheme, very substantial new fees payable to the responsible entity. One of the new fees, payable if the scheme were successfully listed on the Australian Securities Exchange ("the ASX"), amounted to $33 million, which was between one-third and two-thirds of the entire capital expected to be raised on the listing. That fee was payable from the assets of the scheme to the responsible entity, and from there to entities associated with one of the directors, Mr Lewski.

2 Since ASIC did not bring proceedings within six years of the Board meeting on 19 July 2006[1], the contraventions that ASIC sought to prove at trial in the Federal Court of Australia focused upon the events at the later Board meeting on 22 August 2006 and thereafter. Central among the issues was whether the responsible entity and the directors had contravened the *Corporations Act 2001* (Cth) by resolving to lodge the amended constitution with ASIC and by later acts effecting the payment of those fees.

3 The primary judge found that the responsible entity and the directors had contravened numerous provisions of the *Corporations Act*, including, in broad terms, duties of care and skill, duties of loyalty, duties not to make improper use of a position, and duties of compliance. Declarations of contravention were made, as were orders imposing various pecuniary penalties and periods of disqualification on the directors. The Full Court of the Federal Court of Australia allowed appeals by the responsible entity and directors. The Full Court quashed all the declarations and orders made by the primary judge. The Full Court did not, therefore, need to consider ASIC's cross-appeals in relation to the penalties ordered.

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1 *Corporations Act 2001* (Cth), s 1317K.

4 The essence of the Full Court's reasoning was as follows. Since the Board had resolved on 19 July 2006 to amend the scheme constitution, then, absent dishonesty, there could be no contraventions arising from actions intended to give the amendments legal effect or actions to implement payments based upon the amendments. Effectively, any negligence, disloyalty, improper use of a position, or failure of compliance was spent. The Full Court also overturned the primary judge's conclusion that one of the directors, Mr Clarke, who was only appointed on 21 August 2006, had contravened the *Corporations Act* by voting in favour of the 22 August 2006 resolution. In its appeals to this Court, ASIC did not seek to disturb the Full Court's orders in relation to Mr Clarke.

5 For the reasons that follow, the appeals to this Court should be allowed in part. With the exception of the declarations in relation to Mr Clarke and the declarations relating to one group of contraventions concerning s 208 (as modified by s 601LC)[2] of the *Corporations Act*, all the declarations made by the primary judge should be restored. The matter should be remitted to the Full Court for the hearing of ASIC's cross-appeals against penalty in that Court and for re-determination of the penalties and disqualification periods for the directors other than Mr Clarke.

Background

6 By deed dated 27 December 2000, APCHL created a unit trust called the Prime Retirement and Aged Care Property Trust ("the Trust"). The business of the Trust was retirement villages and aged care facilities. On 23 July 2001, the Trust was registered by ASIC, as required by s 601EB of the *Corporations Act*, as a managed investment scheme and the consolidated trust deed became the constitution of the managed investment scheme ("the Constitution").

7 It was difficult for members to sell their units in the Trust, for which there was no secondary market. From March 2006, they could not redeem their units due to suspension of the redemption facility. The Constitution provided that one event that would cause the Trust to vest was where the responsible entity had not passed a resolution, on or before 31 July 2007, to seek listing of the units on an appropriate exchange (such as the ASX).

8 APCHL was the responsible entity of the managed investment scheme. The first respondent in Matter No M79 of 2018, Mr Lewski, together with his

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2 Referred to simply as "s 208" in the remainder of these reasons.

family and an associated company, owned all the shares in APCHL. Mr Lewski was the driving force behind APCHL and a director. Apart from Mr Clarke, the first respondent in each of the other appeals (Dr Wooldridge, Mr Butler, and Mr Jaques) was a director of APCHL at all relevant times. Mr Clarke commenced as a director on 21 August 2006. By the Board meeting on 22 August 2006, each of the first respondents was a director of APCHL ("the Directors").

9 The Constitution provided for various fees payable to APCHL, including (i) an "Exit Fee" payable on the determination of the Trust (2.5 per cent of its gross asset value) or the sale of all of its main assets and undertakings (2.5 per cent of the net sale proceeds), and (ii) a "Takeover Fee" of 2.5 per cent of the gross price paid for the units in any acquisition by an acquirer who held or thereby obtained more than 20 per cent of the units.

10 In June 2006, APCHL was systematically moving towards listing the Trust on the ASX. The likelihood was that the Trust would be listed within the next 12 to 18 months. The Trust had gross assets of $568 million and total liabilities of around $356 million, its net assets therefore being around $212 million.

11 On 20 June 2006, Mr Lewski contacted APCHL's solicitors seeking legal advice about amending the Constitution without consulting the members. Mr Lewski, Mr Butler and Dr Wooldridge said that they were concerned about the possibility of an opportunistic, "low-ball" takeover attempt on the Trust, and that those concerns prompted the Board to investigate "poison pills" to discourage such attempts. However, the primary judge held that (i) there was no real threat of an opportunistic takeover attempt that might have led to APCHL's removal as responsible entity, and (ii) a poison pill would also discourage reasonable takeover offers, which were one of the few ways that a member could crystallise her or his investment before listing or vesting[3].

12 Mr Lewski instructed APCHL's solicitors that he believed that there were "anomalies" in the Constitution because: (i) the Constitution did not provide for a fee to be paid to APCHL upon listing of the Trust; (ii) the Constitution did not provide for a fee to be paid to APCHL upon removal of APCHL as responsible

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3 *Australian Securities and Investments Commission v Australian Property Custodian Holdings Ltd (Receivers and Managers appointed) (In liq) (Controllers appointed) [No 3]* (2013) 31 ACLC ¶13-073 at 1118 [303], [307].

entity either after a takeover or otherwise by the members; and (iii) the Takeover Fee provided for in the Constitution was based on the net equity of the Trust rather than its gross asset value. Mr Lewski wanted to amend the Constitution "without needing to go to the Unit Holders" because he was concerned that the members would not approve these additional fees.

13 The additional fees that Mr Lewski proposed were as follows:

1. a new "Listing Fee" of 2.5 per cent of the gross asset value of the Trust at the time immediately before APCHL is listed on the ASX;

2. a new "Removal Fee" of 2.5 per cent of the gross asset value of the Trust if APCHL is removed as responsible entity of the Trust (other than by reason of proven fraud or misconduct, or by ASIC); and

3. amending the Takeover Fee to be based on the gross asset value of the Trust rather than its net equity

(together, "the Amendments").

14 Mr Lewski discussed with APCHL's solicitors their draft advice on several occasions. The final advice was provided by the solicitors to Mr Lewski on 14 July 2006.

15 The advice from APCHL's solicitors correctly identified s 601GC(1)(b) as an obstacle to the Amendments. The advice said that "case law" indicated that an amendment that changes the value of units does not, of itself, affect members' rights, and that a resolution of the members is not required unless a right, such as a right to a distribution, a right to vote, or a right to receive information, is adversely affected.

16 APCHL's solicitors' advice then turned to cl 25.1 of the Constitution. Clause 25.1 provides relevantly as follows:

"**Amendment to Trust**

(a) Subject to clause 25.1(b), the Responsible Entity for the time being may at any time and from time to time by deed revoke add to or vary all or any of the trusts, powers, conditions or provisions contained in this Deed … provided further that any such revocation, addition or variation:

(i) shall not be in favour of or result in any benefit to the Responsible Entity;

...

(b) Any amendment of this Deed must comply with the Corporations Act.

[See section 601GC for power to amend. The amendment cannot take effect until a copy of the amendment is lodged with ASIC.]"

17 The solicitors advised that cl 25.1 could be interpreted in two ways. On one interpretation, cll 25.1(a) and 25.1(b) both needed to be satisfied such that an amendment was only possible where it (i) neither was in favour of nor resulted in any benefit to APCHL, and (ii) was not contrary to the *Corporations Act*. On the second interpretation, cl 25.1(b) qualified cl 25.1(a) such that an amendment could be made, notwithstanding its noncompliance with cl 25.1(a), if it complied with the *Corporations Act*. This part of the advice concluded by saying, in effect, that the Amendments could be made without member approval if the Directors (none of whom were legally qualified) (i) interpreted cl 25.1 in the second manner, and (ii) reasonably considered that members' rights were not adversely affected. APCHL's solicitors did not advise which interpretation should be preferred.

