7 December 2023

Law Council
OF AUSTRALIA

Business Law Section

Director, Continuous Disclosure Review Unit
Markets Conduct and Digital Division
Treasury
Langton Cres
Parkes ACT 2600

By email: continuousdisclosurereview@treasury.gov.au

Dear Sir/Madam

Continuous Disclosure: Review of liabilities for failure to meet obligations

This submission concerning the Treasury's consultation *Continuous Disclosure: Review of liabilities for failure to meet obligations* is made by the Corporations Committee of the Business Law Section (the **BLS**) of the Law Council of Australia, with input from the Financial Services Committee.

This letter sets out general submissions in response to the request for views from interested parties to assist in the conduct of a review of the operation of the amendments made to the Continuous Disclosure Regime by the *Treasury Laws Amendment (2021 Measures No.1) Act 2021* (Cth) (**2021 Amendments**). The **Annexure** provides specific responses to the questions for consultation in the Consultation Paper.

The BLS supports the continuation of the amendments that are the subject of the review. The BLS supports the principle that civil penalty and civil compensation liability for continuous disclosure breaches should be fault based as a matter of fairness. The 2021 Amendments have imposed an appropriately fair 'knowledge, recklessness or negligence' standard, which provides both a signal and an incentive for disclosing entities to exercise reasonable care to discharge their relevant disclosure obligations under Chapter 6CA of the *Corporations Act 2001* (Cth). This, in the submission of the BLS, has had a material positive effect on continuous disclosure regulation in Australia.

The BLS considers that the 2021 Amendments have better aligned Australia with the liability regime in comparative international markets (refer to the response to Question 8 for more detail) and, in that regard, the Amendments have also had a material positive effect on Australian capital markets.

In the view of the BLS members contributing to this submission, there has been no evidence that the amendments have contributed to an adverse impact on disclosure practices, behaviours or outcomes, or to the number or nature of security-holder class actions in Australia. The relevant disclosure standards were not altered by the 2021 Amendments and, in the experience of the contributing BLS members, disclosing entities and their officers overwhelmingly seek to exercise due care and diligence to discharge their disclosure obligations.

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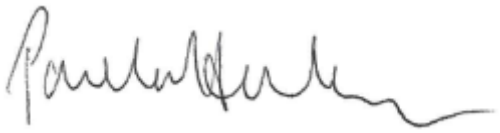
This behaviour has not been altered by the amendments although, following the amendments, there has been an even greater incentive from the viewpoint of the disclosing entity (and by extension for its directors and other officers) to exercise due care and diligence.

The BLS therefore submits that the 2021 Amendments should be retained.

It is noted that the submission of the BLS may be followed by a subsequent submission containing the separate views of the Class Actions Committee of the Law Council's Federal Dispute Resolution Section.

The BLS would be pleased to discuss any aspect of this submission. Please contact the Chair of the Corporations Committee, Mr Robert Sultan, on [redacted] or at [redacted], or Executive Member of the BLS, Mr John Keeves, on [redacted] or at [redacted], if you would like to do so.

Yours faithfully



Dr Pamela Hanrahan
Chair
Business Law Section

Annexure: Responses of the BLS to the Consultation Questions

Consultation Question	BLS Response
Impact on market efficiency and effectiveness	
1. Do you consider that the 2021 Amendments have: (a) resulted in the market for Australian listed securities being materially more efficient, effective, or well-informed; (b) resulted in the market for Australian listed securities being materially less efficient, effective, or well-informed; or (c) had no material impact on the efficiency or effectiveness of, or the level of information in, the market for Australian listed securities? Please explain the reason(s) for your answer.	In the view of the BLS, there has been no material impact on the market for listed securities because the 2021 Amendments did not change the actual disclosure obligation under ASX Listing Rule 3.1 or section 674 (applicable to listed entities) or 675 (applicable to unlisted entities) of the *Corporations Act 2001* (Cth) (**Corporations Act**). . There has been no observable change in market behaviour. The BLS considers that this may be because the disclosure obligation is the same and the bar set by the new 'fault' test to be established to enforce the disclosure obligation is low. Establishing a breach based on negligence is a bar that the Australian Investments and Securities Commission (**ASIC**) has been able to clear in section 180 cases associated with continuous disclosure over many years. Further, the changes have not stopped security-holder class actions, several of which have been filed alleging breaches of section 674A.
Impact on nature and quality of disclosures by disclosing entities	
2. Have you observed any changes in the nature and/or quality of disclosures by disclosing entities since the 2021 Amendments came into effect? If so, what changes have you observed and do you attribute those changes to the 2021 Amendments or to some other cause? What data or specific	No.

