
A call for a bold and effective corporate disclosure regulatory framework

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The strategies and priorities of the corporate disclosure regulators in Australia are not entirely clear. This article calls for a bold and effective regulatory framework in order to achieve the policy goals of market fairness and economic efficiency. It argues that this requires the regulators to place greater emphasis on compliance with, and enforcement of, the periodic and continuous disclosure obligations.

INTRODUCTION

Australia has had company disclosure rules in place for many years. The *Corporations Act 2001* (Cth) (the Act) provides a comprehensive company disclosure framework encompassing periodic reporting; continuous disclosure; takeover, acquisition and buy-out events; and fund raising.¹ This disclosure regulation is supported by market misconduct regimes, including provisions dealing with insider trading and misleading and deceptive conduct. Listed companies are also subject to Australian Securities Exchange (ASX) disclosure Listing Rules. However, questions on whether this disclosure regulation and the associated enforcement regimes are efficacious remain open.

Several scholars have commented on disclosure-related enforcement in Australia.² Some highlighted that legislation can be “misleading where its ‘bark is not co-extensive with its bite’”.³ Dignam and Galanis argued that while Australia has “comparable legislative disclosure standards to those in the UK and the US ... these disclosure requirements have not been properly enforced ... [and this] lax enforcement undermines legal protection of investors”.⁴ They suggested that when “there is insufficient public information available, the close and private relationships of an insider system ... arise[s], rather than the arm’s-length relationships of an outsider system”.⁵

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¹ Part 2M.3 of the *Corporations Act 2001* (Cth) governs periodic reporting and audits. Chapters 6, 6A and 6B provide the disclosure rules that apply to takeovers, compulsory acquisitions and buy-out events. Chapter 6CA deals with the continuous disclosure obligations and Ch 6D outlines the disclosure rules related to fundraising. The market misconduct and insider trading provisions are located within Pt 7.10.

² See eg Golding G and Kalfus N, “The Continuous Evolution of Australia’s Continuous Disclosure Laws” (2004) 22 C&SLJ 385 at 426; Cassidy A and Chapple L, “Australia’s Corporate Disclosure Regime: Lessons from the US Model” (2003) 15 AJCL 81 at 81-82; Bird H, Chow D, Lenne J and Ramsay I, *ASIC Enforcement Patterns* (Working Paper, Centre for Corporate Law and Securities Regulation, University of Melbourne, 2003).

³ Semaan L, Freeman M and Adams M, “Is Insider Trading a Necessary Evil for Efficient Markets? An International Comparative Analysis” (1999) 17 C&SLJ 220 at 235.

⁴ Dignam A and Galanis M, “Australia Inside-Out: The Corporate Governance System of the Australian Listed Market” (2004) 28 MULR 623 at 644-645, 648. Dignam and Galanis argued that two fundamental parameters characterise financial systems: the degrees of financial intermediation and financial securitisation. To characterise a system as one or the other is to describe the degree of intermediation or securitisation. In an insider system, the degree of intermediation is high while the degree of financial securitisation is low; in an outsider system, the reverse is true. They concluded that the Australian listed market was characterised by significant blockholders engaged in private rent extraction; institutional investor powerlessness; a strong relationship between management and blockholders, which resulted in a weak market for corporate control; and an historical weakness in public and private securities regulation, which allowed the creation and perpetration of crucial blocks to information flow. These scholarly arguments were made a few years ago. Arguably, Australia no longer has comparable legislative disclosure standards to those in the United Kingdom and the United States. On the other hand, disclosure-related enforcement actions in Australia have increased in recent years, some of these actions have been against larger companies, and ASIC has indicated that more actions are in the pipeline.

⁵ Dignam and Galanis, n 4 at 642.



This article calls for a regulatory framework in Australia governing listed company disclosure that

- is risk-based, including clearly identified long-term goals and priorities;
- has a primary emphasis on prevention; and
- promotes evidentiary-based decision-making.

It is argued that this framework would result in greater regulatory focus on compliance with, and enforcement of, the periodic and continuous disclosure obligations. It is not suggested that enforcement of other areas such as insider trading litigation should be wound down. Instead, a recalibration of the regulatory priorities and emphases is sought.

Resources available to modern regulators such as the ASX and Australian Securities and Investments Commission (ASIC) are inevitably finite. As such, appropriate resource allocations (i) between preventative and enforcement measures and (ii) within the enforcement allocation to specific cases are critical. Listed companies provide ongoing information to investors under the periodic and continuous disclosure regimes; these disclosures represent the largest body of Australian corporate information provided in the public arena;⁶ and most Australian adults have exposure to the listed securities market through compulsory superannuation or as direct investment into ASX listed securities. This means that clear, concise and effective reporting under the periodic and continuous disclosure regimes must be a high priority for the Australian regulators.

To understand the current regulatory approach to listed company disclosure, enforcement actions under the company disclosure and insider trading regimes are discussed, and selected content from ASX and ASIC policy documents and speeches is outlined. To complete the picture, market participant views and stakeholder responses on listed company disclosure practices and enforcement are presented. This combined evidence suggests that a bold and focused corporate disclosure regulatory framework is needed.⁷

The next part of the article summarises the enforcement actions under the periodic disclosure, continuous disclosure and insider-trading regimes and provides critique. It is followed by outlines of published commentary from regulators and stakeholders on listed company disclosure and a discussion of the proposed regulatory framework. The final part concludes.

LISTED COMPANY DISCLOSURE ENFORCEMENT RECORD

The deterrence impact of rigorous statutes recedes drastically as the likelihood of successful usage lessens. Hence, statutes that are intended to enhance market integrity and investor protection have relatively negligible effect if there exists widespread non-compliance.⁸

This part of the article provides a summary of the enforcement actions under the periodic disclosure, continuous disclosure and insider trading regimes. Disclosure under the periodic and continuous disclosure regimes forms the largest body of company information provided in the public arena in Australia. In addition, trading on materially price-sensitive information that has not been disclosed to the broader market may result in liability under the insider trading regime.

⁶ Takeovers, acquisitions, buy-outs and fundraising tend to be one-off events.

⁷ Scholarly studies on listed company disclosure in Australia support these views. See Neagle A and Tsykin N, "Please Explain": *ASX Share Price Queries and the Australian Continuous Disclosure Regime* (Working Paper, Centre for Corporate Law and Securities Regulation, University of Melbourne Research Report, 2001); Gallery G, Gallery N and Gilchrist C, *Are Australian Corporate Disclosures "Continuous" or Opportunistic?* (Working Paper, University of New South Wales, University of Sydney, 2002); Gallery G, Gallery N and Hsu G, *The Association Between Management and Analysts' Earnings Forecasts in the Australian Continuous Disclosure Environment* (Working Paper, University of New South Wales, University of Sydney, 2002); McNamara C, Gallery G and Fagher N, *Management Reluctance to Disclose Earnings Information in a Continuous Disclosure Environment: Evidence from the Association Between Unexplained Stock Returns and Subsequent Disclosure* (Working Paper, University of New South Wales, February 2004). These scholarly studies are summarised and additional original research is outlined in North G, "Continuous Disclosure in Australia: The Empirical Uncertainties" (unpublished, 2010).

⁸ Steinberg M, "Insider Trading, Selective Disclosure, and Prompt Disclosure: A Comparative Analysis" (2001) 22 *University of Pennsylvania Journal of International Economic Law* 635 at 676.



Periodic disclosure regulation

Periodic disclosure enforcement record

Australian periodic disclosure regulation applying to listed companies includes the statutory reporting requirements and the ASX periodic disclosure Listing Rules. Listed Australian companies must currently provide an online half year report,⁹ an online preliminary final report,¹⁰ and an annual report that is available online or in hard copy by request.¹¹ Chapter 2M of the Act and Ch 4 of the ASX Listing Rules mandate the content of the half year and full year reports including the preliminary final and annual reports.

Australia uses a co-regulatory model for company reporting and disclosure, with the ASX and ASIC as joint regulators. The partnership between the ASX and ASIC is underpinned by a memorandum of understanding.¹² Section 792D of the Act requires the ASX to provide ASIC with the assistance that it reasonably requires to perform its functions. In October 1998, the ASX demutualised and became a listed company.¹³ However, the ASX has continued as the primary supervisor of listed companies.¹⁴ Since 2006, the supervisory functions of the exchange have been located in a separate subsidiary company, the ASX Markets Supervision (ASXMS). The ASXMS has external directors to improve the level of independence and to “minimise further the perception of conflict between the ASX’s regulatory and commercial functions”.¹⁵ The ASX is also subject to external review. The directors of the ASX Supervisory Review Pty Ltd (ASXSR) review and report to the ASX board on compliance by the exchange with its statutory licence obligations.¹⁶ In addition, ASIC is required to review the ASX as a licensee on an annual basis.¹⁷ The scope of this review concerns whether the ASX “management processes are adequate to ensure that ASX’s commercial interests do not prevail over its supervisory function”.¹⁸

Both the ASX and ASIC monitor listed company annual reports for compliance with accounting standards and governance regulation.¹⁹ The ASIC annual report for 2008-2009 indicates that the financial reports of over 100 listed companies were reviewed.²⁰ In addition, the ASX has used its powers of suspension and delisting against companies that failed to lodge half year and annual

⁹ Some listed Australian companies required investors to source their 2009 half year reports online.

¹⁰ ASX Listing Rule 4.3B; ASX Guidance Note 14, *Company Announcement Platform 2*.

¹¹ Mining producing entities and mining exploration companies are required to provide specialised quarterly reports under ASX Listing Rules 5.1-5.18. In addition, other entities must provide quarterly cash flow reports in the format of App 4C to show cash adequacy under ASX Listing Rule 4.7B.

¹² Australian Securities Exchange (ASX), *Memorandum of Understanding Between Australian Securities and Investments Commission and Australian Stock Exchange Limited* (30 June 2004).

¹³ The stated objectives of the ASX include the provision of “a fair and well-informed market for financial securities and providing an internationally competitive market”: ASX, *Introduction to Listing Rules*.

¹⁴ ASX, “ASX Reinvigorates Market Supervision”, *Media Release* (15 December 2005) p 1.

¹⁵ ASX, n 14, p 2.

¹⁶ The ASXSR annual reports are not publicly released.

¹⁷ *Corporations Act 2001* (Cth), s 794C. See eg Australian Securities and Investments Commission (ASIC), *Report 135: Market Assessment Report* (31 July 2008).

¹⁸ See eg ASIC, “ASIC Releases Annual Assessment of Australian Securities Exchange”, *Media Release 08-186* (14 August 2008). The assessment processes and standards used by ASIC to determine whether the ASX supervisory processes are adequate are not made public.

¹⁹ ASX, n 14, Attachment 3; ASIC, “Companies Make Changes Following ASIC Review”, *Media Release 04-103* (13 April 2004); ASIC, “ASIC Releases Preliminary Results of 2004-2005 Financial Reporting Surveillance Project”, *Media Release 05-31* (17 February 2005).

²⁰ ASIC, *ASIC Annual Report 2008-2009*, p 30. The review of annual reports focused on going concern assessments, impairment of assets, fair value determinations, off-balance sheet arrangements, and financial instrument risk disclosures.



reports.²¹ The ASX and ASIC generally endeavour to achieve a regulatory outcome through settlement. Companies are asked to rectify any identified issues.²² However, listed companies and their directors have been prosecuted for breaches of the statutory annual reporting provisions.

For example, in *Australian Securities and Investments Commission v MYOB Ltd* (2002) 41 ACSR 44, ASIC sought a declaration that MYOB had contravened ss 304 and 305 of the *Corporations Law* because the acquisition of assets in the financial statements for the half year ended 30 June 2000 had not been prepared in accordance with Standard 1015 of the Australian Accounting Standards Board (AASB). However, Hansen J dismissed this application holding that AASB 1015 did not apply to the ongoing balances of previously acquired assets. In *Australian Securities and Investments Commission v Loiterton* [2004] NSWSC 172, ASIC initiated civil proceedings against the directors of Clifford Corp Ltd and the Clifford Group of companies for breaches of ss 232, 318, 292, 295A, 298 and 1002G of the *Corporations Law* in the preparation and publication of the statutory accounts. These actions were successful. Bergin J held that the full year consolidated accounts of Clifford Corp included purported profits from pre-acquisition fees and did not give a true and fair view of the profit and loss of the Group (at [585]-[587]). In addition, the notes to the accounts did not comply with AASB 1017 on related-party disclosures.

