REGULATORY CHALLENGES IN ENFORCING SECURITIES LAW: THE *FYFFES* AND *FORTESCUE* CASES

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The early months of 2010 have not proved propitious for regulators but, contrary to commentary and criticism, there has been persistence in legal action against perceived 'corporate wrongdoers'. Two high profile pursuits, in Australia and Ireland, illustrate the cost in investigation and court time in proceeding with these actions in the public interest. The decisions in these instances rest partially on judicial evaluation of the price sensitivity of corporate information and the legal interpretation of the 'materiality' test in both codes. Discussion was also focused on the supportive role of legal oversight and advice, and whether corporate intent and the honesty of directors measured up to the standards required by law.

I. INTRODUCTION

This paper discusses three important issues relating to securities law in the context of both the above cases; one resulting from a prominent Irish[1] case and the other a contentious decision in the Australian courts.[2] The issues emerge from similarities between the two cases. Each case illustrates the difficulty in enforcing regulation that is dependent on definitions, particularly those of 'price sensitivity' or the 'material effect' of specific information on a company's share price.

The ongoing debate concerning the judicial interpretation of 'materiality' in this context contributes to the considerable risk for a regulator in undertaking an action for breach of either the insider trading or continuous disclosure provisions. In Australia, each of these provisions relies on a complex analysis of the likely 'material effect'[3] from the point of view of a 'reasonable investor'. However, the Irish Supreme Court decision endorses the advantage of applying a straightforward 'material effect' test. A further two issues arise in both the cases discussed in this paper: the relevant decision taken by the company's director regarding the corporate information is based on 'legal advice'; and, is thereby construed as an action taken 'reasonably and honestly'.

In 2006 in the Federal Court in Perth, the Australian Securities and Investments Commission (ASIC) sought civil penalties[4] against Fortescue Metals Group Limited (FMG), a listed mining company, and for the first time against an individual, the chief executive, for being knowingly involved[5] in the company's continuous disclosure contravention. These proceedings were dismissed by the Federal Court in December 2009. The court found that FMG had a genuine and reasonable basis for the opinion that underpinned its disclosures, and this was reasonably and honestly held by the company's board and chief executive. ASIC, after assessing these

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1 *Fyffes plc v DCC plc* [2007] IESC 36.

2 *Australian Securities & Investments Commission v Fortescue Metals Group Ltd [No 5]* [2009] FCA 1586 (Unreported, 23 December 2009) [904] (*'Fortescue Metals Group*').

3 *Corporations Act 2001* (Cth) s 677 and s 1042D.

4 *Corporations Act 2001* (Cth) s 674(2), note 2: this subsection is also a civil penalty provision (see s 1317E(1)(ja)).

5 *Corporations Act 2001* (Cth) s 674(2A) (Contravention by an individual) — a person who is involved in a listed disclosing entity's contravention of s 674(2) contravenes this subsection; note 2: s 79 defines 'involved'. Pursuant to section 79 of the *Corporations Act 2001* (Cth) a person is involved in a contravention if, and only if, the person: (a) has aided, abetted, counselled or procured the contravention; or (b) has induced, whether by threats or promises or otherwise, the contravention; or (c) has been in any way, by act or omission, directly or indirectly, knowingly concerned in, or party to, the contravention; or (d) has conspired with others to effect the contravention.

findings of Gilmour J,[6] filed a notice of appeal on 4 February 2010. Among other issues, ASIC believes that the findings 'warrant review by an appeal court' as they raise important questions 'as to the proper interpretation and application of provisions of the *Corporations Act 2001* that govern company announcements such as…the continuous disclosure provisions'.[7]

Just over two weeks prior to this notice of appeal by the Australian regulator, the corporate regulator in Ireland also received a setback. This other high profile case had been running in the Irish courts for a decade and concerned the sale of shares in Fyffes plc by a former director who at the time was in possession of confidential board information. In the most recent development, the Irish High Court released the Report of its Inspector[8] on 19 January 2010 (the investigation by an inspector had been requested in the 'public interest'[9] by the Director of Corporate Enforcement, the Irish equivalent of ASIC).

II. THE *FYFFES CASES*

A. *'Material Effect': Irish High Court Decision*[10]

Fyffes plc ('Fyffes'), the issuer of the securities, and DCC plc ('DCC') were listed on the Irish Stock Exchange and also the London Stock Exchange. Fyffes alleged that one of its non-executive directors, James Flavin, who later resigned from the board of the company, had dealt in Fyffes' shares in advance of a profit correction being announced by Fyffes to the Stock Exchanges. This sale of more than 31 million Fyffes' shares in February 2000 was potentially an unlawful insider dealing within the meaning of Part V of the *Companies Act 1990* (IE).