Consultation Question	BLS Response
examples can you provide to support your observations?	
3. Have the 2021 Amendments affected the ability of investors in Australian listed securities to make informed investment decisions? If so, how?	No.
Impact on class actions	
4. Have you observed any changes in the number and/or type of class actions against disclosing entities for breach of their continuous disclosure obligations since the 2021 Amendments came into effect? If so, what changes have you observed and do you attribute those changes to the 2021 Amendments or to some other cause? What data or specific examples can you provide to support your observations?	No. The BLS members contributing to this submission have no such evidence. A number of class actions have been commenced alleging breach of section 674A. By way of illustration *Nelson v Beach Energy* [2022] VSC 424; *Jowene Pty Ltd v Downer EDI Ltd* [2023] FCA 924; and *Lidgett v Downer EDI Ltd* [2023] VSC 574 are reported decisions relating to the conduct of such proceedings.
5. If the 2021 Amendments were to be repealed, would that have: (a) a materially positive impact; (b) a materially negative impact; or (c) no material impact at all, on the number and/or type of class actions against disclosing entities for breach of their continuous	It is not possible to predict the effect of the repeal of the 2021 Amendments on class actions. The BLS members contributing to the submission are not aware of any evidence to suggest that repeal of the 2021 Amendments would affect the number and/or type of class actions.

Consultation Question	BLS Response
disclosure obligations? Please explain the reason(s) for your answer.	
Impact on D&O insurance	
6. Have you observed any changes in the availability and/or cost of D&O [Directors and Officers] insurance for disclosing entities since the 2021 Amendments came into effect? If so, what changes have you observed and do you attribute those changes to the 2021 Amendments or to some other cause? What data or specific examples can you provide to support your observations?	Generally speaking, it has been a 'hard market' for D&O insurance since the Banking Royal Commission concluded in 2019, meaning that D&O premiums increased and the scope of coverage narrowed, in particular for security issues cover for listed entities from 2019 to 2022. However, these conditions appear to have eased in 2023. Therefore, it is difficult to attribute changes to D&O insurance to only the 2021 Amendments. Further, any changes based on the 2021 Amendments are difficult to pinpoint, given: (a) the recentness of the 2021 Amendments and that most claims involving listed entities which commenced post the 2021 Amendments are not yet finalised; (b) a lack of availability of claims data and the confidentiality of settlements; and (c) any premium changes due to the 2021 Amendments may have yet to occur given insurers' analysis of risks and actuarial data is ongoing.
7. If the 2021 Amendments were to be repealed, would that have: (a) a materially positive impact;	The BLS considers that repealing the 2021 Amendments would have a materially negative impact on the availability and cost of D&O insurance for disclosing entities.

Consultation Question	BLS Response
(b) a materially negative impact; or (c) no material impact at all, on the availability and/or cost of D&O insurance for disclosing entities? Please explain the reason(s) for your answer.	The sunsetting of section 674A may lead to an increase in successful shareholder class actions, as plaintiffs would have fewer elements to prove to establish a breach of the relevant obligations. If this manifests, D&O insurers are likely to perceive a greater risk in successful insurance claims, and hence seek to manage their risks by increasing premiums or narrowing the scope of cover. This would be particularly true for securities claim cover for companies (for example, breaches of continuous disclosure and market conduct regulations or in connection with the issue, sale or purchase of securities). Although the D&O insurance market appears to be softening in 2023 from the recent hard conditions over the 2019 to 2022 period, there is a risk that repealing the 2021 Amendments will mean that premiums for Side C cover (insuring the company for securities holder claims) will again rise, perhaps prohibitively so. It may also lead to an increase in premium or a narrowing of cover for Side A and B cover. Side A cover directly insures directors against specified liabilities and legal costs in circumstances where they are not indemnified by the company (such as where the company is prohibited from indemnifying the director or if the company lacks the financial means to do so). Side B cover, also referred to as 'company reimbursement cover', insures the company against its liability to indemnify directors. Sunsetting the 2021 Amendments could mean that insurers perceive an increased risk of directors being joined in successful class actions against companies, or separately being the subject of successful direct proceedings against them (for example, for breach of directors' duties). Accordingly, there may be a spike in premiums or narrowing of cover for both Side A and Side B D&O cover, which would likely become a barrier to obtaining cover for some companies. BLS members witnessed this increase in premium and narrowing of D&O cover for financial institutions following the Banking Royal Commission.