Interestingly, in *QBE Insurance Group Ltd v Australian Securities Commission* (1992) 38 FCR 270; 8 ACSR 631, Lockhart J dismissed applications by QBE and NRMA for a declaration that para 23 of AASB 1023 pursuant to s 313 of the *Corporations Law* was invalid. Applications seeking orders to set aside the Australian Securities Commission (ASC)²³ decision to refuse their s 313 applications were also dismissed. Lockhart J stated that if, in the opinions of the directors of QBE and NRMA, the profit and loss account prepared in compliance with para 23 of AASB 1023 would not give a true and fair view of the company's profit and loss for a financial year, the directors would be obliged to add information or appropriate notes complying with s 299(10) of the *Corporations Law*.²⁴

Periodic disclosure enforcement critique

Listing Rules

The ASX has a hierarchy of powers that it can use to enforce compliance with the disclosure Listing Rules. Its informal powers of persuasion are considerable. Ultimately, the ASX may suspend or remove securities from trading on the stock exchange.²⁵ However, the exchange states that

it does not have delegated responsibility to "regulate" or "supervise" participants or listed entities' compliance with the law. As a licensee, ASX is obliged to monitor conduct in relation to the markets and facilities it operates, to supervise the market and ensure compliance with its rules, and to refer to ASIC any suspected breaches of the law.²⁶

The ASX Position Paper of June 2008 uploaded onto the supervisory area of the exchange website indicates that the ASX Operational Rules encompass the market rules, clearing and settlement rules, operating rules, and Listing Rules.²⁷ It explains that the market, clearing and settlement, and operating

²¹ See eg *Re Captech Group Ltd and Australian Securities and Investments Commission* (2003) 47 ACSR 381. See also ASX, n 13; ASX Listing Rules 17.2 and 17.3.

²² See eg Brown P and Tarca A, "Achieving High Quality, Comparable Financial Reporting: A Review of Independent Enforcement Bodies in Australia and the United Kingdom" (2007) 43 *Abacus* 438, App A. Appendix A lists 42 annual and interim reporting cases publicised by ASIC during the period 1 July 1998 to 30 June 2004. Of these, only four involved court actions.

²³ The Australian Securities Commission was the predecessor to ASIC.

²⁴ Paragraph 23 of AASB 1023 concerned accounting for the revaluation of non-current assets. It required insurance companies to bring to account in the profit and loss unrealised gains and losses on investments at net market value as at balance date. This requirement applied irrespective of the length to maturity of the investments and whether the gains or losses were real or permanent.

²⁵ ASX, n 13; ASX Listing Rules 17.2 and 17.3.

²⁶ See ASX, *Supervision and Enforcement Approach of ASX Markets Supervision*, http://www.asx.com.au/supervision/enforcement_outcomes/supervision_enforcement_approach.htm viewed 26 March 2010.

²⁷ ASX, *ASX Position Paper: ASX's Role in Australia's Financial Regulatory Framework* (June 2008) p 6.



rules are administered and enforced by the exchange, with referrals to the disciplinary tribunal or ASIC when necessary.²⁸ The paper further indicates that it is not the role of the ASX to investigate and prosecute companies or individuals for breaches of the law. Instead, trades are monitored to identify where trading may be taking place in a listed company but the market is not fully informed,²⁹ with possible breaches of the law referred to ASIC.³⁰ The cited types of breaches referred to ASIC are insider trading, market manipulation and continuous disclosure breaches.³¹ This leaves the issue of who is responsible for supervision and enforcement of the periodic disclosure Listing Rules ambiguous.³²

The preliminary final reports currently provide the most comprehensive information to Australian investors on a timely basis, as reflected in the ASX practice of tagging the releases of preliminary final reports (but not the annual reports) as price-sensitive on the website.³³ While the Listing Rules in relation to half yearly and annual reporting are broadly similar to the statutory requirements, those governing preliminary final reporting are not replicated in statute. However, no evidence could be found of any enforcement of the periodic disclosure Listing Rules by Australian regulators other than the suspension of some companies for a failure to provide periodic reports by the due dates.³⁴

The obligation of listed companies to comply with the ASX operating rules is given statutory force under ss 792A, 793C and 1101B of the Act. The ASIC, a licensee, the ASX, or an aggrieved person may apply to the courts for an order directing compliance with the Listing Rules under ss 793C and 1101B. These provisions have never been utilised and the ability of an applicant to secure a conviction or compensation is unclear. While s 1101B allows a fine to be imposed for a contravention without reasonable excuse,³⁵ the court can only make such an order if it is satisfied that this would not unfairly prejudice any person. No material was found within the ASX supervisory documentation explaining that the exchange can enforce the Listing Rules under ss 793C or 1101B and providing guidance on the circumstances or factors that may result in use of these powers.

²⁸ ASX, n 27, p 6; ASX, *Disciplinary Tribunal*, http://www.asx.com.au/supervision/enforcing_rules/disciplinary_tribunal.htm viewed 26 March 2010. The ASX disciplinary tribunal page outlines the functions, operation and structure of the disciplinary tribunal. The tribunal has jurisdiction over disciplinary matters in relation to alleged breaches of the ASX Market Rules, ASX Settlement Rules, ACH Clearing Rules, Operating Rules of the Sydney Futures Exchange, Clearing Rules of the Sydney Futures Exchange and Austraclear Regulations but not the Listing Rules. The website allows access to the disciplinary announcements.

²⁹ This role will be taken over by ASIC under the proposed multiple operator reforms.

³⁰ ASX, n 27, pp 4-5.

³¹ ASX, n 27.

³² See ASX, *Issuers Unit: Function and Operation*, http://www.asx.com.au/supervision/issuers/function_and_operations.htm#monitoring viewed 20 March 2010. The issuers unit website indicates that the issuers unit reviews (i) all media commentary in major and national newspapers to identify reports about listed entities, and determine whether disclosure is required; and (ii) all information released to ASX's centralised announcement processing office or company announcements platform to determine whether additional or clarifying disclosure is required, and whether other Listing Rules have been complied with. However, neither the annual report nor the website explains how non-compliance with the periodic disclosure Listing Rules is enforced when necessary.

³³ The annual reports of listed companies are released to the market about a month after the release of the preliminary final report. Global empirical research suggests there is minimal price response to the release of annual reports due to their lack of timeliness: Foster T and Vickrey D, "The Incremental Information Content of the 10-K" (1978) 53 *Accounting Review* 921 at 931; Foster T, Jenkins D and Vickrey D, "The Incremental Information Content of the Annual Report" (1986) 16 *Accounting and Business Research* 91 at 98; Cready W and Mynatt P, "The Information Content of Annual Reports: A Price and Trading Response Analysis" (1991) 66 *Accounting Review* 291 at 292.

³⁴ ASX, *ASX Market Supervision Annual Report* (2009) p 10. Page 10 of the 2009 annual report indicates there were 89 ASX-initiated suspensions due to a breach of the Listings Rules for reasons such as non-lodgment of periodic reports by the due date. The ASXMS annual report is only available for 2009 and the release of data on ASX-initiated suspensions appears to be a new initiative. The author requested such information in 2006 and was informed by the customer service area of the ASX that it was not available.

³⁵ Failure to comply with s 1101B(1) is an offence under s 1311(1). The penalty is 100 penalty units or imprisonment for two years or both. The penalty for a body corporate is five times the maximum: s 1312.



Some market participants suggest that complaints to the ASX about disclosure breaches or insider trading are not acted upon.³⁶ Importantly, the ASX has “absolute discretion” on any regulatory or compliance action taken, including a right “to decide to take no action in response to a breach of [a] ... listing rule”.³⁷ The ASX also has discretion to grant a waiver of a particular rule.³⁸

The government announced proposed reforms to the supervision of Australia’s financial markets on 24 August 2009 as an initial step in the process towards possible multiple operators. Under the proposed reforms,

ASIC will become responsible for supervising trading activities by broker participants which take place on a licensed financial market, while individual markets – such as the ... ASX – will retain responsibility for supervising the entities listed on them.³⁹

Chris Bowen, the Minister for Financial Services, Superannuation and Corporate Law, stated that “there is no need for the Government to supervise listed entities. ASIC and the ASX are working well together in performing this role”.⁴⁰

Statutory regime

ASIC has initiated litigation relating to the financial statements within annual reports and failures to comply with accounting standards. However, no evidence could be found of any enforcement of the statutory rules on half year accounts and management discussion and analysis in periodic reports.

Continuous disclosure regulation

Enforcement of continuous disclosure regulation

Under ASX Listing Rule 3.1, companies that become aware of materially price-sensitive information must immediately disclose that information through the ASX company announcement platform.⁴¹ A statutory continuous disclosure regime was introduced in September 1994 to support or reinforce the listing rule obligations.⁴²

ASIC has a range of enforcement options under the statutory continuous disclosure provisions. A failure to comply with the statutory provisions may be an offence,⁴³ or subject to civil proceedings⁴⁴ including an infringement notice process for minor offences.⁴⁵ ASIC may seek an injunction⁴⁶ or initiate a public interest proceeding.⁴⁷ It may also accept enforceable undertakings as an alternative to litigation.⁴⁸

³⁶ Saulwick J and Yeates C, “Regulator Forces Reforms on ASX”, *Sydney Morning Herald* (Sydney) (15 August 2008). Even when systemic breaches of the periodic disclosure rules are identified, the ASX has the discretion to take no action.

³⁷ ASX Listing Rule 18.5.

³⁸ ASX, n 13.

³⁹ Bowen C, Minister for Financial Services, Superannuation and Corporate Law, “Reforms to the Supervision of Australia’s Financial Markets”, *Media Release 013* (24 August 2009).

⁴⁰ ASX, n 13.

⁴¹ ASX Listing Rule 3.1.

⁴² *Corporations Act 2001* (Cth), Ch 6CA, ss 674-678.

⁴³ *Corporations Act 2001* (Cth), ss 674 Note 1, 678, 1311(1).

⁴⁴ *Corporations Act 2001* (Cth), ss 674 Note 2, 1317E, 1317S.

⁴⁵ *Corporations Act 2001* (Cth), ss 674 Note 3, 1317DAC. In 2004, the maximum penalty for a corporate breach of the financial services civil penalty provisions was increased to \$1 million and an infringement notice procedure was introduced for relatively minor breaches of continuous disclosure law: *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004* (Cth); *Corporations Act 2001* (Cth), ss 1317E(ja), 1317G(1B); *Corporations Act 2001* (Cth) Pt 9.4AA, ss 1317DAA-1317DAJ.

⁴⁶ *Corporations Act 2001* (Cth), s 1324.

⁴⁷ *Australian Securities and Investments Commission Act 2001* (Cth), s 50.

⁴⁸ *Australian Securities and Investments Commission Act 2001* (Cth), s 93AA.



Court actions

ASIC has initiated three successful court actions under the statutory continuous disclosure provisions: *Australian Securities and Investments Commission v Southcorp Ltd (No 2)* (2003) 130 FCR 406 (*Southcorp* action); *Australian Securities and Investments Commission v Chemeq Ltd* (2006) 58 ACSR 169 (*Chemeq* case); and *Australian Securities and Investments Commission v Macdonald (No 11)* (2009) 230 FLR 1; [2009] NSWSC 287 (*Hardie* case). In the first two cases, the defendant companies pleaded guilty and were fined under the civil penalty provisions. The *Hardie* case was contested.

The *Southcorp* action was based on an email sent by Southcorp's executive general manager of corporate affairs to analysts on 18 April 2002. The email disclosed that the group's profit for the 2003 year would be negatively impacted to the extent of \$30 million by the poor 2000 vintage. However, this fact was not disclosed to the market through the ASX. From the time the email was sent until a trading halt was called at 1.07 pm on 19 April 2002, the Southcorp share price fell 7% (at 416).⁴⁹ Southcorp subsequently admitted that it had contravened ASX Listing Rule 3.1 and s 674(2) of the Act because at the time the information was selectively released to the analysts, the information had not been announced through the ASX and was not generally available to the market (at 406). The civil penalty applied by the court was \$100,000 from a maximum penalty at the time of \$200,000.