The transactions were investigated by the stock exchanges but neither the Director of Public Prosecutions in Ireland nor the corporate regulator took action at this time. As a result, a civil liability action was taken by Fyffes against one of its own directors, James Flavin, and the company he had founded, DCC. The decision at first instance in the High Court rested on the judicial interpretation of price sensitivity of the information and whether the defendant knew that the information could have a material effect on the price of Fyffes' shares at the time of the transaction. The specific information contained in the reports to the board was not generally available, so it was the materiality or price sensitivity of the information that was contentious.[11]

Applying the 'reasonable investor'[12] test in the 2005 Irish High Court decision, [13] Laffoy J found that the relevant information had no material effect as it was not 'price sensitive'[14] and therefore could not provide the basis of a claim for insider trading. In her decision, Laffoy J

6 *Fortescue Metals Group* [2009] FCA 1586 (Unreported, 23 December 2009) [904].

7 Australian Securities & Investments Commission, 'ASIC Appeals Federal Court Decision in Fortescue Metals Group Civil Penalty Proceedings' (Press Release, 4 February 2010) 10–13AD.

8 *Report of the Inspector into the Affairs of DCC plc, S&L Investments Limited and Lotus Green Limited Pursuant to Section 8 of the Irish Companies Act 1990*, 21 December 2009 (Bill Shipsey). Hereafter referred to as the 'Report of the Inspector'. This Report is discussed in greater detail in: Josephine Coffey, 'Insider Trading in Ireland — Implications of the Fyffes Case for Company Directors' (Paper presented at the European Applied Business Research Conference, Dublin, 7–10 June 2010).

9 Report of the Inspector, above n 8, [12.1.4] — in July 2008, Kelly J gave judgment in which he agreed with the Director that the appointment of an Inspector was in the 'public interest and was not disproportionate'..

10 *Fyffes plc v DCC plc* [2005] IEHC 477.

11 Ibid 228–9.

12 The corresponding test in the Australian legislation is: *Corporations Act 2001* (Cth) s 1042D:

> When a Reasonable Person would take Information to have a Material Effect on Price or Value of Division 3 Financial Products
>
> For the purpose of this Division, a reasonable person would be taken to expect information to have a material effect on the price or value of particular Division 3 financial products if (and only if) the information would, or would be likely to, influence persons who commonly acquire Division 3 financial products in deciding whether or not to acquire or dispose of the first-mentioned financial products.

13 *Fyffes plc v DCC plc* [2005] IEHC 477. This earlier Irish High Court decision by Laffoy J is discussed in: Josephine Coffey, 'A Civil Liability Action for Insider Trading: Fyffes plc v DCC plc [2005] IEHC 477' (Paper presented at the 61st Annual ALTA Conference, Victoria University, Melbourne, 4–7 July 2006) 1–14.

14 The meaning of 'price sensitive' in this context is taken to equate to the materiality of the information or its 'material effect' on the price or value of the relevant securities.

pointed out that there was very little guidance in the statute as to how the price sensitivity test in section 108(1) of the Irish *Companies Act 1990* (IE)[15] should be applied and, as this was the first claim for civil remedies, there was no authority within the jurisdiction to assist the Court.[16]

Laffoy J handed down her decision on 21 December 2005 in which Fyffes failed in its petition for €106 million compensation for the alleged insider dealing by Flavin and DCC. Laffoy J concluded that the defendant was not in possession of price sensitive information at the date of the share sales. It followed that the Fyffes share transactions by Flavin in February 2000 were not unlawful under section 108 of the *Companies Act 1990* (IE) and no civil liability arose under secton 109.[17] Fyffes announced on 8 April 2006 that it would appeal against this single finding of the decision to the superior court, the Irish Supreme Court.

B. *Material Effect': Irish Supreme Court Appeal Decision*[18]

In 2007, Fyffes succeeded as all five justices of Ireland's highest court unanimously allowed the appeal against Flavin and DCC.[19] Damages, considerably less than the compensation claimed at first instance, were awarded to Fyffes, costing DCC over €42 million in costs and compensation. The Supreme Court had deemed that the 'reasonable investor' test was inappropriate and, in the words of Fennelly J, '[Laffoy J] should have adopted a straightforward test of market effect'.[20] The High Court had erred in using this test and the 'reasonable investor' concept was of no assistance as 'it was derived from the jurisprudence of the United States and was developed in relation to a quite different statutory regime with differently worded provisions'.[21]

Denham J in the Supreme Court had abandoned the 'reasonable investor'[22] test for insider trading as it was construed by Laffoy J in the High Court. He reasoned that it was more appropriate to apply a retrospective (*ex post*) test of materiality by viewing the impact of the information on the share price of the relevant securities once the information had been made available to the market.[23]

The real issue was the effect of the information on the share price in the market and Laffoy J in the High Court had 'failed to pay any regard whatsoever to the actual impact upon Fyffes' share price when the information in the possession of Mr Flavin on the dates on which he dealt … was ultimately released to the market'.[24] The earlier High Court decision had rejected the post-disclosure events as having no evidential value and had relied on the opinion of experts. However, the Supreme Court conceded that:

> while expert evidence is of value, where, as here, there are serious conflicts in the same, the court may have to rely on common sense. In this regard post-disclosure market events, properly evaluated, constitute objective evidence.[25]

15 *Fyffes plc v DCC plc* [2005] IEHC 477, 22–3, 30–1. Section 108 of the *Irish Companies Act 1990* (IE) declares that:

> It shall not be lawful for a person who is, or at any time in the preceding 6 months has been, connected with the company to deal in any securities of that company if by reason of his so being, or having been, connected with that company he is in possession of information that is not generally available, but, if it were, would be likely materially to affect the price of those securities.