Consultation Question	BLS Response
Consistency with other markets	
8. Would you say that the continuous disclosure regime in the Corporations Act following the 2021 Amendments is: (a) materially tougher than; (b) materially more lenient than; or (c) in broad alignment with, the disclosure regimes that operate in major overseas markets? Please explain the reason(s) for your answer.	At a technical level, the BLS considers that the 2021 Amendments to the Australian continuous disclosure regime are in broad alignment with comparative disclosure regimes operating in major overseas markets. However, there are both technical and practical differences that make the current Australian regime more onerous for market participants and directors than the United States (**US**) and United Kingdom (**UK**) regimes. At a high level, the regimes can be summarised as follows: • **Australia**—requires a knowing, reckless or negligent misstatement or omission in relation to information that has a material effect on the price or value of ED securities of the entity (Corporations Act, section 674A); • **US**—requires a proof of intent to deceive, manipulate or defraud in relation to the purchase or sale of a security by the entity (*Securities Exchange Act 1934* subsection 10(b)); and • **UK**—requires a dishonest omission or delay regarding information relating to the issuance of securities by the entity (*Financial Services and Markets Act 2000* section 90A). The 2021 Amendments have brought the Australian regime into broader alignment with the US and UK regimes by introducing a fault element, requiring some form of mental intent. The US and UK regimes, like the Australian regime, allow for claims to be made for knowing or reckless misstatements and omissions.

Consultation Question	BLS Response
	The current Australian regime extends to negligent conduct, which is insufficient to create liability in the US or UK. To this extent, the Australian regime is technically more onerous for market participants and directors than the US and UK regimes in relation to rights to shareholder class actions, as they require a stricter fault element to be established. It should be noted that the UK and US regimes have no equivalent to the infringement notice regime for *alleged* breaches of section 674. To that extent, the Australian regime is broader. In relation to section 674 it is also worth noting that a listed entity is subject to criminal liability for misdisclosure, but that the nature of that liability would always require proof of fault. See further the BLS's response to Question 9 on the practical differences internationally.
9. The PJC Report stated that the 2021 Amendments would bring Australia's continuous disclosure regime closer to the regimes in comparable jurisdictions such as the United States and United Kingdom. ASIC, however, has stated that introducing a fault-based framework for ASIC enforcement litigation may have placed Australia out of step with the United States and the United Kingdom, where it appears regulators can take enforcement action without establishing fault. Do you agree with the PJC Report or with ASIC in this regard? Please explain the reason(s) for your answer.	The BLS comments specifically on this question below, but before doing so it is critical to understand the practical differences between the 3 jurisdictions. The UK has a regime where listed entities make disclosure calls with the assistance of an investment bank (generally the 'sponsor' that brought the entity to IPO or a replacement of that party). In almost every case, a listed entity will only make a market disclosure with guidance and input from that investment bank. The UK Financial Conduct Authority (**FCA**), when questioning disclosure issues analyses the process applied by the listed entity, including the advice provided by the investment bank, but very rarely second-guesses the judgment call that is made. The upshot of this is that the technical similarities or otherwise of the UK regime are fairly meaningless because the FCA doesn't intervene in any substantive way.

Consultation Question	BLS Response
	The US regime is different again, but for 2 reasons. Firstly, it does not have a real-time disclosure regime. It has quarterly reporting supplemented by the Form 8-K regime, which is formulaic in nature. Listed entities do not need to make judgment calls about whether to disclose. They either trigger the Form 8-K rules or they don't. So, even if there are technical similarities between the liability regimes, the substantive disclosure obligation is significantly different. In Australia, most continuous disclosure requires fine judgment to be made in real-time. In the US, it almost never does. Secondly, US listed entities are often swarmed by class actions and the Securities and Exchange Commission (**SEC**) itself almost never intervenes (generally, it does not have to). The BLS therefore stresses that comparisons on the regulatory powers are not of practical significance. As indicated above, in the experience of the BLS members involved in this submission, the UK and US regulators are less focused on continuous disclosure in setting their enforcement priorities than in Australia. However, as is evident from our response to question 13, there are notable instances of intervention by UK and US regulators, so it is not an area that they vacate. The BLS agrees with the PJC Report on whether the 2021 Amendments bring Australia's continuous disclosure regime closer to the US and UK regimes at a technical level. The PJC Report broadly argues that, following the 2021 Amendments, Australia's regime is closer to the UK and US on the basis that: • it removes the strict liability requirement for private actions, in a way comparable to the regime in the UK and US; and • the UK and US regimes require an element of misleading conduct or misbehaviour previously lacking in the plaintiff-friendly Australian regime, something that has since been added with the 2021 Amendments;