18 The advice was provided to each of the Directors (other than Mr Clarke, who had not yet been appointed) prior to the Board meeting on 19 July 2006. It was accompanied by a draft Deed of Variation.

19 At the Board meeting on 19 July 2006, Mr Lewski moved, and Mr Jaques seconded, a resolution to pass the Amendments ("the Amendment Resolution"). The Amendment Resolution was passed unanimously, with all of the Directors (again, other than Mr Clarke) voting in favour of the Amendments. Although the minutes of the meeting describe discussion of "'poison pills' and [responsible entity] protection", there was either scant or no discussion of matters concerning the conflict between the interests of APCHL and its members, the gratuitous nature of the fees to be paid to APCHL, the uncertainty deriving from the solicitors' advice concerning the power to make the Amendments, and whether the Amendments were appropriate.

20 The Deed of Variation containing the Amendments was signed by two of the Directors at the Board meeting on 19 July 2006, but, following legal advice from APCHL's solicitors, it was left undated until it could be lodged together

with a "Supplementary Product Disclosure Statement", which was not then ready. The Supplementary Product Disclosure Statement included matters such as: (i) the appointment of Mr Clarke; (ii) updating the fees table to include the Listing Fee and the Removal Fee; and (iii) updating compliance arrangements.

21 On 21 August 2006, the Directors were provided with a draft Supplementary Product Disclosure Statement and a copy of the Deed of Variation signed on 19 July 2006. APCHL's solicitors advised that the Deed of Variation would take effect on the date that it was lodged with ASIC and proposed that it be dated and lodged on 22 August 2006.

22 At the Board meeting on 22 August 2006, the Directors passed a resolution ("the Lodgement Resolution") by which the Board resolved to lodge with ASIC a consolidated Constitution incorporating the Amendments so that they would become effective. The minutes of the meeting included the following:

> "At the last Board meeting, the Directors approved Deed of Variation (No 7) to the Constitution which had not yet taken effect as it had not been lodged with ASIC because a Supplementary PDS had not yet been prepared. As a Supplementary PDS has now been prepared, the Directors resolved that the Consolidated Constitution incorporating Deed of Variation (No 7) be lodged with ASIC to become effective."

23 At the meeting no further consideration was given to the issues of conflict of interest, the gratuitous nature of the fees, the uncertainty about the power to make the Amendments, or the propriety of the Amendments. The Deed of Variation, which had been signed at the 19 July 2006 meeting, was dated 22 August 2006. The form accompanying the lodgement stated that APCHL had modified the Constitution on 22 August 2006. Lodgement occurred on 23 August 2006.

24 On 26 June 2007, with the listing process underway, the Directors formally resolved to list the Trust on the ASX. They also resolved that the Listing Fee be paid to APCHL as follows: (i) ten per cent as units issued to APCHL at the time of allotment and official quotation of the Trust units on the ASX; (ii) the remainder deferred over a three-year "Deferral Period" and payable in annual tranches, 50 per cent in cash and 50 per cent as units, subject to performance hurdles with a waiver of the annual fee if the relevant performance hurdle is not met; and (iii) in the event of removal of APCHL as responsible entity during the Deferral Period, the unpaid balance becomes immediately payable in cash.

25 The total Listing Fee was calculated by APCHL's auditors as $32,939,947. The payment of the Listing Fee was enabled by a number of resolutions and acts of the Directors in addition to the 26 June 2007 resolution, collectively described as the "Payment Resolutions" in submissions (although the defined term includes both resolutions and acts to effect payment):

1. On 27 July 2007, the Directors resolved that the initial tranche of the Listing Fee be paid as units and that 3,293,994 units be issued to APCHL. This occurred on 3 August 2007.

2. On 7 April 2008, the Directors resolved to amend the 26 June 2007 resolution so that if "interests associated with [Mr] Lewski cease to control [APCHL] ... prior to the end of the Deferral Period the unpaid balance will become immediately payable in cash to [APCHL]". As the Directors then knew, an agreement for Mr Lewski to sell his interests in APCHL was either finalised or close to being finalised at that time. Execution of that agreement was approved by the Directors, other than Mr Lewski, on 23 and 24 April 2008.

3. On 27 June 2008, at a Board meeting attended by only Mr Lewski, Mr Jaques, and Mr Clarke, those Directors resolved to execute a Deed of Acknowledgement of Listing Fee Payment that provided for payment of the remainder of the Listing Fee as (i) 9,020,386 units in the Trust (with a value of $5 million), and (ii) $24,645,953 in cash. Following that execution, the unit issue, to a company controlled by Mr Lewski, and the cash payment, to APCHL and then to a company controlled by Mr Lewski, occurred on 27 and 30 June 2008 respectively.

26 The description of the payments as "fees" in these reasons, following the approach taken in submissions, is a euphemism. None was a payment for any additional obligation upon APCHL or the Directors, nor was any a payment for any additional benefit to members. The amounts of the "fees" were substantial. For instance, the Listing Fee of about $33 million amounted to between one-third and two-thirds of the entire capital expected to be raised on the listing. As for the Takeover Fee, in one scenario it could have required that a "fee" of $15 million be paid to APCHL following a takeover, increased from only $75,000 prior to the Amendments[4]. Finally, the amendment of the Listing Fee payment terms on

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4 *Australian Securities and Investments Commission v Australian Property Custodian Holdings Ltd (Receivers and Managers appointed) (In liq) (Controllers appointed) [No 3]* (2013) 31 ACLC ¶13-073 at 1089 [114].

7 April 2008 caused the crystallisation and acceleration of the Listing Fee payment to APCHL and Mr Lewski's associated companies.

The alleged contraventions

27 As the primary judge observed, the contraventions alleged by ASIC fell into three broad groups. None of the contraventions alleged a breach of duty by the Directors in passing the Amendment Resolution on 19 July 2006. As more than six years had elapsed since 19 July 2006, ASIC was barred by s 1317K of the *Corporations Act* from bringing proceedings alleging the commission of a contravention on that date. ASIC therefore relied for its allegations of contravention upon the passing of the Lodgement Resolution and the Payment Resolutions. The three groups, in chronological order of alleged contravention, were as follows.

28 The first group of contraventions concerned the Lodgement Resolution. ASIC alleged that passing the Lodgement Resolution founded various contraventions, which can be categorised as follows:

1. The "Negligence Duties": a breach by APCHL[5] and each Director[6] of their duty to exercise reasonable care and diligence;

2. The "Loyalty Duties": a breach by APCHL[7] and each Director[8] of their duty to act in the best interests of the members of the Trust and to give priority to the interests of the members of the Trust over their own interests;

3. The "Improper Use Duties": a breach by each Director of his duty not to make improper use of his position as an officer of APCHL[9]:

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5 *Corporations Act*, s 601FC(1)(b), (5).

6 *Corporations Act*, s 601FD(1)(b), (3).

7 *Corporations Act*, s 601FC(1)(c), (5).

8 *Corporations Act*, s 601FD(1)(c), (3).

9 *Corporations Act*, s 601FD(1)(e), (3).

(a) to provide an advantage to APCHL or to provide an indirect advantage to persons who would benefit from the fees paid to APCHL; or

(b) to cause detriment to members of the Trust; and

4. The "Compliance Duties": a breach by APCHL of its duty to comply with cl 25.1 of the Constitution in varying or attempting to vary the Constitution in a manner that was in favour of or resulted in a benefit to APCHL[10] and a breach by each Director of his duty to take all steps that a reasonable person in his position would take to ensure that APCHL complied with the Constitution and the *Corporations Act*[11].

29 The second group of contraventions concerned the Payment Resolutions. ASIC alleged breaches by APCHL[12] and each Director[13] of their Loyalty Duties and breaches by APCHL[14] and each Director[15] of their Compliance Duties.