The *Chemeq* case involved two admitted contraventions of s 674(2); the first involved a failure to notify the ASX about the increased costs of constructing and commissioning its manufacturing facility at East Rockingham between 10 February 2003 and 30 April 2004, and the second involved a failure to disclose adequate information between 1.22 am on 6 October 2004 and 3.36 pm on 7 October 2004 about the commercial impact of a patent granted in the United States in 2004 (at 183). Chemeq was fined \$150,000 in respect of the first contravention from a maximum penalty at the time of \$200,000 and \$350,000 in respect of the second contravention from a maximum penalty of a million dollars (at 198).

The *Hardie* case included two contraventions of the continuous disclosure obligations. The first related to a resolution by the James Hardie Industries Ltd (JHIL) board on 15 February 2001 to execute a deed of covenant and indemnity (DOCI). Gzell J of the New South Wales Supreme Court held that JHIL negligently failed to disclose the DOCI information in contravention of ASX Listing Rule 3.1 and s 1001A(2) of the *Corporations Law* as carried into the Act (at 556). The second was a failure by James Hardie Industries NV (JHINV) to notify the ASX of the ABN 60 Foundation information. On 25 March 2003 JHINV resolved:

- that JHINV execute a trust deed establishing the ABN 60 Foundation (Foundation);
- to approve a capital reduction by JHIL;
- to request JHIL to issue 1,000 shares to the Foundation;
- that the fully paid shares held by JHINV be cancelled for no consideration; and
- that it enter into a deed of covenant indemnity and access.

Gzell J held that JHINV failed to notify the ASX of this information in accordance with ASX Listing Rule 3.1 between 25 March and 20 June 2003, thereby contravening s 674(2) of the Act (at 559).

More recently, in *Australian Securities and Investments Commission v Fortescue Metals Group Ltd (No 5)* (2009) 76 ACSR 506; [2009] FCA 1586 an action by ASIC against Fortescue Metals alleging contravention of s 674 of the Act was dismissed. ASIC submitted that Fortescue Metals Group Ltd (FMG) through Forrest, the chief executive officer, had no genuine and or reasonable basis for making its claim within an ASX announcement that framework agreements with China Railway Engineering Corp, China Harbour Engineering Co and China Metallurgical Construction (Group) Corp were binding build and transfer agreements. However, Gilmour J found (at [54]) that "FMG, its board and Forrest held their opinion as to the meaning and legal effect of the framework agreements honestly and reasonably". ASIC has filed a notice of appeal indicating that the findings of Gilmour J

⁴⁹ This equated to a reduction in the market capitalisation of Southcorp Ltd of more than \$332 million.



raise important issues as to the proper interpretation and application of provisions governing company announcements and these issues warrant review by an appeal court.⁵⁰

Infringement notices

In 2004, an infringement notice procedure was introduced for relatively minor breaches of continuous disclosure law.⁵¹ The scheme was introduced to provide ASIC with a timely enforcement process with redress that is “proportionate and proximate in time to the alleged breach”.⁵² Since 2006, ASIC has regularly used these powers, with 12 notices issued to date. Notices have been made against:

- Solbec Pharmaceuticals Ltd for an alleged failure to notify the ASX in detail of the nature of the results of an animal study relating to its cancer drug, CoramsineTM;⁵³
- QRSciences Holdings Ltd for an alleged failure to disclose to the ASX that an underwriter to a fund raising on 31 January 2005 had withdrawn;⁵⁴
- SDI Ltd for an alleged failure to update the ASX of its revised net profit forecast on 2 May 2005;⁵⁵
- Avastra Ltd for an alleged failure to inform the ASX of a significant delay in the publication of results of a clinical trial on 26 April 2005;⁵⁶
- Astron Ltd for an alleged failure to inform the ASX of a significant increase in the mineral resource estimate for its Donald Mineral Sands Project;⁵⁷
- Avantogen Ltd for an alleged failure to inform the ASX of information regarding the unsuccessful outcome of a phase II clinical trial of its Pentrys anti-cancer vaccine;⁵⁸
- Promina Group Ltd for an alleged failure to inform the market about a takeover proposal from Suncorp Metway Ltd after the information ceased to be confidential;⁵⁹
- Raw Capital Partners Ltd for an alleged failure to properly inform the market about the loss of a significant IT service contract;⁶⁰
- Centrex Metals Ltd for an alleged failure to notify the ASX about the signing of a binding Heads of Agreement with Baotou Iron & Steel Co Ltd concerning the supply of hematite;⁶¹
- Sub-Sahara Resources NL for an alleged failure to properly inform the market about metallurgical test results;⁶²
- Rio Tinto Ltd for an alleged failure to notify the ASX of an acquisition of Alcan Inc once the information about the acquisition ceased to be confidential;⁶³ and
- the Commonwealth Bank of Australia for an alleged failure to notify the ASX about a significant deterioration in its expected loan impairment expense for the financial year ending 30 June 2009.⁶⁴

⁵⁰ ASIC, “ASIC Appeals Federal Court Decision in Fortescue Metals Group Civil Penalty Proceedings”, *Media Release 10-13AD* (4 February 2010).

⁵¹ *Corporations Act 2001* (Cth), Pt 9.4AA.

⁵² ASIC, *Continuous Disclosure Obligations: Infringement Notices – An ASIC Guide* (May 2004) p 4.

⁵³ ASIC, “ASIC Issues First Infringement Notice for Continuous Disclosure Breach”, *Media Release 05/223* (1 August 2005).

⁵⁴ ASIC, “ASIC Disclosure Penalty for Perth Company”, *Media Release 06/42* (17 February 2006).

⁵⁵ ASIC, “Melbourne Company Pay Disclosure Penalty”, *Media Release 06/124* (21 April 2006).

⁵⁶ ASIC, “Sydney Life Sciences Company Pays Disclosure Penalty”, *Media Release 06/156* (15 May 2006).

⁵⁷ ASIC, “Chemical Company Pays \$66,000 Penalty”, *Media Release 06/242* (18 July 2006).

⁵⁸ ASIC, “Biotechnology Company Pays \$33,000 Fine”, *Media Release 06-428* (8 December 2006).

⁵⁹ ASIC, “Promina Pays \$100,000 Fine”, *Media Release 07-69* (20 March 2007).

⁶⁰ ASIC, “Information Technology Services Company Pays \$33,000 Fine”, *Media Release 07-207* (1 August 2007).

⁶¹ ASIC, “Mineral Exploration Company Pays \$33,000 Fine”, *Media Release 08-50* (12 March 2008).

⁶² ASIC, “Mineral Exploration Company Pays \$33,000 Fine”, *Media Release 08-87* (29 March 2008).

⁶³ ASIC, “Rio Tinto Complies with ASIC Infringement Notice”, *Media Release 08-117* (5 June 2008).

⁶⁴ ASIC, “Commonwealth Bank Pays \$100,000 Penalty”, *Media Release 09-199* (14 October 2009).



All of these companies elected to comply with the infringement notice and pay the relevant amount without admitting liability.⁶⁵ The penalty payable is determined by the market capitalisation of the company and whether the company has a prior conviction under ss 674(2) or 675(2). Assuming no previous conviction, a company is fined \$100,000 when its market capitalisation exceeds \$1,000 million (Tier 1), \$66,000 when its market cap exceeds \$100 million (Tier 2) and \$33,000 when its market capitalisation is below \$100 million (Tier 3).⁶⁶ Of the 12 infringement notices, three have been issued against Tier 1 companies,⁶⁷ one against a Tier 2 company,⁶⁸ and the remaining 8 have been made against Tier 3 companies.

Enforceable undertakings

In 1996, ASIC argued in its submission to a Companies and Securities Advisory Committee (CASAC) review that the availability of enforcement options other than litigation would encourage compliance with the continuous disclosure regulation. In response, CASAC recommended that ASIC should have the power to demand enforceable undertakings. The legislators agreed. ASIC may currently accept an enforceable undertaking under s 93AA of the *Australian Securities and Investments Commission Act 2001* (Cth).

An ASIC Guide indicates that an

enforceable undertaking can be initiated by a company, an individual or a responsible entity, or as a result of a discussion between that party and ASIC. [However, ASIC] do not have the power ... to require a person to enter into an enforceable undertaking. Similarly, a person cannot compel [ASIC] to accept an enforceable undertaking.⁶⁹

There is considerable flexibility in the drafting of undertakings and there is no limit to the civil penalty that may be imposed. ASIC can enforce compliance with the undertaking by seeking a court order.

ASIC has accepted enforceable undertakings in relation to alleged continuous disclosure failures. In 1998, an enforceable undertaking was made against Crown Ltd for an alleged failure to disclose accumulated operating losses in the 1998 financial year and receipt of a notice that the company was in breach of a debt to equity covenant in its casino licence.⁷⁰ In 2001, Pahth Telecommunications Ltd⁷¹ and Plexus International Ltd⁷² agreed to enforceable undertakings requiring disclosure audits following alleged failures to disclose revenue and profit downgrades or changes. Similarly, Uecomm agreed to review its continuous disclosure compliance proceedings after allegedly failing to continuously advise the market of its expected trading results.⁷³

In December 2006, ASIC accepted an enforceable undertaking from the Multiplex Group relating to its failure to immediately disclose a material change in profit on the Wembley National Stadium project in London on 2 February 2005. The undertaking secured a \$32 million compensation fund for

⁶⁵ An admission of liability is not required under s 1317DAJ(2)(b) of the *Corporations Act 2001* (Cth).

⁶⁶ The penalty amount under s 1317DAE varies according to the market capitalisation of the company and whether the company has a prior conviction under s 674(2) or 675(2).

⁶⁷ ASIC, n 59; ASIC, n 63; ASIC, n 64.

⁶⁸ ASIC, n 57.

⁶⁹ ASIC, *Enforceable Undertakings – An ASIC Guide* (March 2007) at [1.5]. The guide outlines (at [1.6]) the major differences between undertakings given to ASIC and a court.

⁷⁰ ASIC, *Media Release* (11 September 1998).

⁷¹ ASIC, "ASIC Accepts Disclosure Undertaking from Pahth Telecommunications Limited", *Media Release* (2 February 2001).

⁷² ASIC, "ASIC Accepts Disclosure Undertaking from Plexus International Limited", *Media Release 01/121* (5 April 2001).

⁷³ ASIC, "Uecomm to Undertake Disclosure Audit", *Media Release 02/379* (17 October 2002).



investors affected by the company's failure to meet its continuous disclosure obligations and provided for Multiplex's disclosure policies to be monitored by an independent expert.⁷⁴

An enforceable undertaking was also made against TZ Ltd for an alleged failure to disclose price-sensitive information to the ASX in September 2007.⁷⁵ The undertaking required the engagement of an external consultant to ensure disclosure in accordance with industry best practice.⁷⁶

Shareholder actions

No individual shareholder actions have succeeded to date.⁷⁷ In *Riley v Jubilee Mines NL* (2006) 59 ACSR 252 a shareholder plaintiff was initially awarded \$1.8 million in damages for losses resulting from a failure by WMC to comply with its continuous disclosure obligations. However, in 2009 this finding was overturned on appeal in *Jubilee Mines NL v Riley* (2009) 226 FLR 201; [2009] WASCA 62. Martin CJ held that "an announcement by Jubilee of all relevant information pertaining to the WMC drill hole data would not, or would not have been likely to, influence persons who commonly invest in securities in deciding whether or not to buy or sell its shares" (at [123]). In other words, the information did not satisfy the materiality requirement. Martin CJ also upheld other grounds for appeal relating to the content of the ASX announcement and the amount of damages awarded (at [114], [123], [129], [136]). Le Miere J concurred with the Chief Justice (at [199]). McClure J upheld the appeal on grounds of materiality and negligence (at [197]).

However, shareholders have received compensation through class actions alleging failures to continuously disclose. In late 2007, a class action against Telstra for a breach of its continuous disclosure requirements was settled for \$5 million.⁷⁸ The plaintiffs alleged that the company provided materially price-sensitive information at a private briefing to selected investors on 11 August 2005. The investors, who bought shares between 11 August and 7 September when Telstra made an announcement to the ASX on the briefing content, sought compensation on the basis that the share price was inflated during this period.