Consultation Question	BLS Response
	The PJC noted some differences between the 2021 Amendments and the US and UK regime, including that: • negligence is an insufficient ground for liability in the UK, whereas it is available in the amended Australian regime; and • the US has safe-harbour exemptions for forward-looking disclosures that are absent in the Australian regime. Meanwhile, the ASIC submission agreed with the findings of the PJC Report, but noted that there is a distinction between private litigation and enforcement by regulators, and that a fault-based framework would place Australia out of step with the US and UK to the extent that regulators could enforce disclosure obligations without establishing fault. In the view of the BLS, the PJC Report correctly identifies that the lack of a fault element in the Australian regime prior to the 2021 Amendments was unique amongst comparative jurisdictions. Likewise, Australia's plaintiff-friendly regime imposed the most onerous disclosure obligations upon listed entities and directors, compared with any comparable overseas jurisdiction. The 2021 Amendments, while not a complete match for the US and UK regimes, largely due to the inclusion of a negligence test and a lack of safe-harbour defences, did bring Australia's regime much more in line with the US and UK regimes than previously.

Consultation Question	BLS Response
10. If the 2021 Amendments were to be repealed, would that have: (a) a materially positive impact; (b) a materially negative impact; or (c) no material impact at all, on the competitiveness of Australian equity markets to attract new listings compared to major overseas equities markets? Please explain the reason(s) for your answer.	The BLS suggests there could be a negative impact if the 2021 Amendments were repealed because a civil penalty and civil compensation liability regime which is not fault-based is a factor that would be taken into account in assessing the relative competitiveness of Australian equity markets, and would certainty make directorship of an Australian disclosing entity less attractive in comparison to an entity listed on an overseas exchange in a jurisdiction where liability is fault-based.
Compliance and enforcement	
11. Have the 2021 Amendments given rise to barriers that may hinder the effective enforcement by ASIC of a disclosing entity's continuous disclosure obligations under the Corporations Act. If so, what are those barriers and how do you think they should be addressed?	The BLS members who have contributed to this submission observe that ASIC has issued relatively fewer infringement notices in relation to continuous disclosure since the 2021 Amendments than before. However, as a matter of principle and policy (and fairness), the BLS considers that infringement notices are an unsuitable enforcement tool for conduct involving the exercise of judgment and we note that ASIC does not appear to have been hindered in taking other forms of enforcement action in relation to continuous disclosure since the 2021 Amendments.

Consultation Question	BLS Response
12. Have you observed any changes in the number and/or effectiveness of enforcement actions by ASIC against disclosing entities for breach of their continuous disclosure obligations since the 2021 Amendments came into effect? If so, what changes have you observed and do you attribute those changes to the 2021 Amendments or to some other cause? What data or specific examples can you provide to support your observations?	As above, the BLS observes that ASIC has issued relatively fewer infringement notices in relation to continuous disclosure since the 2021 Amendments than before. This may be attributable to the need for ASIC to prove fault in the event that an infringement notice is not paid by the relevant entity and ASIC pursues the matter further.
13. If the 2021 Amendments were to be repealed, would that have: (a) a materially positive impact; (b) a materially negative impact; or (c) no material impact at all, on the capacity of ASIC to take effective enforcement action against disclosing entities for breach of their continuous disclosure obligations? Please explain the reason(s) for your answer.	There is no evidence that ASIC's current enforcement stance and activity in relation to continuous disclosure is not effective. ASIC has had a number of recent successes in enforcement actions in relation to continuous disclosure. There is indeed (as yet) no evidence that the need to prove fault would have changed the outcome in any historical ASIC court enforcement action. The BLS notes that ASIC's ability to obtain an enforcement outcome in relation to the Rio Tinto continuous disclosure enforcement proceedings (*ASIC v Rio Tinto Limited (No 2)* [2022] FCA 184) does not suggest that ASIC was in any materially worse position than the US SEC or the UK FCA, both of which also secured enforcement outcomes in relation to the same conduct based on breach of fault-based obligations.

Consultation Question	BLS Response
14. Are there any other matters concerning the 2021 Amendments that you would like to see addressed in the Review?	First, the BLS submits that the Review should also consider whether the Australian liability regime can be more closely aligned with comparative international jurisdictions. Secondly, the liability regime across the various mandated disclosure requirements under the Corporations Act lack consistency. Leaving aside various disclosures that remain subject to no fault liability for misleading or deceptive conduct under section 1041H, the most significant securities law mandated disclosure requirements under the Corporations Act have some type of fault element as a precondition to liability. Both fundraising disclosure documents under Chapter 6D and takeover documents under Chapters 6 and 6B are: (a) expressly removed from the ambit of no fault liability for misleading or deceptive conduct under section 1041H (see section 1041H(3)); and (b) have fault elements in terms of due diligence (section 731) or lack of knowledge defences (section 670D). Therefore, having continuous disclosure subject to pure strict liability (in the absence of a fault-related defence) by repealing the 2021 Amendments would, in the view of the BLS, be clearly anomalous.