30 The third group of contraventions concerned the actual payment by APCHL of the Listing Fee in cash to itself and then to one of Mr Lewski's associated companies, and in units directly to one of Mr Lewski's associated companies ("the Listing Fee Payments"). ASIC alleged that APCHL contravened s 208 and that the Directors each contravened s 209(2) by their involvement in APCHL's contravention.

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10 *Corporations Act*, s 601FC(1)(m), (5).

11 *Corporations Act*, s 601FD(1)(f), (3).

12 *Corporations Act*, s 601FC(1)(c), (5).

13 *Corporations Act*, s 601FD(1)(c), (3).

14 *Corporations Act*, s 601FC(1)(k), (5).

15 *Corporations Act*, s 601FD(1)(f), (3).

The Federal Court and Full Court decisions

The Federal Court decision

31 The primary judge, Murphy J, held that the Amendment Resolution was invalid. Section 601GC(1) of the *Corporations Act* required that an amendment to the Constitution that was not made by special resolution of the members of the scheme required the responsible entity reasonably to consider that the change would not adversely affect members' rights. Since the Amendments affected members' rights, and since APCHL did not consider whether the Amendments would adversely affect members' rights, the Amendments were not valid[16].

32 As to the Negligence Duties, the primary judge held that the Directors did not read and understand the effects of the Amendments before passing the Amendment Resolution or the Lodgement Resolution, and that the effects of the Amendments were not considered by the Directors acting as a Board[17].

33 As to their understanding, the Directors did not understand the following: (i) the Takeover Fee could be charged on multiple occasions; (ii) the increased Takeover Fee and the Removal Fee could be payable notwithstanding prior payment of the Listing Fee; (iii) the Removal Fee provided little additional protection for members against opportunistic, "low-ball offers" for their units; (iv) the increased Takeover Fee would discourage reasonable offers for members' units; and (v) the Removal Fee would significantly impair the ability of members to remove APCHL as responsible entity.

34 As to their consideration, the Directors did not consider the fact that the introduction of substantial additional fees was effectively gratuitous. None of the Directors gave proper consideration to the mutually exclusive interpretations of cl 25.1 of the Constitution that APCHL's solicitors had left open for their consideration, including whether to seek unequivocal legal advice or a judicial direction. Nor did any Director consider whether the Amendments should be

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16 *Australian Securities and Investments Commission v Australian Property Custodian Holdings Ltd (Receivers and Managers appointed) (In liq) (Controllers appointed) [No 3]* (2013) 31 ACLC ¶13-073 at 1178 [665]-[667], 1179 [673].

17 *Australian Securities and Investments Commission v Australian Property Custodian Holdings Ltd (Receivers and Managers appointed) (In liq) (Controllers appointed) [No 3]* (2013) 31 ACLC ¶13-073 at 1119 [309]-[311], 1120 [315], 1120-1121 [321], 1121 [323]-[324], 1164 [589].

made, that is, whether it was proper to make them even if there were power to do so.

35 The primary judge found that all of the contraventions alleged by ASIC were established. However, as his Honour held, the position of Mr Clarke, who was not a director at the time of the Amendment Resolution, was different in some respects. The primary judge accepted that it was unrealistic to expect Mr Clarke to have called for the legal advice concerning the Amendment Resolution when considering the Lodgement Resolution at the Board meeting on 22 August 2006[18]. Nevertheless, the primary judge concluded that Mr Clarke did not give the Lodgement Resolution or the Amendments any consideration, and that he remained silent through the meeting and was a passive participant[19]. The primary judge concluded that if Mr Clarke had given proper consideration to the matters before him then he should have understood their deleterious effects, APCHL's conflict of interest, and the lack of any countervailing benefit to the members for the imposition of substantial additional fees[20].

36 The primary judge made 47 declarations of contravention by APCHL and the Directors under s 1317E. The declarations concerned: (i) the Lodgement Resolution (the Negligence Duties[21], the Loyalty Duties[22], the Improper Use Duties[23], and the Compliance Duties[24]); (ii) the Payment Resolutions (the Loyalty

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18 *Australian Securities and Investments Commission v Australian Property Custodian Holdings Ltd (Receivers and Managers appointed) (In liq) (Controllers appointed) [No 3]* (2013) 31 ACLC ¶13-073 at 1163 [580].

19 *Australian Securities and Investments Commission v Australian Property Custodian Holdings Ltd (Receivers and Managers appointed) (In liq) (Controllers appointed) [No 3]* (2013) 31 ACLC ¶13-073 at 1147 [493(b)]-[494], 1163-1164 [584].

20 *Australian Securities and Investments Commission v Australian Property Custodian Holdings Ltd (Receivers and Managers appointed) (In liq) (Controllers appointed) [No 3]* (2013) 31 ACLC ¶13-073 at 1163-1164 [584].

21 Declarations 1, 8, 16, 24, 32, 40.

22 Declarations 2, 9, 17, 25, 33, 41.

23 Declarations 10, 11, 18, 19, 26, 27, 34, 35, 42, 43.

24 Declarations 3, 12, 20, 28, 36, 44.

Duties[25] and the Compliance Duties[26]); and (iii) the Listing Fee Payments[27]. Although the primary judge found that APCHL had contravened s 208, s 1317E did not require the primary judge to make a declaration of contravention by APCHL of s 208 and none was made.

37 The primary judge also disqualified each Director except Mr Clarke from managing corporations for various periods of time[28] under s 206C. His Honour ordered pecuniary penalties under s 1317G against each Director[29].

The Full Court decision

38 The Directors, but not APCHL, appealed to the Full Court[30]. ASIC cross-appealed in relation to the adequacy of the pecuniary penalties and disqualifications imposed on the Directors. The Full Court (Greenwood, Middleton and Foster JJ) concluded that the primary judge erred because, although the Amendment Resolution was "invalid" and was "no decision at all"[31], the Amendments nevertheless had "interim validity"[32]; once lodged with ASIC, they would be "valid until set aside"[33]. That concept had the effect that, despite a

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25 Declarations 4, 6, 14, 22, 30, 38, 46.

26 Declarations 5, 7, 15, 23, 31, 39, 47.

27 Declarations 13, 21, 29, 37, 45.

28 Mr Lewski, 15 years (Order 1.1); Mr Butler, 4 years (Order 1.2); Mr Jaques, 4 years (Order 1.3); and Dr Wooldridge, 2 years and 3 months (Order 1.4).

29 Mr Lewski, $230,000 (Order 2.1); Mr Butler, $20,000 (Order 2.2); Mr Jaques, $20,000 (Order 2.3); Dr Wooldridge, $20,000 (Order 2.4); and Mr Clarke, $20,000 (Order 2.5).

30 *Lewski v Australian Securities and Investments Commission* (2016) 246 FCR 200.

31 *Lewski v Australian Securities and Investments Commission* (2016) 246 FCR 200 at 273 [247].

32 *Lewski v Australian Securities and Investments Commission* (2016) 246 FCR 200 at 273 [245].

33 *Lewski v Australian Securities and Investments Commission* (2016) 246 FCR 200 at 274 [253].

failure to comply with the requirement for amending the Constitution in s 601GC(1)(b), when APCHL lodged the Amendments with ASIC they were given retroactive effect unless, and until, set aside.

39 The Full Court also concluded that the primary judge erred in finding that contraventions had occurred when, according to the Full Court, at the time of the Lodgement Resolution and the Payment Resolutions, "[t]he Directors were entitled to act in accordance with the Constitution which they honestly believed existed, and make decisions accordingly"[34]. Hence, the Full Court said that it should proceed on the basis that the Amendment Resolution and the Lodgement Resolution were "made and in existence, and formed a basis for subsequent decision making by the Directors"[35]. On that premise, the Full Court concluded that APCHL and the Directors were not liable for the breaches of duty under ss 601FC and 601FD because they had an honest belief that the Constitution had been amended[36]. The Full Court also overturned the primary judge's finding that, despite Mr Clarke's passive conduct and silence, he had voted in favour of the Lodgement Resolution. That finding was the sole basis for the finding of contravention against Mr Clarke for the events of 22 August 2006[37].