A few months later, settlement was reached on a class action against Aristocrat Leisure. The plaintiffs sought damages for investor losses resulting from misleading and deceptive conduct and a breach of the continuous disclosure obligations by the company relating to a series of profit forecasts provided to the market.⁷⁹ The action was settled for \$145 million,⁸⁰ with Aristocrat incurring a net cost after expenses and taxes of approximately \$40 million.⁸¹

More recently, smaller claims have been settled. For example, settlement was reached on 28 November 2008 on behalf of shareholders who purchased Downer EDI Ltd shares when Downer recognised revenue in respect of a disputed progress claim.⁸² Further disclosure-related class actions

⁷⁴ ASIC, "ASIC Accepts an Enforceable Undertaking from the Multiplex Group", *Media Release 06/443* (20 December 2006). ASIC pointed out that compensation was not guaranteed and the maximum penalty was \$1 million under the civil penalties regime.

⁷⁵ The company indicated that an announcement to the ASX about purchase orders for the company's technology was not made for six days because the orders were not considered to be price-sensitive information and consents under confidentiality agreements were sought prior to the announcement.

⁷⁶ ASIC, "ASIC Accepts Enforceable Undertaking from TZ Limited", *Media Release 08/149* (4 July 2008).

⁷⁷ Individuals have successfully sued for compensation under the misleading and deceptive conduct provisions. See eg *GPG (Australia Trading) Pty Ltd v GIO Australia Holdings Ltd* (2001) 117 FCR 23; 40 ACSR 252.

⁷⁸ ASX, *Court Approves Telstra Settlement* (Telstra Announcement, 13 December 2007); Moran S, "Telstra Settles Class Action", *The Australian* (Sydney) (12 November 2007).

⁷⁹ Sexton E, "Aristocrat Admits Overstating Profit", *Sydney Morning Herald* (Sydney) (5 October 2007); Sexton E, "All Eyes on Class Action", *Sydney Morning Herald* (Sydney) (5 October 2007).

⁸⁰ *Dorajay Pty Ltd v Aristocrat Leisure Ltd* (2008) 67 ACSR 569; [2008] FCA 1311.

⁸¹ Aristocrat Ltd, *Federal Court Class Action: Settlement Update* (ASX Announcement, 28 August 2008).

⁸² IMF (Australia) Ltd, *Company Update* (ASX Announcement, 28 November 2008); IMF (Australia) Ltd, *New Funding Agreement – Downer EDI Limited* (ASX Announcement, 8 May 2007).



are also proceeding, including suits against Multiplex,⁸³ AWB,⁸⁴ Centro Retail Ltd and Centro Properties Ltd,⁸⁵ ABC Learning,⁸⁶ Oz Minerals⁸⁷ and Transpacific Industries Group.⁸⁸

Continuous disclosure enforcement critique

As previously outlined, the ASX does not formally enforce the continuous disclosure Listing Rules. Instead, suspected breaches of the rules are referred to ASIC for action.

While some of the successful continuous disclosure actions were initiated as referrals from the ASX, all of the charges are based on the statutory provisions. This is important because the statutory provisions differ from ASX Listing Rule 3.1 with additional elements of intention and a requirement that the information is not generally available. The legal effects of these differences are still to be tested in the courts.

All of the successful continuous disclosure actions have occurred since 2000. This includes three successful court actions. However, the primary enforcement mechanism used by ASIC has been the infringement notice process. An ASIC Guide on the infringement notice scheme indicates that when determining whether use of the scheme is appropriate, ASIC considers all relevant facts and circumstances and has regard to the seriousness of the alleged breach.⁸⁹ In determining the seriousness of an alleged breach, ASIC has regard to a number of factors including:

- the impact of the alleged breach on the entity's securities including any change in the price of the securities and/or the number of securities traded;
- the materiality of the information;
- whether the information went to the heart of the entity's continued operations;
- whether the conduct giving rise to the alleged breach was negligent, reckless or deliberate;
- the adequacy of the entity's internal controls, and whether they were complied with;
- whether the entity sought and followed professional advice in relation to disclosure; and
- whether the entity took immediate steps to correct the failed disclosure.⁹⁰

Unfortunately, the links between these stated factors and the cases prosecuted under the infringement notice scheme and as court actions are not obvious. More detail in the ASIC media releases explaining the application of these factors would be beneficial for all parties.

The infringement notice scheme has been criticised by a range of parties.⁹¹ To date, no companies have contested the notices issued against them. The size of the current fines and the litigation and

⁸³ Chong F, "Court Paves Way on Multiplex Suit", *The Australian* (Sydney) (22 December 2007). The class action against Multiplex claims that the company failed to keep the market informed of cost and delay issues associated with the Wembley project and the likely effect on the company's profits. More specifically, Multiplex was aware of delays in the construction schedule and cost blowouts by August 2004, but did not inform the market of these until 2005.

⁸⁴ Chappell T, "Class Action Goes Ahead Against AWB", *The Age* (Melbourne) (14 April 2007). The plaintiffs in the action against AWB seek compensation for moneys lost as a result of AWB failing to continuously inform the market about its activities in Iraq and material facts that could reasonably be expected to have affected the AWB share price. The claimants seek an estimated \$25 million of direct losses as well as opportunity losses.

⁸⁵ IMF (Australia) Ltd, *IMF (Australia) Ltd 2008 Annual Report*. The claims against Centro Retail Ltd and Centro Properties allege the companies failed to keep the market informed of material information between 7 August 2007 and 15 February 2008 during which period the plaintiffs purchased securities.

⁸⁶ IMF (Australia) Ltd, *IMF (Australia) Ltd 2009 Annual Report*. This action alleges that ABC Learning failed to disclose information concerning its financial position to the ASX.

⁸⁷ IMF, n 86. This action alleges that material information was not disclosed to the ASX.

⁸⁸ Lindsay B, "IMF Funds Claims Against Waste-management Firm Transpacific Industries Group", *The Australian* (Sydney) (8 March 2010). This action alleges that Transpacific Industries Group breached its continuous disclosure obligations between 28 February 2008 and 16 February 2009.

⁸⁹ ASIC, n 52, pp 6-7.

⁹⁰ ASIC, n 52, pp 6-7.

⁹¹ See eg Baxt R, "The New 'Fining' Power for the Australian Securities and Investments Commission" in "Company Law and Securities" (2004) 32 ABLR 61 at 62; Welsh M, "Eleven Years On – An Examination of ASIC's Use of an Expanding Civil Penalty Regime" (2004) 17 AJCL 22.



reputational costs or risks involved in fighting an allegation in court are generally unwarranted when balanced against a fee of \$33,000-100,000 and no admission of liability.⁹² This is particularly so for the Tier 3 smaller capitalised companies subject to a fixed fine of \$33,000, the group of companies that have been the subject of most of the notices to date.

Finally, some shareholders have successfully gained compensation through class actions alleging failures to comply with the continuous disclosure obligations. The advent of successful class actions is likely to alter the corporate disclosure enforcement environment. However, the nature and extent of this change is still to be determined.⁹³ The risks or uncertainties for potential class action plaintiffs are significant and the number of scenarios that might lead to potential actions remains limited. Likely settlements need to be large enough to cover the procedural costs and risks associated with multi-party actions. In addition, key elements that need to be established for successful disclosure-related class actions in Australia are still uncertain. It is not yet clear

- how shareholder losses must be determined;
- whether the purchase of securities at an inflated price is sufficient to establish loss;
- on what basis investor reliance is assessed and whether market reliance is sufficient or reliance by individual shareholders needs to be proved;
- what causation links are required; and
- how materiality must be established.⁹⁴

The successful shareholder class actions to date have been settled to avoid long court actions focused on these elements.

Insider trading regulation

Enforcement of insider trading regulation

ASIC has successfully initiated insider trading prosecutions against 16 individuals or entities since the beginning of 2002.⁹⁵ Eight of these involved insider trading on non-public information concerning a proposed takeover or merger (O'Reilly, Panchal, Petsas, Miot, Frawley, Rivkin, Hannes and Doff),⁹⁶ four involved trading on company earnings information prior to its official release (McKay, Hall, Sweetman and Reddell),⁹⁷ one involved trading on private information about a gold mine project

⁹² See Langley R, "Over Three Years On: Time for Reconsideration of the Corporate Cop's Power to Issue Infringement Notices for Breaches of Continuous Disclosure" (2007) 25 C&SLJ 439 at 460. Pakchung confirmed that client companies believe that it is not worth fighting an infringement notice for the amount involved; Pakchung E (Partner, Blake Dawson), "Continuous Disclosure: Key Issues for Companies and Their Advisers", speech delivered at a seminar arranged by the Centre for Corporate Law and Securities Regulation, University of Melbourne, Sydney, 16 July 2008.

⁹³ A straw poll by IMF (Australia) Ltd of institutional investors found that the primary driver for involvement in disclosure-related class actions is the potential deterrent effect rather than the settlement moneys: Walker J (Managing Director, IMF (Australia) Ltd), "Continuous Disclosure: Key Issues for Companies and Their Advisers", speech delivered at a seminar arranged by the Centre for Corporate Law and Securities Regulation, University of Melbourne, Sydney, 16 July 2008.

⁹⁴ Walker, n 93.

⁹⁵ ASIC, "Sydney Man Enters Guilty Plea to Insider Trading Charges", *Media Release 10-72AD* (6 April 2010) (Hartman); ASIC, "New South Wales Man Pleads Guilty to Insider Trading", *Media Release 09-254AD* (15 December 2009) (Stephenson); ASIC, "Former Director of Lion Selection Pleads Guilty to Insider Trading", *Media Release 09-235* (23 November 2000) (O'Reilly); ASIC, "Former Company Secretary Pleads Guilty to Insider Trading", *Media Release 09-10* (4 February 2009) (Panchal); ASIC, "Melbourne Sharetrader Pleads Guilty to Insider Trading", *Media Release 07-303* (19 November 2007) (Woodland); ASIC, "Brisbane Research Analyst Pleads Guilty to Insider Trading Charge", *Media Release 07-154* (6 June 2007) (Reddell); *R v McKay* (2007) 61 ACSR 470 (McKay); *R v Hall (No 2)* [2005] NSWSC 890 (Hall); *Australian Securities and Investments Commission v Petsas* (2005) 23 ACLC 269 (Petsas and Miot); *R v Frawley* [2005] NSWSC 585 (Frawley); *R v Doff* (2005) 54 ACSR 200 (Doff); ASIC, "Former Harts Executive Director Jailed for Insider Trading", *Media Release 04-415* (17 December 2004) (Sweetman); *R v Rivkin* (2003) 45 ACSR 366 (Rivkin); ASIC, "Perth Man Sentenced on Insider Trading", *Media Release 03-240* (1 August 2003) (MacDermott); *R v Hannes* (2002) 173 FLR 1; 43 ACSR 508 (Hannes).

⁹⁶ ASIC, "Former Company Secretary Pleads Guilty to Insider Trading", *Media Release 09-10* (4 February 2009); *Australian Securities and Investments Commission v Petsas* (2005) 23 ACLC 269; *R v Frawley* [2005] NSWSC 585; *R v Rivkin* (2003) 45 ACSR 366; *R v Hannes* (2002) 173 FLR 1; 43 ACSR 508; *R v Doff* (2005) 54 ACSR 200.

⁹⁷ *R v Hall (No 2)* [2005] NSWSC 890; *R v McKay* (2007) 61 ACSR 470; ASIC, "Former Aristocrat Media Relations Consultant Pleads Guilty to Insider Trading", *Media Release 06-413* (28 November 2006); ASIC, "Former Harts Executive



(Woodland),⁹⁸ two related to insider trading prior to administration or liquidation (Stephenson and MacDermott)⁹⁹ and one involved an equities dealer with inside information about an asset management company's trading intentions (Hartman).¹⁰⁰ Of the four earnings-related cases, one involved trading prior to a major announcement (McKay),¹⁰¹ two involved directors trading prior to the announcement of an earnings downgrade (Hall and Sweetman),¹⁰² and one involved a research analyst trading on earnings news prior to its public release (Reddell).¹⁰³

Additional criminal insider trading charges have been alleged, with court hearings planned during 2010.¹⁰⁴

The only successful insider trading case initiated by ASIC under the civil penalty provisions is *Australian Securities and Investments Commission v Petsas* (2005) 23 ACLC 269.¹⁰⁵ This case involved a client relationship manager at a bank passing on confidential information to a client about a pending corporate merger. The defendants, Petsas and Miot, admitted they had contravened the insider trading provisions and were ordered to pay pecuniary penalties and compensation of the profits made.¹⁰⁶ It is not clear why civil penalties were sought in this particular case.