16 *Fyffes plc v DCC plc* [2005] IEHC 477, 206.

17 Ibid 366–7.

18 *Fyffes plc v DCC plc* [2007] IESC 36.

19 Ibid 88. This decision is discussed in greater detail in: Josephine Coffey, 'The Reasonable Investor Test Across Two Continents' (2008) 1(1–2) *Journal of the Australasian Law Teachers Association* 45–53.

20 Report of the Inspector, above n 8, [11.3.5].

21 *Fyffes plc v DCC plc* [2007] IESC 36, 88.

22 Ibid 22. *TSC Industries Inc v Northway Inc* 426 US 438–49 (1976) is US authority for a judicial test where materiality was held to be a function of the size of the effect that an event has on a company. Marshall J, in delivering the opinion of the US Supreme Court, stated that there must be 'a substantial likelihood that the omitted fact would have been viewed by the reasonable investor as having significantly altered the "total mix" of information made available'.

23 *Fyffes plc v DCC plc* [2007] IESC 36, 7(iii).

24 Ibid 88.

25 Ibid .

This was the basis of an *ex post* simplified 'material effect' test as set out in section 108(1) of the *Companies Act 1990* (IE). Denham J concluded:

> There was information. It was not generally available. It was bad news, it was information of a risk, it would concern the market. It was information likely to affect the price of the shares on the market.[26] For all these reasons I am satisfied that the information was price sensitive. This finding determines the appeal. For the reasons given I would allow the appeal.[27]

C. *Report of the Irish High Court Inspector*[28]

It had already been determined by the Supreme Court on appeal that Flavin and DCC had breached the insider dealing provisions. However, the Director of Corporate Enforcement[29] remained concerned that others, in addition to Flavin, may have facilitated the share transactions and could have been implicated in the 'insider dealing'.[30] The role of the Director was to ensure the highest standards of corporate compliance in Ireland: 'He is both a corporate "policeman", ensuring compliance with the requirements of the Companies Acts, and the enforcer of good corporate behaviour and governance'.[31] The Director's authority included the power to apply to the High Court for the appointment of an Inspector to investigate issues in the 'public interest'.[32]

On 19 January 2010 the Irish High Court released the report of its Inspector, as requested by the Director of Corporate Enforcement. The Inspector noted that 'at the root of the application to appoint Inspectors lay a suggestion that DCC and its officers and directors did not take their compliance obligations seriously'.[33] The Inspector's approach was more lenient. Although the Supreme Court held that Flavin had been in possession of price sensitive information at the time of dealing, the Inspector believed that Flavin's was an error of appreciation and judgment: judgment as to what the Supreme Court would find as a matter of law to constitute 'price sensitive' information. Flavin's conclusion that he was not in possession of price sensitive information had a rational, if legally wrong, basis.[34]

1. *'Honesty and Integrity'*

The Inspector also agreed with the findings of Laffoy J in the earlier High Court decision that there was no evidence of dishonesty on the part of Flavin or DCC: 'I did not understand the Plaintiff to assert dishonesty on the part of any of the Defendants. In any event, I find that dishonesty was not established on the Evidence.'[35]

The Inspector concluded that '... on the basis of all the evidence which I have heard from all of the witnesses and from Mr Flavin himself, that there was no deliberate wrongdoing or dishonesty on his part'.[36]

In spite of the Supreme Court decision, the Inspector supported the earlier findings of Laffoy J in the High Court that although Flavin was in possession of the confidential information at the time, he had not used or relied on the Fyffes trading 'information in dealing and, further, that the information did not in any way motivate the share sales are findings which I believe have been surprisingly overlooked'.[37] These were considered important findings with regard to the reputation of Flavin and DCC and the investigation into the Fyffes share sales were said to

26 Ibid 31.
27 Ibid 32.
28 Report of the Inspector, above n 8.
29 Director of Corporate Enforcement, Paul Appleby.
30 Report of the Inspector, above n 8, [11.3.1]–[11.3.3].
31 Ibid [12.1.1].
32 Ibid [12.1.4].
33 Ibid [12.1.5].
34 Ibid [11.3.87]–[11.3.88].
35 *Fyffes plc v DCC plc* [2005] IEHC 477, 243. Report of the Inspector, above n 8, [11.3.13], [11.3.56].
36 Report of the Inspector, above n 8, [11.3.86].
37 Ibid [11.3.90].