40 Before orders were made on the appeals, the Directors submitted that the consequence of allowing the appeals was that the declarations against APCHL should not have been made. On the Directors' application, APCHL was joined to each appeal. ASIC sought leave to file a notice of contention and submitted that the Full Court should reconsider its reasons for decision. The Full Court did so but did not depart from any of its reasons or conclusions. In lengthy reasons, it reiterated its previous reasons for decision and ordered that all of the orders and declarations made by the primary judge, including those in relation to APCHL,

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34 *Lewski v Australian Securities and Investments Commission* (2016) 246 FCR 200 at 296 [341].

35 *Lewski v Australian Securities and Investments Commission* (2016) 246 FCR 200 at 275 [257].

36 *Lewski v Australian Securities and Investments Commission* (2016) 246 FCR 200 at 284-285 [301]-[302], 297 [346].

37 *Lewski v Australian Securities and Investments Commission* (2016) 246 FCR 200 at 241 [129]-[130].

be set aside[38]. As the Full Court allowed the appeals, it did not need to consider the cross-appeals brought by ASIC and simply ordered that they be dismissed.

The grounds of appeal and the pleading issues

41 The orders of the Full Court were expressed globally in relation to all of the Directors and ASIC appealed against those global orders. However, ASIC did not seek to disturb the Full Court's orders in relation to Mr Clarke (the sixth defendant at trial). Hence, although an appeal was brought from the global orders made in relation to Mr Clarke, there was no challenge to the quashing of the primary judge's particular declarations[39] and penalty[40] concerning Mr Clarke.

42 ASIC relied upon three grounds of appeal in each appeal in this Court. The first alleged that the Full Court erred by concluding that Pt 5C.3 of the *Corporations Act*, which includes s 601GC(1)(b), contains a concept of interim validity. The second ground of appeal alleged that the Full Court erred in finding that APCHL and the Directors were not liable for the breaches of duty under ss 601FC and 601FD because they had an honest belief that the Constitution had been amended. The third ground of appeal was that the Full Court erred in concluding that the onus lay upon ASIC to prove that the Listing Fee Payments were not authorised by the Constitution consistently with s 208(3).

43 The Directors other than Mr Clarke ("the active respondents") submitted that ASIC's first two grounds of appeal were not matters that were pleaded at trial. The active respondents submitted that ASIC had not sought declaratory relief that the Constitution had not been validly amended, and they submitted that ASIC had not pleaded any event between the Amendment Resolution on 19 July 2006 and the Lodgement Resolution on 22 August 2006.

44 There is no substance to this pleading submission. Although ASIC did not seek a declaration that the Constitution had not been validly amended, ASIC's pleading concerning lodgement had this effect. ASIC pleaded that by lodging the Amendments APCHL intended to amend the Constitution. Section 601GC(2) prevents an amendment taking effect until it is lodged. ASIC pleaded that

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38 *Lewski v Australian Securities and Investments Commission [No 2]* (2017) 352 ALR 64 at 128 [200]-[201].

39 Declarations 40-47.

40 Order 2.5.

lodgement of a version of the Constitution containing the Amendments was not effective to amend the Constitution. ASIC also pleaded that by passing the Lodgement Resolution, the Directors contravened the Negligence Duties, the Loyalty Duties, the Improper Use Duties, and the Compliance Duties. All the pleaded facts concerning negligence, loyalty, improper use and compliance were matters that existed on 19 July 2006 and still existed on 22 August 2006. They were relied upon in ASIC's pleadings of contravention. That was ASIC's pleaded case. That was ASIC's case before the Full Court. And that was ASIC's case before this Court.

45 Apart from the three grounds of appeal, a logically anterior matter was raised by a notice of contention filed by each of the active respondents. The notice of contention sought to uphold the findings of the Full Court on the basis that a member's "right to have a managed investment scheme administered according to its terms" was not a "member's right" within the meaning of s 601GC(1)(b), such that APCHL had the power to make the Amendments.

The notice of contention and the first ground of appeal: s 601GC

46 The notice of contention and the first ground of appeal both focus closely on the meaning of s 601GC of the *Corporations Act*. It is convenient to set out that section in full:

> "**Changing the constitution**
>
> (1) The constitution of a registered scheme may be modified, or repealed and replaced with a new constitution:
>
> (a) by special resolution of the members of the scheme; or
>
> (b) by the responsible entity if the responsible entity reasonably considers the change will not adversely affect members' rights.
>
> (2) The responsible entity must lodge with ASIC a copy of the modification or the new constitution. The modification, or repeal and replacement, cannot take effect until the copy has been lodged.
>
> (3) The responsible entity must lodge with ASIC a consolidated copy of the scheme's constitution if ASIC directs it to do so.

(4) The responsible entity must send a copy of the scheme's constitution to a member of the scheme within 7 days if the member:

(a) asks the responsible entity, in writing, for the copy; and

(b) pays any fee (up to the prescribed amount) required by the responsible entity."

47 Section 601GC(1) confers a power on a responsible entity to amend the constitution of a registered scheme. That power can be exercised if, but only if, either of the conditions in para (a) or para (b) is met.

The notice of contention: the meaning of "members' rights" in s 601GC

48 The active respondents' notice of contention alleged that the primary judge and the Full Court both erred by concluding that APCHL was required, on 19 July 2006, to consider reasonably that the change to the Constitution would not adversely affect members' rights. The active respondents' submission was that the members had no "right" to the due administration of the Trust in accordance with the existing Constitution.

49 In contrast, ASIC submitted that the relevant members' rights had two sources. First, they were sourced in a "basal rule" arising from s 601GA(2) that any rights of APCHL "to be paid fees out of scheme property" must be "specified in the scheme's constitution" and "available only in relation to the proper performance of [APCHL's] duties". Secondly, they were sourced in the Constitution itself. Clause 34.1 provided that the Constitution was not "capable of being revoked added to or varied" otherwise than in accordance with Pt 25. Part 25 contained only cl 25.1, extracted above, which empowered the responsible entity to amend the Constitution subject to conditions including that the amendment "shall not be in favour of or result in any benefit to the Responsible Entity" (cl 25.1(a)(i)) and that the amendment must comply with the *Corporations Act* (cl 25.1(b)). It was common ground that the Amendments resulted in a benefit to APCHL.

50 The simple answer, however, to the notice of contention lies in the concession by senior counsel for Dr Wooldridge and Messrs Butler and Jaques that if "right" is used in s 601GC to mean "interest" then members' rights would have been adversely affected by the Amendments. That concession was properly

made. The word "interest" has a broad, general meaning[41] which, on any view, includes the concern of the members with the due administration of the Trust. And in s 601GC(1) that is, indeed, the sense in which "right" is used.

51 In the dictionary to the *Corporations Act*, s 9, a managed investment scheme is defined to include the feature that "people contribute money or money's worth as consideration to acquire rights (***interests***) to benefits produced by the scheme (whether the rights are actual, prospective or contingent and whether they are enforceable or not)". The definition also refers to the pooling of contributions to produce "benefits consisting of rights or interests in property, for the people (the ***members***) who hold interests". An "interest" in a managed investment scheme is defined as "a right to benefits produced by the scheme (whether the right is actual, prospective or contingent and whether it is enforceable or not)". And a "member" in relation to a managed investment scheme is defined as "a person who holds an interest in the scheme".

52 A further difficulty with the active respondents' interpretation of members' rights in a manner that does not treat them as "interests" generally is that this interpretation is contrary to the purpose of s 601GC to protect the members of the scheme. Section 601GC(1) is contained in Pt 5C.3 of the *Corporations Act*, which is concerned with the constitution of managed investment schemes. The responsible entity, which administers that constitution, was designed with a protective purpose[42]. Although a responsible entity is given some power to amend the constitution, the purpose of s 601GC(1) is therefore to confine that power to circumstances that, considered reasonably, will not adversely affect the members' rights unless the members so resolve. This purpose requires the notion of members' rights to have a broad construction.