Insider trading enforcement critique

The ASIC record of successful prosecutions against approximately two individuals or entities a year since 2002 is higher than the levels achieved in the 1980s and 1990s.¹⁰⁷ However, these enforcement actions are likely to represent only the tip of the iceberg in terms of insider trading occurrences. In practice, detection and enforcement of insider trading is complex and requires considerable resources. Obtaining the evidence to establish the required elements for an insider trading action in Australia is difficult. "Piecing together an insider trading case can be a complex and painstaking process."¹⁰⁸ As the Securities Exchange Commission (SEC) in the United States and the Financial Services Authority (FSA) in the United Kingdom point out, most insiders take care to cover their tracks and cases must often be built on circumstantial inferences of suspected misconduct.¹⁰⁹ The SEC highlights that

Director Jailed for Insider Trading", *Media Release 04-415* (17 December 2004); ASIC, "Brisbane Research Analyst Pleads Guilty to Insider Trading Charge", *Media Release 07-154* (6 June 2007); ASIC, "Brisbane Research Analyst Sentenced on Insider Trading Charge", *Media Release 07-203* (26 July 2007).

⁹⁸ ASIC, "Melbourne Sharetrader Pleads Guilty to Insider Trading", *Media Release 07-303* (19 November 2007). Woodland pleaded guilty to one count of insider trading and one count of communicating inside information to other persons.

⁹⁹ ASIC, "New South Wales Man Pleads Guilty to Insider Trading", *Media Release 09-254AD* (15 December 2009); ASIC, "Perth Man Sentenced on Insider Trading", *Media Release 03-240* (1 August 2003).

¹⁰⁰ ASIC, "Sydney Man Enters Guilty Plea to Insider Trading Charges", *Media Release 10-72AD* (6 April 2010).

¹⁰¹ *R v McKay* (2007) 61 ACSR 470; ASIC, "Former Aristocrat Media Relations Consultant Pleads Guilty to Insider Trading", *Media Release 06-413* (28 November 2006).

¹⁰² *R v Hall (No 2)* [2005] NSWSC 890; ASIC, "Former Harts Executive Director Jailed for Insider Trading", *Media Release 04-415* (17 December 2004).

¹⁰³ ASIC, "Brisbane Research Analyst Pleads Guilty to Insider Trading Charge", *Media Release 07-154* (6 June 2007); ASIC, "Brisbane Research Analyst Sentenced on Insider Trading Charge", *Media Release 07-203* (26 July 2007).

¹⁰⁴ ASIC, "Former Director Charged with Insider Trading", *Media Release 10-108AD* (26 May 2010); ASIC, "Two NSW Men Charged with Insider Trading", *Media Release 10-25AD* (16 February 2010). *Media Release 10-108AD* states that one individual has been charged with 12 contraventions of s 1043A. *Media Release 10-25AD* indicates that 10 charges of insider trading have been laid against two individuals, with no pleas yet entered. Seven of these charges involve inside information on a pending takeover bid and three relate to inside information on pending earnings or other ASX announcements.

¹⁰⁵ See also *Australian Securities and Investments Commission v Vizard* (2005) 145 FCR 57; 54 ACSR 394.

¹⁰⁶ Both Petsas and Miot purchased call options in one of the merging companies resulting in significant realised profits.

¹⁰⁷ ASIC, "ASIC Releases Guidance on Directors' Share Trading", *Media Release 08-139* (27 June 2008); Overland J, "Two Steps Forward, One Step Back: Assessing Recent Developments in the Fight Against Insider Trading" (2006) 24 C&SLJ 207 at 210.

¹⁰⁸ Thomsen L (SEC), "Testimony Concerning Insider Trading Before the US Senate Committee on the Judiciary" (26 September 2006). See also Cole M (Director of Enforcement, Financial Services Authority), "Insider Dealing in the City", speech delivered at the London School of Economics, London, 17 March 2007.

¹⁰⁹ Thomsen, n 108; Cole, n 108.



“[b]uilding an insider trading case based on circumstantial evidence can be frustrating, risky and time-consuming”.¹¹⁰ The FSA indicates that the “two most common reasons for closing insider trading investigations are (i) the absence of evidence of links between the dealer and any insiders and (ii) the absence of evidence of the passage of inside information”.¹¹¹

The SEC, the FSA, a prior head of enforcement at the London Stock Exchange, and commentators suggest that the most significant insider trading problems and losses arise from systemic professional insider trading on either a transactional or longer-term basis.¹¹² The SEC highlights that individuals engaged in misconduct are increasingly “securities professionals, gatekeepers or high ranking corporate officials”.¹¹³ “[R]ecidivist insider trading cases” and “serial illegal trading” have become more common.¹¹⁴ In such cases, insider trading can be carried out by a number of defendants, involving multiple trades over a number of months, using sophisticated approaches.¹¹⁵ However, none of the insider trading actions in Australia to date have involved systemic professional insider trading.¹¹⁶

An individual’s response to the company disclosure and insider trading enforcement records depends on their interpretation of what constitutes a breach of the periodic disclosure, continuous disclosure and insider trading regimes. As might be expected, the regulatory, market participant and other stakeholder perspectives on listed company disclosure practices and enforcement differ. These views are outlined in the next part.

REGULATORY AND STAKEHOLDER COMMENTARY ON LISTED COMPANY DISCLOSURE

Regulators, under unprecedented pressure, face a range of demands, often contradictory in nature: be less intrusive – but more effective; be kindlier and gentler – but don’t let the bastards get away with anything; focus your efforts – but be consistent; process things quicker – and be more careful next time; deal with important issues – but don’t stray outside your statutory authority; be more responsive to the regulated community – but don’t get captured by industry.¹¹⁷

Selected content from a range of ASX and ASIC policy documents and speeches is provided to understand the regulatory aspirations and approaches to listed company disclosure matters. This material is presented on a chronological basis to reflect ongoing policy developments. Published market participant and stakeholder views on the listed company disclosure environment are then outlined.

ASX commentary

In 2002, Richard Humphrey, a prior managing director and chief executive officer of ASX, indicated in a speech entitled “Incentives to Integrity – ASX as a ‘For Profit’ Supervisor” to the Group of 100 that

[T]he listing rules cover a lot of detail but their central theme is disclosure. A fair, orderly and transparent market is one that is fully informed. So we are in the business of information – and in

¹¹⁰ Thomsen, n 108.

¹¹¹ Financial Services Authority, *Market Watch*, Issue 26 (April 2008) pp 6-7.

¹¹² ASIC, *Our Financial Markets: The Big Issues* (ASIC Summer School 2008 Report, 18-20 February 2008) p 90; Cole, n 108; Rider B, *Insider Trading* (1983) p 73; Thomsen, n 108; Thomsen L (SEC), “Opening Remarks”, speech delivered at the Securities Industry and Financial Markets Association Regulatory Symposium on Insider Trading, 19 May 2008.

¹¹³ Thomsen, n 112.

¹¹⁴ Thomsen, n 112.

¹¹⁵ Thomsen, n 112. See also Cole, n 108.

¹¹⁶ Systemic professional insider trading involves organised and ongoing sharing or trading of private information by multiple professional parties. See eg SEC, *SEC Charges Wall Street Lawyers and Traders in \$20 Million Insider Trading Scheme* (5 November 2009), <http://www.sec.gov/news/press/2009/2009-236.htm> viewed 17 March 2010.

¹¹⁷ Sparrow M, *The Regulatory Craft* (Brookings Institution Press, Washington DC, 2000) p 17.



particular, we are in the continuous disclosure business: ensuring that listed companies are keeping the market informed by providing material information under Listing Rule 3.1.¹¹⁸

In 2003, Maurice Newman, a prior Chairman of ASX, stated in an address on “The Markets and Investors: Is There Too Much Disclosure?” to the CEDA Copland Program that the “integrity, efficiency and international standing of Australia’s capital markets is to a large extent dependent on a sound system of disclosure”.¹¹⁹ He went on to say that

[e]nsuring that our continuous disclosure regime remains at the forefront of world’s best practice is something that ASX is strongly committed to.

There is no doubt, that today’s market has much greater transparency. There is also a greater demand indeed a thirst for information. The advent of discount brokers, advances in internet technology, the introduction of open interface trading technology have all created an information flow which is constantly challenging whether the market is fully informed.¹²⁰

In 2006, Newman addressed the AIRA Conference on “The Perfect Storm: Managing Investor Relations in a Volatile Market”. He indicated that

[a]s a market operator licensed by the Australian Government, ASX is obliged to provide a market of integrity – one that is fair, orderly and transparent. A market of integrity ensures a level-playing field, inspiring confidence among all users and, by doing so, reducing risk and driving down the cost of capital ... In Australia, we are about sunlight and transparency.¹²¹

In 2009, Eric Mayne spoke to AIRA on “Governance & Supervision”. He concluded that

[d]isclosure and the “informed shareholder” go hand in hand. Shareholders would only be able to exercise their rights in a responsible, informed and considered way only if companies uphold the highest standards of disclosure and transparency. It is not about boiler plate reporting nor is it about tick-a-box compliance – the key is quality reporting.¹²²

ASIC commentary

An ASIC publication entitled *Better Disclosure for Investors: Guidance Rules* was released in 2000.¹²³ The final guidance rules incorporate 10 broad principles for companies to consider in the development of their disclosure policies. These principles are described as practical steps for companies to take to ensure they meet the letter and spirit of the continuous disclosure regulation. Principle 6 states that “[p]rice sensitive information must be publicly released through the stock exchange before disclosing it to analysts or others outside the company”.¹²⁴ Companies are encouraged

- to have written policies and procedures on information disclosure;¹²⁵
- to nominate a senior officer to oversee and coordinate disclosure;¹²⁶
- to restrict the number of officers authorised to speak on behalf of the company;¹²⁷

¹¹⁸ Humphry R (Managing Director and Chief Executive Officer ASX), “Incentives to Integrity – ASX as a “For Profit” Supervisor”, speech delivered at the Group of 100, 27 November 2002, p 5.

¹¹⁹ Newman M (Chairman, ASX), “The Markets and Investors: Is There Too Much Disclosure?”, speech delivered at the CEDA Copland Program, 8 August 2003, p 2.

¹²⁰ Newman, n 119, pp 5-6.

¹²¹ Newman M (Chairman, ASX), “The Perfect Storm: Managing Investor Relations in a Volatile Market”, speech delivered to AIRA Conference, 23 November 2006, pp 2, 4.

¹²² Mayne E (Chief Supervision Officer, ASX), “Governance & Supervision”, speech delivered at the AIRA Conference, 2 December 2009, pp 26-27.

¹²³ ASIC, *Better Disclosure for Investors: Guidance Rules* (2000).

¹²⁴ ASIC, n 123, Principle 6.

¹²⁵ ASIC, n 123, Principle 1.

¹²⁶ ASIC, n 123, Principle 3.

¹²⁷ ASIC, n 123, Principle 4.



- to monitor disclosures;¹²⁸
- to develop procedures in relation to rumours, leaks and inadvertent disclosures;¹²⁹
- to review private discussions with analysts for inadvertent disclosure;¹³⁰
- to take care that responses to analysts' questions include only information that has been released through the stock exchange;
- to confine comments on analysts' financial projections to errors in factual information and underlying assumptions;¹³¹ and
- to use current technology to give investors better access to information.¹³²

The suggested way to manage earnings expectations is to publicly disclose a forecast earnings range, with any changes in these expectations publicly announced prior to any comment to a third party.¹³³ The principles or measures in the paper are not mandatory. Companies remain free to develop disclosure policies that meet their particular needs and circumstances.