'reflect the honesty and integrity' of all the DCC officers and directors interviewed during the investigation.[38]

2. *'Rational, if Legally Wrong'*

The Inspector was satisfied that Flavin had maintained the confidentiality of the Fyffes reports and only communicated the trading information in discussions with the compliance officer and the company solicitor.[39] The Inspector considered it was to Flavin's credit that he sought legal advice when it was appropriate and 'followed such advice when it was offered'.[40] Unfortunately, Flavin's conclusion that 'he was not in possession of price sensitive information had a rational, if legally wrong, basis'.[41]

This third chapter in the *Fyffes* saga appears to have reached a conclusion when the Director of Corporate Enforcement admitted that the inquiries were 'at the end of the road'.[42] The Director acknowledged the Inspector's findings that DCC directors had followed advice from a 'trusted' legal adviser to the company:

> If, as the Inspector has found, the directors were quite entitled to do that — even if the legal advice was wrong — there is very little I can do. There's no way that any court would sanction a director for having followed the company's legal advice. This is at an end, really, at this stage.[43]

Will a similar obituary apply to the *Fortescue* case in Australia?

III. THE *FORTESCUE CASE*

A. *Australian Securities & Investments Commission v Fortescue Metals Group Ltd [No 5] [2009] FCA 1586*

On 2 March 2006 in the Federal Court in Perth, ASIC initiated proceedings seeking civil penalty[44] orders of up to $3 million against Fortescue Metals Group Limited ('FMG'), a mining company listed on the Australian Securities Exchange ('ASX'). In an unprecedented action, the regulator also sought penalties of up to $600,000 against Andrew Forrest, the chief executive, for being knowingly involved[45] in the company's continuous disclosure contravention.[46] Following a referral from the ASX, the regulator commenced its investigation in May 2005. ASIC alleged that Andrew Forrest had failed to ensure that FMG complied with its disclosure obligations, which would have prevented misleading and deceptive conduct regarding various contracts with Chinese parties. The continuous disclosure obligations were said to have been breached on 23 August and 5 November 2004.

38 Ibid [11.3.90].
39 Ibid [12.1.15].
40 Ibid [12.1.6].
41 Ibid [11.3.87]–[11.3.88].
42 Colm Keena and Paul Cullen, 'Flavin Deal an "Error in Judgment", Fyffes Inquiry Concludes', *The Irish Times* (Dublin), 20 January 2010.
43 Paul Cullen, 'Inquiry at "End of the Road", says Appleby', *The Irish Times* (Dublin), 20 January 2010.
44 Civil penalties are available for contravention of the amended continuous disclosure provision, *Corporations Act 2001* (Cth) s 674(2) Note 2: this subsection is also a civil penalty provision (see s 1317E of *Corporations Act 2001* (Cth)). For relief from liability to a civil penalty relating to this subsection, see s 1317S. Section 674(2) of the*Corporations Act 2001* (Cth) is a civil penalty provision under the extended s 1317E(1)(ja). Civil penalties and compensation provide an alternative to criminal liability and Schedule 3 penalties. Section 1317E of the *Corporations Act 2001* (Cth) was amended effective 11 March 2002.
45 *Corporations Act 2001* (Cth) s 674(2A) Contravention by an individual — A person who is involved in a listed disclosing entity's contravention of s 674(2) contravenes this subsection; Note 2: s 79 defines involved — A person is involved in a contravention if, and only if, the person: (a) has aided, abetted, counselled or procured the contravention; or (b) has induced, whether by threats or promises or otherwise, the contravention; or (c) has been in any way, by act or omission, directly or indirectly, knowingly concerned in, or party to, the contravention; or (d) has conspired with others to effect the contravention.
46 Australian Securities & Investments Commission, 'ASIC Commences Proceeding Against Fortescue Metals Group and Andrew Forrest' (Press Release, 2 March 2006).

ASIC filed a new statement of claim against FMG on 27 April 2006 to include reference to an ASX announcement of 8 November 2004.[47] As with the Director of Corporate Enforcement in his application to the Irish High Court,[48] ASIC believed that this action was in the 'public interest' as 'keeping markets properly informed underpins confidence in the integrity of our markets and in doing so, it assists in keeping the cost of capital low which is important as our companies recapitalise'.[49]

Proceedings commenced on 6 April 2009 before Gilmour J and were dismissed by the Federal Court on 23 December 2009. It was found that neither Andrew Forrest nor FMG had engaged in misleading and deceptive conduct or failed to comply with continuous disclosure obligations.[50]