53 In contrast with the broad construction of rights (as "interests") that the purpose of s 601GC would suggest, the active respondents' submission would have the consequence that a successful members' special resolution would be needed for matters having a relatively trivial adverse effect on members but not for matters having a catastrophic effect on members. For instance, member approval would be needed if a scheme constitution were amended to change the

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41 *Craig v Federal Commissioner of Taxation* (1945) 70 CLR 441 at 446, 457; [1945] HCA 1.

42 Australia, House of Representatives, *Parliamentary Debates* (Hansard), 3 December 1997 at 11928-11929.

frequency of reports to members from semi-annual to annual. But, on the active respondents' construction, it would not be needed for an amendment to require a payment out of scheme property that would remove most of the members' equity. An interpretation of s 601GC that has this effect gives no operation to its protective purpose.

54 An interpretation of members' rights as "interests" also accords with the prevailing authority. In *360 Capital RE Ltd v Watts*[43], the Court of Appeal of the Supreme Court of Victoria considered a purported amendment to the constitution of a registered managed investment scheme which removed restrictions upon the issue of redeemable unsecured convertible notes. 360 Capital submitted, relying upon decisions of the Supreme Court of New South Wales[44], that "members' rights" did not include the rights to have a managed investment scheme administered according to the constitution as it stands[45]. It was said that such a broad view of members' rights would deny all efficacy to s 601GC(1)(b) because any modification of the constitution would involve "an invasion of that right that is arguably adverse"[46]. The Court of Appeal unanimously rejected that submission and the authorities that supported it.

55 The Court of Appeal, following an earlier decision of Gordon J[47], held that members' rights included the right "to have a managed fund managed and administered in accordance with the constitution of the fund"[48]. As their Honours explained, that broad characterisation does not deny efficacy to s 601GC(1)(b). It may be that there are very few, if any, circumstances where an amendment to a constitution would not affect members' rights in this broad sense. But this is

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43 (2012) 36 VR 507.

44 *Smith v Permanent Trustee Australia Ltd* (1992) 10 ACLC 906; *ING Funds Management Ltd v ANZ Nominees Ltd* (2009) 228 FLR 444; *Re Centro Retail Ltd* (2011) 255 FLR 28.

45 (2012) 36 VR 507 at 513 [23].

46 (2012) 36 VR 507 at 515 [31], 516-517 [39], quoting *ING Funds Management Ltd v ANZ Nominees Ltd* (2009) 228 FLR 444 at 461 [98].

47 *Premium Income Fund Action Group Inc v Wellington Capital Ltd* (2011) 84 ACSR 600.

48 (2012) 36 VR 507 at 514 [26].

because the due administration of the scheme according to the constitution is "fundamentally the most important right of membership"[49]. In any event, amendments can nevertheless be made where they reasonably are not considered to affect members' rights *adversely*. An example is abbreviating a period for redemption of units from 90 days to 60 days[50].

56 The active respondents submitted that such a broad characterisation of members' rights in these terms involved the misdescription of a "right" and the mischaracterisation of its correlativity. They submitted that the characterisation would break down a necessary distinction between the nature of the rights and their value. But the meaning to be given to "member's right" in s 601GC(1)(b) is not to be derived, independently of the legislation, from philosophical conceptions of a right, themselves disputed and used in different senses. Further, a distinction, extrinsic to the legislation, between the nature of the rights and their value is "beside the point"[51]. The meaning of "members' rights" is to be determined by the statutory context in and purpose for which the words are used. That context and purpose reveals that "right" is used to mean "interest".

57 As the primary judge correctly held, each of the Lodgement Resolution and Payment Resolutions adversely affected the members' interests, and therefore their rights. The notice of contention must be dismissed.

The first ground of appeal: a notion of "interim validity" in s 601GC

58 The Full Court's conclusion that the Amendments had interim validity despite being passed contrary to s 601GC(1) was akin to a conclusion that s 601GC(1) was not a provision concerned with authority but only rendered noncompliant amendments voidable. Even then, however, the Full Court recognised two limitations that mean that the notion would be more accurately described as qualified voidability or qualified interim validity. First, amendments that were not made in compliance with s 601GC(1) would only

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49 (2012) 36 VR 507 at 517 [40]. See also *Youyang Pty Ltd v Minter Ellison Morris Fletcher* (2003) 212 CLR 484 at 498 [32]; [2003] HCA 15.

50 (2012) 36 VR 507 at 517 [41], citing *Eagle Star Trustees Ltd v Heine Management Ltd* (1990) 3 ACSR 232.

51 *360 Capital RE Ltd v Watts* (2012) 36 VR 507 at 518 [45].

"ordinarily" be valid until set aside[52]. The Full Court left open the possibility that an amendment would have no effect if the directors knew or had reason to believe that there was no authority to make it under s 601GC(1)[53]. Secondly, a notion of interim validity in s 601GC would only take effect once the amendments had been lodged with ASIC[54]. In effect, noncompliant amendments would have no legal force until lodged, but, upon lodgement, they would become voidable unless they had been made with knowledge of noncompliance. This notion of qualified interim validity is not supported by the text of s 601GC, which confers a power and defines its scope, nor by its protective purpose.

59 The Full Court sought to support the interim validity principle textually by analogy with this Court's approach in *Project Blue Sky Inc v Australian Broadcasting Authority*[55]. That decision held that an act will not usually be invalidated by a statutory requirement that regulates the exercise of functions already conferred, rather than imposing essential preliminaries to the exercise, especially where the provisions are expressed in indeterminate language, they do not have a rule-like quality, and the result of invalidity would be public inconvenience[56]. This analogy is inapt. There is no textual basis for interpreting s 601GC(1) as not invalidating a noncompliant amendment, still less as conferring some qualified interim validity upon it, based upon *Project Blue Sky* considerations. This is for a number of reasons: (i) the authority to amend the constitution derives from s 601GC(1) itself so the sub-section does not merely regulate an existing power; (ii) the sub-section contains a rule and is not expressed in indeterminate language; and (iii) any consideration of public

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52 *Lewski v Australian Securities and Investments Commission [No 2]* (2017) 352 ALR 64 at 125 [186].

53 *Lewski v Australian Securities and Investments Commission [No 2]* (2017) 352 ALR 64 at 127 [191].

54 *Lewski v Australian Securities and Investments Commission [No 2]* (2017) 352 ALR 64 at 125 [186]. See also *Lewski v Australian Securities and Investments Commission* (2016) 246 FCR 200 at 274 [253], [256].

55 (1998) 194 CLR 355; [1998] HCA 28. See *Lewski v Australian Securities and Investments Commission [No 2]* (2017) 352 ALR 64 at 125-126 [186].

56 (1998) 194 CLR 355 at 391-392 [94]-[97]. See also *Forrest & Forrest Pty Ltd v Wilson* (2017) 91 ALJR 833 at 844 [62]; 346 ALR 1 at 14; [2017] HCA 30.

inconvenience cannot ignore the injustice caused to members by an amendment that permits $33 million of their equity to be paid away without authority.

60 A notion of interim validity would also be in considerable tension with the structure of the *Corporations Act* in three significant respects. First, the *Corporations Act* has mechanisms to exonerate those who cause a constitution to be invalidly amended, which are inconsistent with the conversion of the requirement in s 601GC(2) to lodge the constitution with ASIC into a blunt guarantee of interim validity qualified only by dishonesty. Instead, the exoneration mechanisms provide the Court with wide latitude to grant relief, closely tailored to the circumstances of the case. For instance, s 1318 confers a power to relieve a person from liability for negligence, default, breach of trust or breach of duty, on such terms as the Court thinks fit, where the person has acted honestly and ought fairly to be excused. Further, s 1322(4)(c) permits the Court to make an order relieving a person from civil liability for a broad range of contraventions or failures referred to in s 1322(4)(a)[57], subject to conditions in s 1322(6) that include, but are not limited to, honesty.