In 2008, Belinda Gibson, an ASIC Commissioner, made a speech on "Disclosure and the Role of ASX and ASIC" at the Listed Companies Conference.¹³⁴ Gibson indicated that the key elements of the disclosure regime are:

- disclosure of price-sensitive information to the market in a timely fashion;
- announcements that are not false, misleading or deceptive; and
- announcements that are clear, accurate and complete.¹³⁵

She defined "clear announcements" as information contained in a market release that is factual and expressed in an objective and clear manner; "complete announcements" as documents that can be read as a whole without reference to other documents to locate price-sensitive information; and "accurate announcements" as disclosure of information that is factually correct, easily understandable, with due prominence to positive and negative information.¹³⁶

In a presentation to the Company Directors Conference in June 2009 on "Regulators At the Forefront of Change", Gibson stated that the big focus is on restoring confidence in the capital markets. She indicated that this requires the promotion of market integrity – "the attributes of transparency and fairness that set our market above many".¹³⁷

The ASIC annual report for 2007-2008 outlined the following organisational priorities:

- a focus on retail investors;
- capital market integrity;
- developing our capital markets;
- helping small and medium business;
- lifting operational effectiveness; and
- a strategic review.

An ASIC-commissioned review on retail investors was highlighted within the first category.¹³⁸ Under the capital market integrity priority, ASIC reviewed the accounts of 325 entities, including 28

¹²⁸ ASIC, n 123, Principle 5.

¹²⁹ ASIC, n 123, Principle 7.

¹³⁰ ASIC, n 123, Principle 8.

¹³¹ ASIC, n 123, Principles 9 and 10.

¹³² ASIC, n 123, Principle 2.

¹³³ ASIC, n 123, Principle 10.

¹³⁴ Gibson B (ASIC Commissioner), "Disclosure and the Role of ASX and ASIC", speech delivered at the Listed Companies Conference, 26 March 2008.

¹³⁵ Gibson, n 134, p 6.

¹³⁶ Gibson, n 134, pp 11-12.

¹³⁷ Gibson B (ASIC Commissioner), "Regulators at the Forefront of Change", speech delivered at the Company Directors Conference, 11 June 2009, p 6.

¹³⁸ ASIC, *ASIC Annual Report 2007-2008*, p 16.



companies listed on the ASX 200, and found a generally positive level of compliance with accounting standards.¹³⁹ Other company disclosure issues discussed in the report included the referral processes between the ASX and ASIC relating to insider trading and other market abuses; an investigation into trading on rumours; the provision of guidance on disclosure of margin loan and stock lending arrangements;¹⁴⁰ and the establishment of policy guidance and standards for unlisted and undated debenture prospectuses and advertising.¹⁴¹ The major enforcement actions during the period were outlined, some of which involved company disclosure issues such as Westpoint and James Hardie.¹⁴² The strategic review process was assisted by the engagement of management consultants McKinsey & Co.¹⁴³

The ASIC annual report for 2008-2009 confirmed the six organisational priorities.¹⁴⁴ Actions to support retail investors included:

- a focus on recovery of funds associated with failed investments such as Westpoint and Opes Prime;¹⁴⁵
- improving product disclosure relating to unlisted mortgage schemes and unlisted property funds, superannuation, agricultural management investment schemes, and banking services;¹⁴⁶ and
- supporting financial literacy in the community.¹⁴⁷

Work to promote the integrity of the market included increased investigative work to pursue market manipulation and insider trading,¹⁴⁸ an inquiry into rumourtrage,¹⁴⁹ and good practice guidelines for website publication.¹⁵⁰ The major enforcement actions during the period included James Hardie, Opes Prime, Westpoint, Fortescue Metals, AWB, and Chartwell Enterprises.¹⁵¹

The ASIC submission to the Company and Markets Advisory Committee (CAMAC) review on *Aspects of Market Integrity* acknowledged that there may be real and perceived fairness issues “in relation to the current practice of private briefings with well-connected analysts potentially having access to more detailed and higher quality discussion with management”.¹⁵² In a speech to the Australian Investor Relations Association in December 2009, Gibson, an ASIC Commissioner, admitted that “[p]erhaps the most informative material ... is provided at the investor analyst briefings that usually occur when the annual and half yearly results are announced”.¹⁵³ She noted that the “analysts’ briefings to investors released with the annual results are often more informative” than the

¹³⁹ ASIC, n 138, pp 20-21.

¹⁴⁰ ASIC, n 138, p 7.

¹⁴¹ ASIC, n 138, p 16. ASIC estimated that retail and self-managed superannuation fund investors held \$34 billion in debentures, of which \$8 billion was unlisted unrated debentures.

¹⁴² ASIC, n 138, pp 14-15. Ongoing investigations into issues associated with the collapses of Opes Prime Stockbroking Ltd, Fincorp and Australian Capital Reserve were noted.

¹⁴³ ASIC, n 138, p 30.

¹⁴⁴ ASIC, n 20, pp 4-5.

¹⁴⁵ ASIC, n 20, p 20.

¹⁴⁶ ASIC, n 20, pp 22-23.

¹⁴⁷ ASIC, n 20, pp 24-25.

¹⁴⁸ ASIC, n 20, pp 28-29.

¹⁴⁹ ASIC, n 20, p 29.

¹⁵⁰ ASIC, n 20, p 29.

¹⁵¹ ASIC, n 20, pp 16-17. Ongoing investigations into Fincorp and Storm Financial were also noted.

¹⁵² ASIC, *ASIC's Submission on CAMAC's Issues Paper: Aspects of Market Integrity* (March 2009) p 20.

¹⁵³ Gibson B (ASIC Commissioner), “Playing by the Rules: A New Regulatory Environment is Changing the Way That Corporations Relate to Investors and the Finance Community”, speech delivered at the AIRA Annual Conference 2009, 2 December 2009, p 9.



annual reports.¹⁵⁴ The briefing material is “usually approved by the board ... [It] is usually prospective and looks over the company’s business model and analyses the various segments.”¹⁵⁵

Gibson also highlighted that

good disclosure is an essential attribute of a market “with integrity” ... [including] disclosure of information about an investment in the initial offering material and also ongoing disclosure of current information to the market. It is both the quality of information as well as the quantity of information which is crucial in determining whether disclosure advances the transparency and fairness of a market.¹⁵⁶

In 2010, Gibson spoke on the topic “Working in a Regulated Environment” to the Law Society of Western Australia Summer School. She highlighted that the current disclosure regulatory model can be traced back to the Wallis Inquiry Report in 1997 and the general view that “markets only need ... quality disclosure and enforcement of proper market conduct for their operation”.¹⁵⁷ Gibson suggested that ASIC’s role is

to oversee the quality of information that is provided, but it is not tasked with, nor resourced for, monitoring every transaction that occurs, and every disclosure document that is issued (only some of which must be lodged with ASIC). We can, and do, establish good practices. We do conduct market surveillance of disclosure practices and we must take action if we identify illegal practices.¹⁵⁸

Gibson explained that

[t]he *Corporations Act* sets out a comprehensive disclosure regime from the IPO [initial public offering], through the annual reports, to the material that shareholders must be given when there is a company transforming event, such as a takeover or related party dealing.¹⁵⁹

She described the continuous disclosure regime as sitting over these formal documents and as a regime that, rather than being prescriptive, “requires inclusion of ‘everything investors and their advisers reasonably require to make an informed assessment of the investment’”.¹⁶⁰ She defined “clear, concise and effective” documentation to mean that

[d]ocuments must be readable – if they are lengthy, there must be a clear road map to enable the readers to select the information they need to make a sensible investment decision. They must be understandable. The content must be clear and relevant to the investment decision at hand. The risk must be put up front and in one place.¹⁶¹

Stakeholder commentary

General criticisms made against company and securities regulators include that:

- the organisations are too reactive and not proactive enough;¹⁶²
- actions are taken too late;¹⁶³
- responses tend to be crises or politically based;¹⁶⁴

¹⁵⁴ Gibson, n 153, p 11.

¹⁵⁵ Gibson, n 153, pp 8-9.

¹⁵⁶ Gibson, n 153, p 5.

¹⁵⁷ Gibson B (ASIC Commissioner), “Working In a Regulated Environment”, speech delivered at the Law Society of Western Australia Summer School, 26 February 2010, p 2.

¹⁵⁸ Gibson, n 157, p 3.

¹⁵⁹ Gibson, n 157, p 4.

¹⁶⁰ Gibson, n 157, p 5.

¹⁶¹ Gibson, n 157, p 5.

¹⁶² Allen Consulting Group (Allen), *ASIC Stakeholder Survey* (April 2008) pp 18, 34; Commonwealth, Parliamentary Joint Committee on Corporations and Financial Services, *Inquiry into Financial Products and Services in Australia* (November 2009) p 98.

¹⁶³ Commonwealth, Parliamentary Joint Committee on Corporations and Financial Services, n 162, p 98.

¹⁶⁴ See Dooley M, “Comment from an Enforcement Perspective” (1999) 50 *Case Western Reserve Law Review* 319 at 323.



- weaker targets are selected;¹⁶⁵
- smaller companies are treated relatively more harshly than larger entities;¹⁶⁶ and
- the management are captured by their most powerful constituents.

In an ASIC stakeholder survey in 2008,

- 50% of the business sample and 42% of the consumers indicated that ASIC concentrates on easy targets for enforcement actions;
- 40% of the business respondents and 57% of the consumers indicated that ASIC was too cautious about taking enforcement action;¹⁶⁷ and
- only 30% of the business respondents and 31% of the consumers thought that fraud, dishonesty and misconduct are likely to be found and punished in Australia.¹⁶⁸

Even some of the largest Australian institutional investors have complained about significant levels of insider trading and information asymmetry. Morgan, the investment director of 452 Capital and a well-respected fund manager in Australia, suggested there “is a lot of questionable trading going on and it is in some ways, out of hand ... 80 per cent of announcements from large companies [are] associated with some sort of unusual trading beforehand”.¹⁶⁹ Sisson, the managing director of Balanced Equity Management Pty Ltd, agreed, indicating that “[a]gain and again you see price movements that are unexplained”.¹⁷⁰ Several commentators have suggested there are clear trading patterns of very high share trading volumes and profits made prior to announcements of “takeover bids, capital raisings and other price sensitive news” in Australia.¹⁷¹ Hunt, the chairman of Caliburn, indicated that “[u]nusual price movements ahead of takeover announcements and capital raisings in this market are frustratingly commonplace”.¹⁷² He suggested that the incidence of insider trading is “unacceptably high” and that a change in regulatory approach is required.¹⁷³ Seabrook, an executive director of Gresham Investment Partners, suggested there “are some outrageous practices at the larger end of the market where leaks occur”.¹⁷⁴

Scholarly studies on company disclosure in Australia support the stakeholder and participant views.¹⁷⁵ In addition, Gibson, an ASIC Commissioner, acknowledged at the end of 2009 that Australian listed company processes around confidential information are suboptimal and below the standards adopted in overseas markets. She described the environment for obtaining company information as “pushy” and indicated that some investors even frequent bars that company executives are known to use.¹⁷⁶ The combined evidence suggests that a bold and focused regulatory approach is needed governing listed company disclosure matters. A proposed regulatory framework is outlined and discussed below.

¹⁶⁵ Allen, n 162, pp 18, 34. See also Cox J and Thomas R, “SEC Enforcement Heuristics: An Empirical Inquiry” (2003) 53 Duke LJ 737 at 778.

¹⁶⁶ Bird et al, n 2, p 108. See also Cox and Thomas, n 165.

¹⁶⁷ Allen, n 162, pp 18, 34.

¹⁶⁸ Allen, n 162, pp 14, 30.

¹⁶⁹ Newman G, “Praise for ASIC Surveillance Boost”, *The Australian* (Sydney) (12 December 2006) p 17.

¹⁷⁰ ASIC, n 112, p 83.

¹⁷¹ Elias D, “Insiders Profit in Murky Business”, *The Age* (Melbourne) (6 August 2005); Maiden M, “Marriage of Exchanges a Licence to Print Monopoly Money”, *The Age* (Melbourne) (25 May 2006) p 10.