The primary issue before the court was the company's obligation to disclose information to ASX under section 674 Chapter 6CA *Corporations Act 2001* (Cth) concerning the feasibility study of a mining project and the legal effect of related agreements. Other issues that occupied the court's attention, as had also been the case with *Fyffes*,[51] were whether an *ex ante* or *ex post* inquiry was the correct approach for the materiality test. In addition, the court deliberated whether FMG had received legal advice concerning the effect on the share market of its agreements and disclosure obligations.[52]

B. *Issue of Materiality*

Although the court found that relevant information was not of the kind that FMG ought to have been aware and therefore the company did not contravene section 674(2) of the *Corporations Act 2001* (Cth), Gilmore J still discussed the issue of the materiality[53] with an analysis of sections 674(2)(c)(ii) and 677.[54]

Gilmore J agreed with the submissions of both ASIC and FMG that the above provisions and ASX listing rule 3.1 required 'the issue of materiality to be determined on an *ex ante* basis, that is a forward, not backward, looking exercise',[55] with notification to ASX of information that a reasonable person would expect, if it were generally available, to have a material effect on the price or value of FMG's shares. However, the contrary interpretation was also accepted, 'that evidence of the actual effect of the information actually disclosed on FMG's share price may be relevant to assist the Court in its determination of whether s 674(2) has been contravened'.[56] This approach, identical to the one adopted by the Irish Supreme Court in the *Fyffes* appeal case,[57] would involve an *ex post* test of the effect of the information once it was released to the market and could provide a 'relevant cross-check as to the reasonableness of an *ex ante* judgment about a different hypothetical disclosure'.[58]

47 Australian Securities & Investments Commission, 'ASIC Files New Statement of Claim Against Fortescue Metals' (Press Release, 27 April 2006).

48 See above n 28.

49 Australian Securities & Investments Commission, 'ASIC Takes Action Against Fortescue Metals and CEO Andrew Forrest' (Press Release, 3 April 2009).

50 Australian Securities & Investments Commission, 'ASIC's Proceedings Against Fortescue Metals Group Ltd and Andrew Forrest Dismissed' (Press Release, 23 December 2009); *Fortescue Metals Group* [2009] FCA 1586 (Unreported, 23 December 2009) 904.

51 See above n 20.

52 The Irish High Court appointed Inspector had considered it highly relevant to his investigation of the Fyffes' share sales that Flavin had sought legal advice and had 'followed such advise when it was offered'. See above n 37.

53 *Fortescue Metals Group* [2009] FCA 1586 (Unreported, 23 December 2009) 472–3.

54 *Corporations Act 2001* (Cth) s 677 (see also sections 674 and 675) — Material Effect on Price or Value: For the purposes of sections 674 and 675, a reasonable person would be taken to expect information to have a material effect on the price or value of ED securities of a disclosing entity if the information would, or would be likely to, influence persons who commonly invest in securities in deciding whether to acquire or dispose of the ED securities.

55 *Fortescue Metals Group* [2009] FCA 1586 (Unreported, 23 December 2009) 474.

56 Ibid 477.

57 See above n 20.

58 Ibid 477.

1. *Macdonald Case*

Gilmore J made reference to *Australian Securities & Investments Commission v Macdonald (No 11)* (2009) 256 ALR 199, 1067, citing Gzell J '[w]here likelihood of the occurrence of an event is in issue and relevant facts are available, they are to be preferred to prophecies'.[59] Gilmore J distinguished the market sentiment in the *Macdonald* case, as opposite to the situation in the *Fortescue* case where the market held a positive view of FMG, but following the November notification the mood became negative. Gilmore J also noted that Gzell J had found in *Macdonald* that the contraventions had been made out 'without analysis of quantitative or statistical information'.[60] Gzell J also did not apply the statutory 'reasonable investor' test from section 677 of the *Corporations Act 2001* (Cth) and its former equivalent section 1001D. Instead, Gzell J referred to the direct question under sections 674(2) and 1001A(2) of the *Corporations Act 2001* (Cth), whether a reasonable person would expect the information, if it were generally available, to have a 'material effect' on the price or value of the shares. Gilmore J supposed that in the *Macdonald* case

> it would appear that the question under ss 677 and 1001D, namely, whether the information would have had the relevant influence on investors, would have been answered affirmatively by Gzell J on the basis that … the reduction and severing of the company's possible connection to asbestos claims was likely to reduce negative sentiment.[61]

2. *Jubilee Mines*

Such an inquiry was also considered in *Jubilee Mines NL v Riley* (2009) 253 ALR 673, 33–4 where Martin CJ in the Court of Appeal of the Supreme Court of Western Australia upheld the appeal of the company and set aside the lower court judgment of Master Sanderson. Master Sanderson, at first instance, had observed the 'material effect' on the company's share price, following an announcement made in June 1996, and acknowledged the US Supreme Court decision *TSC Industries Inc v Northway Inc* [1976] USSC 119; (1976) 426 US 438.[62] Master Sanderson adopted

> that formulation. Applying that test, I am satisfied that a reasonable person would expect the information to have a material effect. This was good news… it can be seen that the expectations of the reasonable person were proved right.[63]

On appeal, Martin CJ was unimpressed by this application of the test from the US Supreme Court. These sentiments are similar to those of the Irish Supreme Court in 2007 when it overturned the High Court decision and dismissed the 'reasonable investor' concept as being of no assistance.[64] Martin CJ stated that:

> in the result, nothing appears to turn on this, these paragraphs reflect an erroneous approach to the construction of the Corporations Law… Further, the 'material effect' referred to in s 1001A and s 1001D is the effect on price, whereas the materiality referred to in the case cited by the Master is the materiality of information'.[65]

59 *Australian Securities & Investments Commission v Macdonald (No 11)* (2009) 256 ALR 199, 1067.