61 Secondly, a general rule of interim validity after lodgement despite noncompliance with s 601GC(1), subject only to dishonesty, is in tension with provisions such as s 1322(2), which establishes a presumption of validity, but only for a procedural irregularity, defined to include matters such as the absence of a quorum at a meeting[58], and only unless the Court is of the opinion that the irregularity has caused or may cause substantial injustice that cannot be remedied by any order of the Court.

62 Thirdly, interim validity has never been suggested to apply to unauthorised amendments to the constitutions of corporations, either generally[59] or under the *Corporations Act*, where the definition of "constitution" in s 9 includes both a constitution of a company and a constitution of a managed investment scheme. For instance, s 136(2) of the *Corporations Act* provides that a company may modify or repeal its constitution, or a provision of it, by special resolution. And s 136(5) provides that the special resolution must be lodged with ASIC. Since s 601FC(2) creates a statutory trust of scheme property, it is also relevant that the notion of interim validity is inconsistent with the general law

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57 See *Weinstock v Beck* (2013) 251 CLR 396; [2013] HCA 14.

58 *Corporations Act*, s 1322(1)(b).

59 *Gambotto v WCP Ltd* (1995) 182 CLR 432 at 454; [1995] HCA 12.

principles concerning unauthorised amendments to a trust deed without consent of the beneficiaries[60]. In none of these analogous contexts has it been held that noncompliant amendments have interim validity.

63 The first ground of appeal must be upheld.

The second ground of appeal: the Negligence, Loyalty, Improper Use and Compliance Duties

The general premise of the Full Court's findings

64 The Full Court's conclusion in relation to the contraventions of the Negligence, Loyalty, Improper Use and Compliance Duties was effectively based upon a short premise: that, in the absence of any new facts or knowledge by any Director, any breach of duty was spent after the Amendment Resolution[61]. The active respondents submitted that the Directors committed no breach given that there were no new facts that could have given rise to a breach of duty since the Amendment Resolution was passed on 19 July 2006, and given that the Directors acted honestly in passing the Lodgement Resolution on 22 August 2006 and the subsequent Payment Resolutions.

65 The active respondents submitted that the Lodgement Resolution could not have involved any breach of duty because it was merely the performance of a duty required by s 601GC(2) and that duty was performed honestly. But although s 601GC(2) obliges the responsible entity to lodge an amendment with ASIC, and prevents the amendment taking effect until it has been lodged, the sub-section is concerned with amendments validly made. It does not oblige a responsible entity to lodge an amendment that was invalidly made. And it does not confer validity upon an amendment invalidly made.

66 The step of lodging the Constitution with ASIC, and therefore the resolution to do so, was no mere administrative task by APCHL. The Directors' resolution of 22 August 2006 that the Amendments be lodged with ASIC, and the dating of the Deed of Variation that same day, were acts intended to give legal effect to the Amendment Resolution, which, even if valid, would have remained inchoate and dependent upon dating and lodging to give it legal effect. As the

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60 See *Re Dion Investments Pty Ltd* (2014) 87 NSWLR 753 at 763-764 [45]-[46].

61 *Lewski v Australian Securities and Investments Commission* (2016) 246 FCR 200 at 284-285 [301], 296 [341].

Directors had been advised, without lodgement the Amendments could have no legal effect.

67 Even after the Lodgement Resolution, the Directors' subsequent actions were not insulated from the possibility of further contraventions. The Payment Resolutions, by which the Listing Fee was resolved to be paid to APCHL and Mr Lewski and his associated companies in an accelerated manner, also attracted, at least, the pleaded Loyalty Duties and Compliance Duties.

The Negligence Duties

68 The contraventions found by the primary judge based upon ss 601FC(1)(b) and 601FD(1)(b), concerning APCHL and each Director respectively, involve an objective test of the degree of care that a reasonable person would exercise tailored to the circumstances of the responsible entity or director. As the primary judge concluded[62], on 22 August 2006 the circumstances of each Director other than Mr Clarke were such that he ought reasonably to have known that his consideration of the Amendments on 19 July 2006 was inadequate[63].

69 The Full Court's conclusion that "a reasonable director, honestly believing the previous decisions to be adequate, would not normally re-visit such decisions"[64] missed the point that the vote by the Directors in favour of the Lodgement Resolution was the step taken by the Directors to facilitate giving legal effect to the Amendments. They did so in the same circumstances as had prevailed on 19 July 2006 at the time of the Amendment Resolution. The inadequate consideration given to the Amendments by the Directors (other than Mr Clarke) on 19 July 2006, of which they should have been aware, meant that the same lack of understanding existed at the time of the Lodgement Resolution: the misunderstandings concerning the Takeover Fee and the Removal Fee

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62 *Australian Securities and Investments Commission v Australian Property Custodian Holdings Ltd (Receivers and Managers appointed) (In liq) (Controllers appointed) [No 3]* (2013) 31 ACLC ¶13-073 at 1161-1162 [568]-[569].

63 See *Shafron v Australian Securities and Investments Commission* (2012) 247 CLR 465 at 482 [34]-[35]; [2012] HCA 18.

64 *Lewski v Australian Securities and Investments Commission* (2016) 246 FCR 200 at 284-285 [301]; *Lewski v Australian Securities and Investments Commission [No 2]* (2017) 352 ALR 64 at 111 [111].

remained; there was no consideration of the nature or propriety of the introduction of substantial, additional, effectively gratuitous fees; and the uncertainty deriving from the solicitors' equivocal advice about the power to make the Amendments had not been resolved.

The Loyalty Duties

70 Sections 601FC(1)(c) and 601FD(1)(c) each involve two separate duties of loyalty. The first is a duty to act in the best interests of the members. The second is to give priority to the members' interests if there is a conflict between the members' interests and the interests of the responsible entity. The Full Court overturned the primary judge's finding[65] that both duties had been contravened by the Lodgement Resolution and the Payment Resolutions. The Full Court held that the Directors were "entitled to act in accordance with the Constitution which they honestly believed existed, and make decisions accordingly"[66].

71 The Loyalty Duty requiring a director to act in the best interests of members is not purely subjective. As Bowen LJ said of the equitable progenitor from which this statutory duty was developed and adapted[67], otherwise a wholly irrational but honest director could conduct the affairs of the company by "paying away its money with both hands in a manner perfectly *bonâ fide* yet perfectly irrational"[68]. Although the duty is not satisfied merely by honesty, it is a duty to act in the best *interests* of the members rather than a duty to secure the best *outcome* for members. Key factors in ascertaining the best interests of the members are the purpose and terms of the scheme, rather than "the success or

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65 *Australian Securities and Investments Commission v Australian Property Custodian Holdings Ltd (Receivers and Managers appointed) (In liq) (Controllers appointed) [No 3]* (2013) 31 ACLC ¶13-073 at 1168 [617], 1169 [619], 1193 [748].

66 *Lewski v Australian Securities and Investments Commission* (2016) 246 FCR 200 at 296 [341], see also at 283 [297], 297 [346]. See also *Lewski v Australian Securities and Investments Commission [No 2]* (2017) 352 ALR 64 at 88 [36], 99 [48], 109-110 [102], 111 [111], 119-120 [159]-[160].

67 Australia, House of Representatives, *Parliamentary Debates* (Hansard), 3 December 1997 at 11929; Australia, House of Representatives, *Parliamentary Debates* (Hansard), 3 March 1998 at 242.

68 *Hutton v West Cork Railway Co* (1883) 23 Ch D 654 at 671.

otherwise of a transaction or other course of action"[69]. The purpose and terms of the Trust are the existing legal purposes and terms of the Constitution, not the purpose or terms that are honestly believed to exist.

72 The Loyalty Duty requiring a director to give priority to the members' interests in circumstances of conflict of interest is narrower in one respect than the equitable rule concerning conflict of interest and duty[70]. It does not proscribe acts of a director that put herself or himself in a position of conflict[71]. It only proscribes acts in the course of that conflict that do not give priority to the members' interests. Nevertheless, the duty is not satisfied by an honest or reasonable belief. A contravention occurs when a director prioritises her or his own interests over those of the members, no matter how honest or reasonable the director was in doing so.