¹⁷² West M, “Insider Trading Still on the Rise”, *Sydney Morning Herald* (Sydney) (20 February 2008) p 19.

¹⁷³ West, n 172.

¹⁷⁴ ASIC, n 112, p 82.

¹⁷⁵ See n 7.

¹⁷⁶ Gibson B, “Responsible Handling of Market Information – Inside Information and Rumours”, speech delivered at a University of Sydney Faculty of Economics and Business Conference on Aspects of Market Integrity – Where Next?, Sydney, 1 October 2009.



A BOLD AND EFFECTIVE COMPANY DISCLOSURE REGULATORY FRAMEWORK

The current author argues that the regulatory framework in Australia for listed company disclosure should:

- be risk-based, with clearly identified long-term goals and priorities;
- have a primary focus on prevention; and
- promote evidentiary-based decision-making.

Adoption of this framework would result in a greater emphasis on compliance with, and where necessary enforcement of, the periodic and continuous disclosure obligations.

What is a risk-based regulatory approach?

All regulatory organisations should have long-term goals and priorities. A systemic risk-based approach also requires ongoing assessment of the potential risks and consequences associated with each of the goals. The accepted measurement of risk encompasses the probability or likelihood of an identified adverse event and the consequences of the event occurring.¹⁷⁷ Policies and practices must then be established to counter or mitigate these risks. To the extent that a regulator has clearly identified long-term goals and priorities and is using a systemic risk-based approach, it is well positioned to counter criticisms that it is responding to the latest crisis, political pressure or vested interests.

An example of a risk-based regulatory approach is provided in the Financial Services Authority (FSA) documents. Section 1.3.1 of the *FSA Handbook* states that its risk assessment of companies is based on the extent to which they pose risks to the regulatory objectives. The measurement of risks encompasses the impact of such risks were they to crystallise and the probability of their doing so.¹⁷⁸ The FSA identified timely disclosure of takeover bids and price-sensitive company announcements as high-risk scenarios with a material impact on investors. Consequently, it commissions ongoing annual independent empirical market cleanliness studies to monitor the possible extent to which trading may be occurring on an informed basis ahead of these announcements.¹⁷⁹

A guide on how ASIC works indicates that a risk-based approach is used.¹⁸⁰ However, the guide provides no detail on what a risk-based approach means or how the processes work. Importantly, a number of the submissions from large financial institutions to the recent parliamentary inquiry into financial products and services (FPS Inquiry) argued that ASIC should adopt a more risk-based or risk-weighted approach to monitoring and supervision.¹⁸¹ Although ASIC responded that it “adopts a risk based methodology to assist with which disclosure documents it should review”,¹⁸² no details on the adopted methodology could be found.

In the ASIC stakeholder survey, 41% of business respondents indicated that ASIC makes clear what it is doing and why, 32% thought it communicates well with business, and 34% suggested that ASIC is open and accountable.¹⁸³ However, only 24% of the business respondents thought ASIC provides a real opportunity for consumers to contribute to the development of policy and priorities,¹⁸⁴ and 21% that there is a real opportunity for business to contribute to policy and priority

¹⁷⁷ Risk Management Institution of Australasia, *Definition of Risk*, <http://www.rmia.org.au/Standards/IndustryStandards/tabid/85/Default.aspx> viewed 18 March 2010.

¹⁷⁸ United Kingdom, *FSA Handbook*, Supervision s 1.3, “The FSA’s Risk Based Approach to Supervision”.

¹⁷⁹ See eg Dubow B and Monteiro N, “Measuring Market Cleanliness”, *Financial Services Authority Occasional Paper Series* 23 (March 2006); Monteiro N, Zaman Q and Leitterstorf S, “Updated Measurement of Market Cleanliness”, *Financial Services Authority Occasional Paper Series* 25 (March 2007).

¹⁸⁰ ASIC, *ASIC: A Guide to How We Work* (July 2006) p 6.

¹⁸¹ See eg Commonwealth, Parliamentary Joint Committee on Corporations and Financial Services, n 162, p 108.

¹⁸² Commonwealth, Parliamentary Joint Committee on Corporations and Financial Services, n 162, p 98.

¹⁸³ Allen, n 162, p 16.

¹⁸⁴ ASIC, n 112, pp 21, 23.



developments.¹⁸⁵ This survey feedback suggests that ASIC is communicating its strategies, priorities and processes reasonably effectively, but it could do more.

The regulatory goals and priorities of ASIC in relation to disclosure issues could be articulated and explained more effectively. At this stage, it is not clear how the goals and priorities expounded in the annual reports and other regulatory material are translated into resource allocation decisions. The Act includes disclosure regulation relating to financial reports and audits in Ch 2M; takeovers in Ch 6; continuous disclosure in Ch 6CA; fundraising in Ch 6D; and financial services and products in Ch 7. Within this spectrum, there has been significant parliamentary and regulatory focus on disclosure issues relating to financial services.¹⁸⁶ In addition, ASIC has provided policy guidance on disclosure associated with unlisted debenture and mortgage schemes,¹⁸⁷ and has indicated that it intends providing further guidance on the readability of prospectuses.¹⁸⁸ These are all important and worthwhile projects. However, a risk-based regulatory approach requires a primary focus on the periodic and continuous disclosure obligations, particularly disclosures from the largest companies.¹⁸⁹

A 2008 ASX survey indicated that nearly seven million Australians, or 41% of the adult population, participated in the Australian share market.¹⁹⁰ Within this sample, an estimated six million Australian adults, or 36% of the adult population, invested in ASX listed shares directly;¹⁹¹ a level of direct or retail investor participation that was close to the highest within global stock markets.¹⁹² And as Cooper, the prior Deputy Chairman of ASIC, indicated at the ASIC Summer School in 2008, “[w]e’re nearly all retail investors” in Australia because of compulsory superannuation, with only around 20% of consumers using financial advisers.¹⁹³ Most of the information provided by Australian corporates to these direct or retail investors is disseminated as periodic and continuous disclosures through the ASX. The levels of investments, both generally and by retail investors in particular, into IPOs and the unlisted markets are not as significant as those made into listed company securities.¹⁹⁴

No material could be found on the risk-based approach (if any) used by the ASX to company disclosure issues. Importantly, it is retail investors who are in the most vulnerable position under the co-regulatory structure, as these investors are in a weak position to persuade listed companies to comply with the disclosure Listing Rules and are the most likely to be uninformed when the rules are not enforced. This position will not change under the multiple operator reforms. The Australian co-regulatory model is not used overseas. In the United Kingdom, the FSA rather than the London Stock Exchange is responsible for enforcement of the Listing Rules governing quarterly, half yearly and preliminary final reporting.¹⁹⁵ Similarly, in the United States, the SEC actively monitors and

¹⁸⁵ Allen, n 162, p 21.

¹⁸⁶ Commonwealth, Parliamentary Joint Committee on Corporations and Financial Services, n 162.

¹⁸⁷ ASIC, n 138, p 16.

¹⁸⁸ Gibson, n 153, p 10.

¹⁸⁹ See Cox and Thomas, n 165.

¹⁹⁰ ASX, *2008 Australian Share Ownership Study* (2009) p 3.

¹⁹¹ ASX, n 190, p 3.

¹⁹² ASX, n 190, p 34. See also ASX, *International Share Ownership* (September 2005) p 2.

¹⁹³ ASIC, n 112, p 5.

¹⁹⁴ See eg ASIC, n 138, p 16.

¹⁹⁵ *Financial Services and Markets Act 2000* (UK), ss 72, 91; United Kingdom Listing Authority, Listing Rule 9.7A.1. See also Gadinis S and Jackson H, “Markets as Regulators: A Survey” (2007) 80 *Southern California Law Review* 1239 at 1282, 1298.



enforces all of the reporting regulation including the quarterly (10-Q) and preliminary final reports (10-K).¹⁹⁶ The SEC also enforces the regulation on management, discussion and analysis within the periodic disclosures.¹⁹⁷

Identification of disclosure risks should be informed by market consultation to understand what conduct is of most concern and the likely impact of the conduct across the market. Institutional practitioners suggest the listed company disclosure activity of most concern is trading based on private information concerning pending takeover bids, capital raisings and earnings releases.¹⁹⁸ When parties have private (inside or selectively disclosed) information on a pending takeover bid, capital raising or earnings news, these parties continue to trade until the security price reflects the relevant information. During this period, the uninformed parties (those without the private information) that rationally trade on the basis of fundamental security valuations incorporating information within the public arena often sustain significant trading losses (or lost opportunity gains). The number of parties involved and the potential losses are likely to be greatest when the securities traded are issued by companies with the largest market capitalisations. The market participants most likely to be uninformed are retail investors. Yet a noticeable gap in the ASIC guide on consultation processes used is the lack of public forums and policy access difficulties for retail investors.¹⁹⁹

As previously outlined, insider trading and continuous disclosure actions in Australia encompass the areas identified as high risk by market practitioners. The continuous disclosure and insider trading actions in Australia that can be categorised as takeover bid related include Promina, Rio Tinto, O'Reilly, Panchal, Petsas, Miot, Frawley, Rivkin, Hannes and Doff. One continuous disclosure action involving capital raisings is the infringement notice issued against QRSciences. Continuous disclosure and insider trading actions concerning earnings releases include Southcorp, SDI, Pahth Telecommunications, Plexus International Ltd, Uecomm, Multiplex, McKay, Hall, Sweetman and Reddell. Some of the remaining actions could also be labelled as earnings-related given the inherent broad nature of this category. A view on the appropriateness of this level of enforcement depends on the perspective of the individual making the judgment. A range of views on listed company disclosure practices and enforcement were outlined above.

What does a greater emphasis on prevention mean within the company disclosure arena?

Company and securities regulators must establish cultures and processes that

- enable enforcement action, including litigation, against illegal conduct;
- deter or prevent prohibited conduct; and
- actively encourage best practice market behaviour.

For the purposes of this article, the latter two categories are called “preventative measures” or measures that “seek to foster a ‘climate of compliance’”.²⁰⁰ Enforcement actions, including litigation,

¹⁹⁶ See accounting and auditing enforcement actions on the United States Securities and Exchange Commission (SEC) website, <http://www.sec.gov/divisions/enforce/friactions.shtml> viewed 1 March 2008. This website provides details on many actions taken by the SEC relating to the content of quarterly reports (10-Qs) and preliminary final reports (10-Ks).

¹⁹⁷ See eg *Re Sony Corp and Sumio Sano* (Release No 40305, 5 August 1998), <http://www.sec.gov/litigation/admin/3440305.txt> viewed 27 April 2010; *Re Bank of Boston Corp* (Administrative Proceeding File No 3-8270, 1995), <http://www.sec.gov/litigation/aljdec/id81bpm.txt> viewed 27 April 2010.

¹⁹⁸ ASIC, n 112, pp 82-83.

¹⁹⁹ Retail investor response to Australian policy discussion is typically limited to the Australian Shareholders Association. Most retail investors are probably not aware of ongoing policy consultations. Notably, in the United Kingdom, the FSA has public forums. Similarly, the minutes of many SEC meetings are available in the public arena: see <http://www.sec.gov/news/webcasts.shtml> viewed 15 March 2010. Shareholders' suggestions are also actively sought for the Investor Advisory Committee: see <http://www.sec.gov/spotlight/investoradvisorycommittee.shtml> viewed 15 March 2010. In addition, the SEC website maintains a section on its home page that seeks “public” online comment on its proposals: see <http://www.sec.gov> viewed 15 March 2010. For example, nearly 6,000 retail investors made online submissions to the Regulation Fair Disclosure proposal: see <http://www.sec.gov/spotlight/insidertrading.shtml> viewed 18 March 2010.

²⁰⁰ Cameron A, “Enforcement, Getting the Regulatory Mix Right” (1994) 4 AJCL Lexis 121 at [3].



are essential within any regulatory framework. However, given the limited moneys and manpower available to regulators, decisions on the allocation of resources between preventative measures and enforcement actions, and to specific enforcement cases, are critical.

Regulatory measures that might be defined as preventative within the company disclosure arena include:

- the setting of best practice standards;
- the issuance of policy guidance;
- clarification on acceptable and prohibited conduct;
- investor education;
- the running of test cases; and
- policy advice.