60 *Fortescue Metals Group* [2009] FCA 1586 (Unreported, 23 December 2009) 555–6.

61 Ibid 556.

62 The Court said: 'There must be a substantial likelihood that the omitted fact would have been viewed by the reasonable investor as having significantly altered the total mix of information available.'

63 *Kim Riley in his capacity as Trustee of the Ker Trust v Jubilee Mines NL* [2006] WASC 199 (Unreported, 6 September 2006) 290. On 6 September 2006, Master Sanderson in the Supreme Court of Western Australia awarded damages of $1.856 million to a private plaintiff for the negligent failure by Jubilee Mines NL to notify ASX of certain material information required under the old listing rule 3A. The action arose under the original s 1001A(2) and was only a matter of weeks after the provision became effective on 5 September 1994. The former s 1005 provided damages for a person who suffered a financial loss from a contravention of Pt 7.11 of the Corporations Law if the action was commenced within six years of this contravention. The company successfully appealed the decision.

64 See Finnegan J above n 18, 19.

65 *Jubilee Mines NL v Riley* (2009) 253 ALR 673, 34. (*TSC Industries Inc v Northway Inc* [1976] USSC 119; (1976) 426 US 438 is the 'case cited').

Martin CJ concluded that the Jubilee Mines information as a whole was not information that was likely to have influenced persons who commonly invest in securities.[66] Master Sanderson 'should have concluded that, when all relevant information was taken into account, Jubilee was under no obligation to make disclosure'.[67] McLure J A and Le Miere AJA agreed with the Chief Justice.

3. *Expert Evidence*

Returning to the *Fortescue* case, given that the market was aware of conditional nature of the project, Gilmore J did not consider that information concerning FMG's agreements would be likely to influence investors to acquire these securities. However, there was detailed deliberation of the 'materiality' evidence given by the three experts called by ASIC. Although the evidence 'traversed an *ex ante* approach and an *ex post,* statistically based, approach' in considerable detail, the court did not find it particularly helpful.[68]

In the *Fyffes* 2005 Irish High Court decision, Laffoy J had utilised the opinions of a number of experts in formulating a 'reasonable investor' test to establish the materiality of the confidential information. However, on appeal the Supreme Court, similar to Gilmore J in *Fortescue*, was circumspect concerning the value of expert evidence.[69]

C. *Legal Advice*

One aspect of ASIC's submission was that 'the failure by FMG to obtain legal advice is a relevant consideration'.[70] The regulator argued that if such advice had been obtained, then a responsible company or board of directors could not have made misleading statements. To support this contention, ASIC referred to Gzell J's findings in *Macdonald* that the regulator had successfully made out its case. In that case, the company, James Hardie Industries Limited, was found to have negligently failed to disclose information:

> in that it did not obtain any legal advice as to whether it should disclose the DOCI Information and in that neither the board nor management of JHIL considered disclosure of the DOCI Information.[71]

In the *Fortescue* case, Gilmore J was unconvinced by this argument and accepted that Peter Huston, 'as a qualified, experienced and practicing commercial solicitor' had 'joined the company as in-house counsel shortly before 3 October 2004 although he had acted as FMG's solicitor on a private basis before that'.[72] Emails confirmed that the chief executive, Andrew Forrest, on behalf of FMG:

> was relying on Huston in his capacity as a lawyer to oversee and ensure that agreements entered into by FMG were legally enforceable. They also confirm that Huston in performing that role had given advice (instructions) to FMG to that end in relation to some contracts. It is not clear that Forrest was speaking here of the framework agreements, although they may well have been included. [73]

On this issue Gilmore J concluded that according to the email referred to above, Huston had been employed by FMG principally to ensure its agreements were legally enforceable.[74] The evidence demonstrated, 'contrary to ASIC's assertion, Huston did give legal advice to FMG as to the legal enforceability of the framework agreements'.[75]

66 *Jubilee Mines NL v Riley* (2009) 253 ALR 673, 86.
67 Ibid 125–36.
68 *Fortescue Metals Group* [2009] FCA 1586, (Unreported, 23 December 2009) 494, 626–8.
69 See Denham J, above n 22. In contrast to Gilmore J's decision in *Fortescue Metals Group* [2009] FCA 1586, (Unreported, 23 December 2009), the Irish Supreme court regarded post-disclosure market events, when properly evaluated, constituted the most objective evidence.
70 Ibid 363.
71 *Australian Securities & Investments Commission v Macdonald (No 11)* (2009) 256 ALR 199, [1275].
72 *Fortescue Metals Group* [2009] FCA 1586 (Unreported, 23 December 2009) 364–6.
73 Ibid 373.
74 Ibid 380–1.
75 Ibid 391.