73 In summary, it was not sufficient for compliance with either of the Loyalty Duties that the Directors acted honestly, having regard to their belief that the Constitution had been amended. The primary judge correctly concluded that none of the Directors could reasonably have believed that it was in the best interests of the members to bring the Amendments into effect by the Lodgement Resolution or to make the accelerated Listing Fee Payments by the Payment Resolutions. His Honour also correctly concluded that the Directors should have voted against the Lodgement Resolution in order to prioritise the members' interests in having APCHL comply with the Constitution over the conflicting interest of APCHL in receiving the fees.

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69 Langford, *Directors' Duties: Principles and Application* (2014) at 61 [4.2.2]. See also Nicholls, "Trustees and their Broader Community: Where Duty, Morality and Ethics Converge" (1996) 70 *Australian Law Journal* 205 at 211.

70 See *Chan v Zacharia* (1984) 154 CLR 178 at 198; [1984] HCA 36.

71 Compare *Commonwealth Bank of Australia v Smith* (1991) 42 FCR 390 at 392; *Maguire v Makaronis* (1997) 188 CLR 449 at 466; [1997] HCA 23; *Beach Petroleum NL v Kennedy* (1999) 48 NSWLR 1 at 47 [200].

The Improper Use Duties

74 The Full Court overturned the primary judge's conclusion[72] that, in passing the Lodgement Resolution, each Director had made improper use of his position as an officer of APCHL, contrary to s 601FD(1)(e), to (i) provide an advantage to APCHL and an indirect advantage to persons who would benefit from the fees paid to APCHL, and (ii) cause detriment to members of the Trust. Although the Full Court gave no specific reasons in relation to these duties, it must be taken to have reached its conclusion again on the basis that the Directors were entitled to act in accordance with the terms of the Constitution that they honestly believed to exist[73].

75 The Full Court erred in concluding that the Improper Use Duties were fulfilled by the honest beliefs of the Directors at the time of the Lodgement Resolution. In the context of a director's duty to the company not to use her or his position for an improper purpose, it has been repeatedly said in this Court that[74]:

> "[i]mpropriety does not depend on an alleged offender's consciousness of impropriety. Impropriety consists in a breach of the standards of conduct that would be expected of a person in the position of the alleged offender by reasonable persons with knowledge of the duties, powers and authority of the position and the circumstances of the case. When impropriety is said to consist in an abuse of power, the state of mind of the alleged offender is important: the alleged offender's knowledge or means of knowledge of the circumstances in which the power is exercised and his purpose or intention in exercising the power are important factors in determining the question whether the power has been abused. But

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72 *Australian Securities and Investments Commission v Australian Property Custodian Holdings Ltd (Receivers and Managers appointed) (In liq) (Controllers appointed) [No 3]* (2013) 31 ACLC ¶13-073 at 1172 [634].

73 *Lewski v Australian Securities and Investments Commission* (2016) 246 FCR 200 at 285 [302]. See also *Lewski v Australian Securities and Investments Commission [No 2]* (2017) 352 ALR 64 at 119-120 [159]-[160].

74 *R v Byrnes* (1995) 183 CLR 501 at 514-515; [1995] HCA 1; *Angas Law Services Pty Ltd (In liq) v Carabelas* (2005) 226 CLR 507 at 531 [65]; [2005] HCA 23. See also *Doyle v Australian Securities and Investments Commission* (2005) 227 CLR 18 at 28 [35]; [2005] HCA 78.

impropriety is not restricted to abuse of power. It may consist in the doing of an act which a director or officer knows or ought to know that he has no authority to do." (footnote omitted)

76 The same principles generally apply to the meaning of impropriety in s 601FD(1)(e). The primary judge correctly found that the Lodgement Resolution had the same improper purpose as the Amendment Resolution[75]. That purpose was to provide an advantage to APCHL. The advantage intended by the Listing Fee was to incentivise Mr Lewski to pursue listing. The advantage intended in relation to the Removal Fee and the increased Takeover Fee was to ensure that APCHL did not miss out on the Listing Fee by being removed before listing occurred. No reasonable person in each of the Directors' positions could have considered it proper to pass the Lodgement Resolution[76].

The Compliance Duties

77 The primary judge found[77] that each Director had contravened s 601FD(1)(f), by failing to take all steps that a reasonable person would take, if he or she was in the Director's position, to ensure that APCHL complied with the *Corporations Act* and the Constitution. The failures arose from: (i) passing the Lodgement Resolution, by which the Directors failed to ensure that APCHL complied with cl 25.1 of the Constitution and its duty under s 601FC(1)(m) to comply with the Constitution; and (ii) passing the Payment Resolutions, by which the Directors failed to ensure that APCHL complied with s 208 when making payments from scheme property that were not in accordance with the Constitution. The payments from scheme property were, themselves, also contraventions by APCHL of s 601FC(1)(k).

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75 *Australian Securities and Investments Commission v Australian Property Custodian Holdings Ltd (Receivers and Managers appointed) (In liq) (Controllers appointed) [No 3]* (2013) 31 ACLC ¶13-073 at 1170-1171 [629]-[630].

76 *Australian Securities and Investments Commission v Australian Property Custodian Holdings Ltd (Receivers and Managers appointed) (In liq) (Controllers appointed) [No 3]* (2013) 31 ACLC ¶13-073 at 1171-1172 [631]-[632].

77 *Australian Securities and Investments Commission v Australian Property Custodian Holdings Ltd (Receivers and Managers appointed) (In liq) (Controllers appointed) [No 3]* (2013) 31 ACLC ¶13-073 at 1173 [641], 1196 [766].

78 Although the Full Court did not give specific reasons for overturning the primary judge's conclusion that the Directors had contravened their Compliance Duties, the basis for the Full Court's conclusion must again have been the general premise that it was sufficient, in the circumstances, that the Directors had acted honestly in passing the Lodgement Resolution and the Payment Resolutions[78]. But, again, this does not address the objective duty in s 601FD(1)(f), which required each Director to take all steps that a reasonable person in his position would take. The unreasonableness of the vote in favour of the Lodgement Resolution has been addressed above. As for the Payment Resolutions and related acts, the relevant declarations of the primary judge[79] recorded that a reasonable person in the position of each Director would have obtained clear legal advice, a judicial direction, or member approval for the Listing Fee Payments. In the circumstances of the highly unusual and equivocal nature of the solicitors' legal advice, in addition to the circumstances of acceleration of the Listing Fee Payments, this conclusion was correct.

The third ground of appeal: the Directors' involvement in the contravention by APCHL of s 208

79 The Full Court allowed the Directors' appeals from the primary judge's finding[80] that they were involved, under s 209(2), in a contravention of s 208 by APCHL. That contravention concerned the payment of the Listing Fee by a cash payment from APCHL to itself, and then to a company associated with Mr Lewski, and by the issue of units to a company associated with Mr Lewski.

80 By s 79(c), a person will be involved in a contravention if the person "has been in any way, by act or omission, directly or indirectly, knowingly concerned in, or party to, the contravention". To satisfy this requirement of s 79 against each Director, ASIC needed to prove that the Director was intentionally involved in the contravention with knowledge of all of the essential elements of the contravention[81]. It was common ground that ASIC could not prove that the

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78 *Lewski v Australian Securities and Investments Commission* (2016) 246 FCR 200 at 285 [302], 296 [341].

79 Declarations 15, 23, 31, 39.

80 *Australian Securities and Investments Commission v Australian Property Custodian Holdings Ltd (Receivers and Managers appointed) (In liq) (Controllers appointed) [No 3]* (2013) 31 ACLC ¶13-073 at 1191 [734].

81 *Yorke v Lucas* (1985) 158 CLR 661 at 669-670; [1985] HCA 65.

Directors knew that the Constitution did not authorise the Listing Fee. The issue in dispute was whether, as the Full Court held, a lack of authorisation in the Constitution for the Listing Fee Payments was an essential element of the contravention of s 208. One reason the Full Court held that the Directors were not involved in APCHL's contravention of s 208 was that it had not been proved that the Directors knew that the Listing Fee was not authorised by the Constitution.