To its credit, ASIC is currently using all of these measures.²⁰¹ For instance, ASIC recently reviewed practices around the handling of confidential company information. It found these were below the standards adopted in overseas markets and in response, will publish best practice standards on the handling of confidential information.²⁰² Similarly, the ASX issues best practice standards and guidelines, compliance training is provided, and various educational programs are conducted to promote compliance with the Listing Rules.²⁰³ The ASX Markets Supervision 2009 Annual Report also states that the compliance unit supervisory approach is “pro-active and forward-looking ... This ‘preventative compliance’ strategy seeks to promote open communication and assist participants achieve compliance.”²⁰⁴

Nevertheless, stakeholder feedback suggests that further debate on the roles, responsibilities and operating frameworks of the ASX and ASIC are warranted. The ASX has been criticised for inadequate responses to failed broker settlements, short selling, insider trading and market manipulation; failures to monitor and enforce director trades; the promotion of high-risk investment products to retail investors; allowing poison pills to managers of subsidiary listed funds; and failures to enforce the Listing Rules.²⁰⁵ Some market participants suggest that complaints to the ASX about disclosure breaches are not acted upon.²⁰⁶ Morgan, a well-respected fund manager, even suggests that it is not good enough for ASIC to give the ASX a clean bill of health given what has been happening in the industry.²⁰⁷ In the ASIC stakeholder survey, 37% of business respondents indicated that ASIC is more collaborative than adversarial and 36% thought the organisation is not overly legalistic. However, only 26% of business respondents thought that ASIC focuses on outcomes rather than process,²⁰⁸ and 44% of business respondents and 35% of consumer respondents indicated that ASIC focuses too much on punishment and not enough on prevention.²⁰⁹

Similarly, ASIC was criticised in the FPS Inquiry for not being sufficiently proactive. The Q Invest submission suggested that “ASIC should strive for a primarily preventive function, through greater monitoring, supervision and enforcement of obligations”.²¹⁰ The submission from the Investment and Financial Services Association suggested that “ASIC’s approach of acting on

²⁰¹ ASIC, n 20; ASIC, n 138.

²⁰² ASIC, *Handling Confidential Information, Consultation Paper 128* (December 2009). The value of these standards may be limited if they are merely voluntary standards that are not monitored or enforced.

²⁰³ ASX, n 34, pp 14, 22.

²⁰⁴ ASX, n 34, p 14.

²⁰⁵ Saulwick and Yeates, n 36; Durie J, “ASX Showdown”, *The Australian* (Melbourne) (10 September 2008); Collins M, “ASX Director Target of Activists”, *The Australian* (Melbourne) (10 September 2008); McIlwraith I, “At ASX, the Buck Stops Nowhere”, *The Age* (Melbourne) (25 September 2008).

²⁰⁶ Saulwick and Yeates, n 36.

²⁰⁷ Saulwick and Yeates, n 36.

²⁰⁸ ASIC, n 112, p 21; Allen, n 162, p 20.

²⁰⁹ Allen, n 162, pp 18, 34.

²¹⁰ Commonwealth, Parliamentary Joint Committee on Corporations and Financial Services, n 162, p 97.



complaints had been too reactive ... They really need to toughen up on the proactive, doing things earlier.”²¹¹ Similarly, CPA Australia stated that “ASIC currently appears to employ a reactive rather than proactive approach to enforcing the regulation”.²¹² The Inquiry Committee also indicated that ASIC had been too slow in some of its enforcement.²¹³ In response, ASIC indicated that its “power to take action ahead of non-compliance is limited”.²¹⁴

What does evidence-based regulatory decision-making entail?

Evidence-based regulatory decision-making is simply regulatory decisions supported by evidence. The evidence available to regulators can be generated, gathered and assessed from a broad range of sources both within and outside of the organisational structure. External evidence should encompass as broad a range of sources as possible, including scholarly research, commissioned research, media reports, parliamentary inquiries, law reform forums, consultation with a broad spectrum of participants, online debate, and public forums.

The 2008 and 2009 annual reports suggest that ASIC has improved its feedback and evidence-gathering processes. An experienced external advisory panel has been established, there are annual summer schools, an independent consultancy firm was asked to conduct a stakeholder survey, and a limited retail investor survey was commissioned. These are commendable efforts. The 2008 report indicated there would be increased investment in research and analysis²¹⁵ and the 2009 report confirmed “significant investment in market research and economic analysis to better identify emerging issues and monitor real-time changes in the markets”.²¹⁶ Nevertheless, the extent to which the current ASIC approach to company disclosure issues is evidentiary-based may be limited.

The outlined ASIC commentary and enforcement actions suggest that the ASIC review of the periodic disclosure regime is focused solely or predominantly on annual reports. The audits and enforcement actions to date have been founded on whether the financial statements within annual reports were in accordance with accounting standards. Further, Gibson, an ASIC Commissioner, recently suggested that the management discussion and analysis in annual reports is “sometimes so formulaic that it communicates very little to the reader”.²¹⁷ However, a regulatory focus limited to the annual reports is flawed. Australian annual reports are released up to four months after a financial year-end, by which time the reported information is no longer timely.

Regulatory reviews of empirical continuous disclosure issues also appear to be limited. The ASX and ASIC confirm that the continuous disclosure regime is intended to encompass disclosure of everything that investors require to make a well-informed assessment of an investment. The stated goal is for clear, concise and effective documentation, defined as announcements that are complete, readable and understandable with clear upfront risk analysis. The ASX Guidance Note 8 provides the most comprehensive guidelines on Listing Rule 3.1 including guidance on the disclosure of earnings expectations. The guidance in Note 8 recommending the provision of management forecasts is reiterated in the “Better Disclosure” document. However, no regulatory research or evidence could be found on:

- the nature and scope of information that investors need to make well-informed investment decisions;
- the extent to which this information is provided within the periodic and continuous disclosures;
- whether the information provided under these regimes is clear, concise and effective;

²¹¹ Commonwealth, Parliamentary Joint Committee on Corporations and Financial Services, n 162, p 98.

²¹² Commonwealth, Parliamentary Joint Committee on Corporations and Financial Services, n 162, p 109.

²¹³ Commonwealth, Parliamentary Joint Committee on Corporations and Financial Services, n 162, p 98.

²¹⁴ Commonwealth, Parliamentary Joint Committee on Corporations and Financial Services, n 162, p 97.

²¹⁵ ASIC, n 138, p 8.

²¹⁶ ASIC, n 20, p 8.

²¹⁷ Gibson B (ASIC Commissioner), “Facilitating Capital Raising for Corporate Australia”, speech delivered at the Corporate Finance World Australia 2009 Conference, 10 November 2009, p 8.



- whether risk disclosures are included; and
- the extent to which companies are following the Note 8 guidance on disclosure of earnings expectations.

Finally, ASIC made a series of comments on disclosures made through company briefings. It conceded that the material provided at company briefings is perhaps the most informative provided to investors and that inequities may arise when this material is provided selectively. Yet the Commission submission to the CAMAC review concluded that:

- the briefings provide a *net efficiency benefit*,²¹⁸ “provided the law is complied with”,²¹⁹
- access to these briefings should remain discretionary because “[c]ompanies are best placed to determine what is the most effective and efficient disclosure mechanism in their particular circumstances”,²²⁰ and
- “it is not practicable or appropriate to require all private briefings to be recorded”.²²¹

The ASX submission on company briefings indicated that it was not aware of any new developments that suggested there had been “an increase in the extent of non-compliance with continuous disclosure obligations or insider trading”.²²² Thus, it queried whether a market failure problem had been identified which required addressing.²²³

CONCLUSION

The ASX and ASIC consistently indicate that their roles and responsibilities include the establishment of policies and measures to promote investor confidence, transparency, fairness, equal access and the provision of clear, concise and effective information. However, these aspirations are difficult to reconcile with:

- the lack of regulatory focus on the periodic and continuous disclosure regimes; and
- regulatory policies that allow listed companies to disseminate what ASIC concedes as “perhaps the most informative company material provided by companies to investors”²²⁴ on a discretionary basis behind closed doors.

The ASIC stakeholder feedback, participant views, and scholarly studies on company disclosure and enforcement suggest that a bold and effective regulatory framework is needed. The current author proposes a framework that:

- is risk-based, with clearly identified long-term goals and priorities;
- has a primary focus on prevention; and
- promotes evidentiary-based decision-making.

Adoption of this framework would result in a greater emphasis on compliance with, and where necessary enforcement of, the periodic and continuous disclosure obligations. First, a significant proportion of Australian adults have an investment in ASX listed securities, either indirectly or directly. Company information provided under the periodic and continuous disclosure regimes constitutes the largest body of information provided by Australian corporates to investors and other stakeholders. Secondly, regulatory measures designed to ensure better compliance with the periodic and continuous disclosure regimes (and to thereby reduce potential future incidences of insider trading) are likely to ultimately represent a lower risk approach and a more efficient use of resources than a primary focus on insider trading litigation. Such preventative measures could be expected to cost less, achieve better disclosure outcomes, and result in less detrimental effects on investors and

²¹⁸ Emphasis added. No definition of net efficiency is given in the ASIC submission and no evidence or argument provided to support the conclusion that closed briefings enhance net efficiency.

²¹⁹ ASIC, n 152, p 20.

²²⁰ ASIC, n 152, p 21.

²²¹ ASIC, n 152, p 22. No argument is provided to support the conclusion that recordings are impracticable or inappropriate.

²²² ASX, *Aspects of Market Integrity: Issues Paper* (11 March 2009) p 4.

²²³ ASX, n 222.

²²⁴ ASIC, n 152, p 11.



other stakeholders over the long run. In practice, most cases of insider trading arise when companies fail to comply with their periodic and continuous disclosure obligations. A failure by companies to periodically or continuously disclose, or selective disclosure by companies to a small group of investors, often affects a significant proportion of investors in the relevant company with large amounts of money involved. Thirdly, detection and litigation of insider trading cases is generally more difficult and requires greater regulatory resources than enforcement actions relating to the periodic or continuous disclosure provisions.

However, a major difficulty with a regulatory emphasis on compliance with, and enforcement of, the periodic and continuous disclosure obligations are the uncertainties around what these obligations currently encompass. ASX Listing Rule 3.1 requiring continuous disclosure when a listed Australian company becomes aware of materially price-sensitive information is arguably the most important provision within the Australian company disclosure framework. Similarly, the preliminary final report provides Australian investors with the most comprehensive periodic information on a timely basis. Yet there is no case law on Listing Rule 3.1 or the periodic disclosure Listing Rules as stand alone regulation.

ASIC is sometimes criticised for a policy based on achieving a high litigation success rate.²²⁵ Such a policy is an efficient use of taxpayer funds but inevitably results in a failure to prosecute cases with less certain outcomes.²²⁶ However, the 2009 annual report states that ASIC is “taking on the difficult cases, where, whether we win or lose, we use the case, consistent with the principles of a model litigant, to test important principles which clarify the law on issues in the public interest (eg insider trading)”.²²⁷ Baxt argues that ASIC should run more test cases and that legislation should only be revised if these test cases throw up deficiencies in the current legislation.²²⁸ This argument aptly applies to corporate disclosure regulation, particularly the continuous disclosure provisions. Given the critical importance of the continuous disclosure regime within the broader company disclosure framework, the ASX and ASIC are encouraged to initiate test cases to better define these obligations and to determine whether the existing regulation is achieving the policy goals of market fairness and economic efficiency.

²²⁵ Wilson S, “ASIC a Puppy in Need of Bite”, *The Australian* (Sydney) (18 October 2005) p 22.

²²⁶ Buffini F, “DPP Wants Reforms to Catch Directors”, *Australian Financial Review* (Sydney) (16 September 2005) p 55; Sexton E, “Action Stations”, *Sydney Morning Herald* (Sydney) (13-14 October 2007) pp 39, 44.

²²⁷ ASIC, n 20, p 3.

²²⁸ Baxt B, “Aspects of Market Integrity – What Next?”, paper delivered at University of Sydney Faculty of Economics and Business Conference on Aspects of Market Integrity – Where Next?, Sydney, 1 October 2009.