Reliance on legal counsel, even if this advice was later shown to be limited or inappropriate, emerged as a defining argument in defence of the FMG management in *Fortescue.* As previously discussed, the Irish High Court Inspector highlighted reliance on legal advice as an attribute to the credit of James Flavin in the Fyffes' share sales.[76]

D. *Honestly and Reasonably*

'Was the opinion of FMG and Forrest honestly and reasonably held?'[77] This was the question posed by Gilmore J and answered in the affirmative. The opinions of Forrest and FMG that the agreements were legally binding were reasonably and honestly held.[78] The honesty of the company was dependent on that of its chief executive and the members of its board. Gilmore J considered that ASIC had failed to show that there was a reasonable basis to contend dishonesty.[79]

The court employed the definition of 'aware' in ASX listing rule 19.12 to decide that FMG was not aware of the information and was under no obligation to disclose it to the ASX. FMG did not have information at the relevant times and the disclosures to the market operator in August and November 2004 were sufficient to satisfy the listing rules. ASIC's case under section 674(2) of the *Corporations Act 2001* (Cth) failed for this reason.[80] It followed, as a consequence of Gilmore J's findings, that if FMG did not contravene:

> then Forrest could not have been a person who was involved in a contravention … [and] at all material times, he believed, on reasonable grounds, and took all necessary steps to ensure, that FMG was complying with its obligations under s 674(2) of the Act.[81]

Gilmore J, in conclusion, reiterated these findings:

> I have already concluded that FMG by its directors including Forrest was not 'aware' of the legal effect of the framework agreements propounded by ASIC. I have also found that FMG's opinion which underpinned its disclosures as to the legal effect of the framework agreements was reasonably and honestly held by it through its board including Forrest.[82]

IV. Conclusion

Following this decision of Gilmour J in the Federal Court, ASIC filed a notice of appeal on 4 February 2010 in respect of the dismissal of its application for civil penalty orders. Among other issues, ASIC believed that the findings of Gilmore J warranted review by an appeal court since the decision raised important questions 'as to the proper interpretation and application of provisions of the *Corporations Act 2001* that govern company announcements such as the … the continuous disclosure provisions'.[83]

To proceed with an appeal against the decision is a hazard to be considered carefully by ASIC, as Gilmore J stated: 'I am well satisfied that Forrest acted reasonably to ensure that FMG both complied with s 674 of the Act and did not contravene s 1041H of the Act. He did not breach s 180(1) of the Act as alleged by ASIC.'[84]

76 See above n 36–38.
77 *Fortescue Metals Group* [2009] FCA 1586 (Unreported, 23 December 2009) 353.
78 Ibid 71.
79 Ibid 353, 394.
80 Ibid 466–7.
81 Ibid 468.
82 Ibid 903.
83 Australian Securities & Investments Commission, 'ASIC Appeals Federal Court Decision in Fortescue Metals Group Civil Penalty Proceedings', above n 7.
84 *Fortescue Metals Group* [2009] FCA 1586 (Unreported, 23 December 2009) 903–4.

Further action taken in the 'public interest' was considered unwarranted following the regulator's failure to obtain a penalty in either the *Rich*[85] or *Citicorp*[86] cases. In the former case, ASIC initially lodged a notice of intention to appeal in the NSW Court of Appeal. This related to the dismissal on the 18 November 2009 in the NSW Supreme Court of ASIC's civil penalty proceedings against One.Tel's former joint managing director, Jodee Rich and the finance director, Mark Silbermann.[87] The NSW Supreme Court made orders on 5 February 2010 as to ASIC's legal costs in the One.Tel proceedings.[88] The court ordered ASIC to make payments towards the defendant's legal costs and interest as ASIC had reconsidered and '[p]ublic interest considerations, cost and effluxion of time were key factors in deciding not to appeal'.[89]

In spite of the cost of these setbacks, the Chairman of ASIC has pointed out that the regulator has listened and responded to these events. For example:

> Major litigation we have reviewed our approach to major litigation and made changes (as part of the strategic review). These include improving the way we run cases and explaining their strategic importance (win or lose) to the market.[90]

Regarding the result of the *Fortescue* litigation, one commentator has stated that '… there is simply no way ASIC can leave the decision unchallenged. The first step will be a court challenge, and if that fails it will try to change the law'.[91]