81 Section 208, as modified by s 601LC, is entitled "Need for member approval for financial benefit". Section 208(1) provides as follows:

> "If all the following conditions are satisfied in relation to a financial benefit:
>
> (a) the benefit is given by:
>
> (i) the responsible entity of a registered scheme; or
>
> (ii) an entity that the responsible entity controls; or
>
> (iii) an agent of, or person engaged by, the responsible entity
>
> (b) the benefit either:
>
> (i) is given out of the scheme property; or
>
> (ii) could endanger the scheme property
>
> (c) the benefit is given to:
>
> (i) the person or a related party; or
>
> (ii) another person referred to in paragraph (a) or a related party of that person;
>
> then, for the person referred to in paragraph (a) to give the benefit, either:
>
> (d) the person referred to in paragraph (a) must:
>
> (i) obtain the approval of the scheme's members in the way set out in sections 217 to 227; and
>
> (ii) give the benefit within 15 months after the approval; or

(e) the giving of the benefit must fall within an exception set out in sections 210 to 216."

82 Section 208(2) provides that member approval is "taken to have been given" if the giving of the benefit is required by a contract approved by the members and made within 15 months of that approval, or beforehand if the contract is conditional on that approval. Section 208(3) then provides:

> "Subsection (1) does not prevent the responsible entity from paying itself fees, and exercising rights to an indemnity, as provided for in the scheme's constitution under subsection 601GA(2)."

83 Although a matter falling within an exception referred to in s 208(1)(e) is a matter that must be pleaded and proved by the person seeking to rely upon it, each of the elements in s 208(1)(a) to (d) is a matter that must be pleaded and proved by the person alleging the contravention[82]. ASIC submitted that s 208(3) was, in effect, another exception to liability like s 208(1)(e) that must be pleaded and proved by the person seeking to rely upon it[83]. That submission should not be accepted. Properly interpreted, s 208(3) operates to define the scope of s 208(1)(d), noncompliance with which is a matter that must be proved by ASIC.

84 One important question concerning the scope of s 208(1)(d) is whether member approval of a contract also approves the giving of a financial benefit that is required by the contract. "Giving a financial benefit" is defined broadly and inclusively in s 229. That definition includes the financial benefit of entry into a contract (whether informal or otherwise): s 229(2)(b) provides that giving a financial benefit includes making an informal agreement, an oral agreement or an agreement that has no binding force.

85 If member approval were given to enter a contract, consistently with s 208(1)(d), and that approval did not extend to payments required under the contract, then separate member approval would be required to make each and every payment despite the obligations to make those payments having already been approved. Section 208(2) resolves this issue by providing that member approval of payments made under a contract is taken to have been given, but only for a 15-month period and only where the contract was not itself conditional upon member approval.

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82 *Waters v Mercedes Holdings Pty Ltd* (2012) 203 FCR 218 at 230 [38].

83 See *Chugg v Pacific Dunlop Ltd* (1990) 170 CLR 249 at 258; [1990] HCA 41.

86 A similar issue related to member approval under s 208(1)(d) is addressed by s 208(3). Section 208(3) is concerned with payments that are provided for in the scheme's constitution rather than payments required by an approved contract. The opening words, "[s]ubsection (1) does not prevent", indicate that the concern of sub-s (3) is with clarifying the scope of the required elements of s 208(1). And just as s 208(2) sets out the circumstances in which a benefit given under an approved contract is taken to have been approved by the members, s 208(3) sets out the circumstances in which a responsible entity's right in the constitution to be paid fees out of scheme property, or to be indemnified out of scheme property, is taken to be approved by the members. Those circumstances, from s 601GA(2), are that the right must be (i) specified in the scheme's constitution, and (ii) available only in relation to the proper performance of the responsible entity's duties.

87 For these reasons, s 208(3) is directed to the circumstances of member approval under s 208(1)(d), which ASIC must prove was not obtained in order to establish a contravention of s 208. Therefore, the Full Court was correct to conclude that[84], in order for ASIC to prove that the Directors were involved in the contravention of s 208 by APCHL, ASIC needed to prove that the Directors knew that the Constitution did not authorise the Listing Fee. It did not do so.

88 This ground of appeal should be dismissed.

Conclusion

89 The orders to be made on these appeals can conveniently be divided into (i) the orders concerning the primary judge's declarations and (ii) the orders concerning the pecuniary penalties and disqualifications imposed by the primary judge. In each category the orders are the same in each of the first four appeals. The exception is the fifth appeal, in relation to Mr Clarke, where ASIC did not seek to disturb the orders made by the Full Court.

90 As to the declarations, the effect of allowing the appeals on the first and second grounds of appeal, but dismissing the appeals on the third ground, is that in each appeal the global orders made by the Full Court should be quashed to the extent necessary to reinstate all declarations made by the primary judge other

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84 *Lewski v Australian Securities and Investments Commission* (2016) 246 FCR 200 at 291 [323].

than (i) those that were the subject of the appeal in relation to Mr Clarke[85], and (ii) those that related to the contraventions of s 209(2) that were the subject of the third ground of appeal[86]. In place of the orders of the Full Court concerning the declarations other than those specified above, orders should made dismissing the appeals from the primary judge.

91 As to the pecuniary penalties and disqualifications ordered by the primary judge, the effect of dismissing the appeals on the third ground is that part of the basis for the orders made by the primary judge against each Director is removed. Each matter should be remitted to the Full Court for determination of what, if any, effect this has on (i) the pecuniary penalties and disqualifications that the primary judge ordered against each Director other than Mr Clarke, and (ii) the orders as to costs. This issue can be determined together with ASIC's cross-appeals to the Full Court concerning the pecuniary penalties and disqualifications ordered by the primary judge.

92 The orders in each appeal (Matters No M79, M80, M81 and M82 of 2018) other than the appeal in relation to Mr Clarke (Matter No M83 of 2018), consistently with the approach of the primary judge and the Full Court of making global orders that apply in each proceeding, should therefore be:

1. Appeal allowed in part.

2. Set aside orders 2 to 6 of the orders of the Full Court of the Federal Court of Australia made on 1 November 2017 and in their place order that:

    (a) the appeal be allowed in part;

    (b) declarations 13, 21, 29, 37, 40, 41, 42, 43, 44, 45, 46, and 47 of the declarations and orders 1.1 to 1.4 and 2.1 to 2.5 of the orders made by the primary judge in proceeding VID 594 of 2012 ("Trial Proceeding") dated 2 December 2014 be set aside;

    (c) order 3 of the orders made in the Trial Proceeding be set aside and in its place order that the second to fifth defendants pay the plaintiff's (namely, ASIC's) costs of and incidental to the proceeding; and

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85 Declarations 40-47.

86 Declarations 13, 21, 29, 37, 45.

(d) the first respondent (namely, ASIC) pay the appellant's costs of and in connection with the dispute as to the form of orders.

3. Remit the matter to the Full Court of the Federal Court for determination of penalty and disqualification orders, costs, and the cross-appeal to that Court.

4. The first respondent pay the appellant's costs of the appeal to this Court.

93 The orders in the appeal in relation to Mr Clarke (Matter No M83 of 2018), which were not the subject of any dispute, should be made in the following terms:

1. Appeal allowed in part.

2. Set aside the orders of the Full Court of the Federal Court of Australia made on 1 November 2017 and in their place order that:

(a) the appeal be allowed in part;

(b) declarations 40 to 47 and order 2.5 of the orders made by the primary judge in proceeding VID 594 of 2012 ("Trial Proceeding") dated 2 December 2014 be set aside and in lieu thereof order that the plaintiff's claim in paragraphs 6 to 19 of its originating process dated 21 August 2012 in the Trial Proceeding in so far as it is made against the sixth defendant be dismissed; and

(c) the first respondent (namely, ASIC) pay the costs of the appellant (namely, Mr Clarke) in the Trial Proceeding and in the Full Court of the Federal Court, including reserved costs.

3. There be no order as to the costs of the appeal to this Court.