In anticipation that the ASIC appeal against the *Fortescue* will proceed, it is hoped that the court will achieve the 'proper interpretation'[92] of the provisions desired by the regulator, in particular section 677 of the *Corporations Act 2001* (Cth) and 'material effect'. If a court challenge is unsuccessful, then, as suggested above by the commentator, in what way could ASIC 'try to change the law'? One suggestion would be a clarification of the test to determine 'price sensitive' information. As the common law 'reasonable investor' test, adapted from TSC Industries Inc v Northway Inc,[93] has been found by both the West Australian Federal Court (in *Fortescue*) and the Irish Supreme Court (in *Fyffes* case) to be of no assistance, then the choice is narrowed to the statutory 'reasonable investor' test found in the Australian statute.[94] This test offers the options of *ex ante*, as adopted by Gilmore J, or on occasion the *ex post* interpretation of the materiality of the information. Hence, as discussed previously, the confusion that arose in both cases between relying on the opinions of experts as to the likely 'material effect' of the information if it is made public, or evaluating the effect on the share price after the information

85 *Australian Securities & Investments Commission v Rich* 236 FLR 1 (*'Rich*'). In 2001, ASIC had commenced proceedings against One.Tel's directors based on the duties and obligations of officers to disclose a company's financial position to the board and the market.

86 *Australian Securities & Investments Commission v Citigroup Global Markets Australia Pty Limited* [2007] FCA 963 (Unreported, 28 June 2007) ('*Citigroup*') was an unsuccessful civil penalty action against a corporate entity.

87 Australian Securities & Investments Commission, 'ASIC Lodges Notice of Intention to Appeal' (Press Release, 17 December 2009).

88 Australian Securities & Investments Commission, 'NSW Supreme Court Makes One.Tel Civil Penalty Cost Orders by Consent' (Press Release, 5 February 2010).

89 Australian Securities & Investments Commission, 'ASIC Not to Appeal One.Tel Decision' (Press Release, 26 February 2010).

90 Tony D'Aloisio, 'Implications of a Fast Changing Regulatory Landscape' (Speech delivered at the Australia – Israel Chamber of Commerce, Brisbane, 21 July 2010) 70.

91 John Durie, 'ASIC Prepares for Battle over Disclosure Power', *The Australian* (Sydney), 6 January 2010.

92 Australian Securities & Investments Commission, 'ASIC Appeals Federal Court Decision in Fortescue Metals Group Civil Penalty Proceedings', above n 7.

93 426 US 438–49 (1976).

94 *Corporations Act 2001* (Cth) s 677 (see also sections 674 and 675) — Material Effect on Price or Value: For the purposes of sections 674 and 675 of the *Corporations Act 2001* (Cth), a reasonable person would be taken to expect information to have a material effect on the price or value of ED securities of a disclosing entity if the information would, or would be likely to, influence persons who commonly invest in securities in deciding whether to acquire or dispose of the ED securities. Also, at s 1042D of the *Corporations Act 2001* (Cth) — When a Reasonable Person would take Information to have a Material Effect on Price or Value of Division 3 Financial Products: For the purpose of this Division, a reasonable person would be taken to expect information to have a material effect on the price or value of particular Division 3 financial products if (and only if) the information would, or would be likely to, influence persons who commonly acquire Division 3 financial products in deciding whether or not to acquire or dispose of the first-mentioned financial products.

95 *Fyffes plc v DCC plc* [2007] IESC 36, 88.

was made public. The alterative is to circumvent even a statutory 'reasonable investor' test by applying a simplified *ex post* 'material effect' construal as adopted in the *Fyffes* appeal case.[95]

Regulators in both jurisdictions also require clarification from the courts on the related issues; the circumstances in which company directors can be considered to be acting 'reasonably and honestly' when relying on 'legal advice' concerning the likely 'material effect' of confidential corporate information. These are important issues that ASIC rightly believes 'warrant review by an appeal court'. For the Irish regulator, the Report of the High Court's Inspector has resolved these issues, if not to the satisfaction of the regulator, for the time being. In the words of the Irish Director of Corporate Enforcement already quoted, this is the 'end of the road': 'There's no way that any court would sanction a director for having followed the company's legal advice'.[96]

Concluding on a contrary note, can ASIC take heart from a positive side to these unsuccessful attempts at regulatory enforcement? Does it mean that such regulatory persistence, as evidenced by the *Fyffes* cases is unnecessary? As the optimistic closing statement of the Irish Inspector' Report in January 2010 suggests:

> The good news from the perspective of the Director of Corporate Enforcement, and corporate compliance in Ireland, is that the Court, the public and the market can be reassured and take comfort from the fact that one of Ireland's largest listed public companies had a well developed culture of compliance, maintained high corporate standards and was a good corporate citizen, notwithstanding the costly error of appreciation by its then Chief Executive.[97]

96 Paul Cullen, 'Inquiry at "End of the Road", says Appleby', above n 43.
97 Report of the Inspector, above n 8, [12.1.17].