FEDERAL COURT OF AUSTRALIA

Australian Securities and Investments Commission v Drake (No 2)

[2016] FCA 1552

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| File number: | QUD 596 of 2014 |
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| Judge: | **EDELMAN J** |
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| Date of judgment: | 23 December 2016 |
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| Catchwords: | **CORPORATIONS** – directors’ duties – s 180(1) of the *Corporations Act* *2001* (Cth) – onus of proof in relation to proving alternative courses of action in s 180 of the *Corporations Act*  **CORPORATIONS** – directors’ duties – s 181 and s 182 of the *Corporations Act* – test for proving improper purpose – test for causation  **TRUSTS AND TRUSTEES** – breach of trust – nature of trustee’s duty of care – whether trust deed can exclude equitable obligation or obligation in s 22 of the *Trusts Act 1973* (Qld) to act as a prudent trustee |
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| Legislation: | *Corporations Act 2001* (Cth) ss 180(1), 180(2), 181(1), 181(1)(b), 181(2), 182(1), 182(1)(a), 1317S, 1318(1)  *Evidence Act 1994* (Cth) s 140  *Trustee Act 1925* (ACT) s 14A(1)  *Acts Interpretation Act 1954* (Qld) s 14B(3)(b)  *Trusts Act 1973* (Qld) ss 4(1), 4(4), 5, 10, 20, 21, 22, 22(1), 22(1)(a), 23(3), 24, 24(1), 24(1)(a), 30B, 30B(a), 31, 60, 61, 65, 79, 111; Div 1, Pts 3, 4, 5, 6, 7, 10  *Trusts (Investments) Amendment Act 1999* (Qld) s 5  *Trusts (Investments) Amendment Bill 1999* (Qld)  *Trustee Act 1925* (NSW) s 14A(1)  *Trustee Act* *1907* (NT) s 6(1)  *Trustee Act 1936* (SA) s 7(1)  *Trustee Act 1898* (Tas) s 7(1)  *Trustee Act 1958* (Vic) s 6(1)  *Trustees Act 1962* (WA) s 18(1)  *Trustee Act 1925* (UK) ss 3(1)(ii), 31, 69(2) |
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| Cases cited: | *Agricultural and Rural Finance Pty Ltd v Gardiner* [2008] HCA 57; (2008) 238 CLR 570  *Agricultural Land Management Ltd v Jackson (No 2)* [2014] WASC 102; (2014) 48 WAR 1  *Amaca Pty Ltd v Booth* [2011] HCA 53; (2011) 246 CLR 36  *Armitage v Nurse* [1998] Ch 241  *Australian Iron & Steel Pty Ltd Limited v Krstevski* [1973] HCA 42; (1973) 128 CLR 666  *Australian Safeway Stores Pty Ltd v Zaluzna* [1987] HCA 7;(1987) 162 CLR 479  *Australian Securities and Investments Commission v Adler* [2002] NSWSC 171; (2002) 168 FLR 253  *Australian Securities and Investments Commission v Cassimatis (No 8)* [2016] FCA 1023  *Australian Securities and Investments Commission v Citigroup Global Markets Australia Pty Ltd (No 4)* [2007] FCA 963; (2007) 160 FCR 35  *Australian Securities and Investments Commission v Fortescue Metals Group Ltd (No 5)* (2009) 264 ALR 201  *Australian Securities Commission v AS Nominees Limited* (1995) 62 FCR 504  *Backwell IXL Pty Ltd v Robert Grant Hogg* [1998] VSC 155  *Breen v Williams* [1996] HCA 57; (1996) 186 CLR 71  *Briginshaw v Briginshaw* [1938] HCA 34; (1938) 60 CLR 336  *Brookfield Multiplex Ltd v Owners Corporation Strata Plan 61288* [2014] HCA 36; (2014) 254 CLR 185  *Byrnes v Kendle* [2011] HCA 26; (2011) 243 CLR 253  *Chan v Zacharia* [1984] HCA 36; (1984) 154 CLR 178  *Commissioner of Stamps (South Australia) v Telegraph Investment Company Pty Limited* (1995) 184 CLR 453  *Cowan v Scargill* [1985] Ch 270  *Crossman v Sheahan* [2016] NSWCA 200  *Currie v Dempsey* (1967) 69 SR (NSW) 116  *Doyle v Australian Securities and* *Investments Commission* [2005] HCA 78; (2005) 227 CLR 18  *Electricity Generation Corporation v Woodside Energy Ltd* [2014] HCA 7; (2014) 251 CLR 640  *Fouche v Superannuation Fund Board* [1952] HCA 1; (1952) 88 CLR 609  *Gardiner v Agricultural and Rural Finance Pty Ltd* [2007] NSWCA 235  *Graham Barclay Oysters Pty Ltd v Ryan* [2002] HCA 54; (2002) 211 CLR 540  *Green v Wildern Pty Ltd* [2005] WASC 83  *Hackshaw v Shaw* [1984] HCA 84;(1984) 155 CLR 614  *Harvard College v Amory*, 26 Mass (9 Pick) 446 (1830)  *Hedley Byrne & Co. Ltd v Heller & Partners Ltd* [1964] AC 465  *Henderson v Merrett Syndicates Ltd and Ors* [1995] 2 AC 145  *Hospital Products Ltd v United States Surgical Corporation* [1984] HCA 64; (1984) 156 CLR 41  *In re Chapman* [1896] 2 Ch 763  *In re Erskine’s Settlement Trusts* [1971] 1 WLR 162  *In the matter of Colorado Products Pty Ltd (in prov liq)* [2014] NSWSC 789  *Inland Revenue Commissioners v Bernstein* [1960] Ch 444  *Inland Revenue Commissioners v Bernstein* [1961] Ch 399  *John Pfeiffer Pty Ltd v Canny* [1981] HCA 52; (1981) 148 CLR 218  *Jones v Dunkel* [1959] HCA 8; (1959) 101 CLR 298  *Kelly v Cooper* [1993] AC 205  *Kennedy Taylor (Vic) Pty Ltd v Baulderstone Hornibrook Pty Ltd* [2000] VSC 43  *Kenyon, Sons & Craven Ltd v Baxter Hoare & Co. Ltd* [1971] 1 WLR 519  *Learoyd v Whiteley* (1887) 12 App Cas 727  *Leerac Pty Ltd v Fay* [2008] NSWSC 1082  *Lochgelly Iron & Coal Co v McMullan* [1934] AC 1  *Mahmood v State of Western Australia* [2008] HCA 1; (2008) 232 CLR 397  *Motor Vehicles Insurance Ltd v Woodlawn Capital Pty Ltd* [2014] NSWSC 1503; (2014) 290 FLR 285  *Nagle v Rottnest Island Authority* [1993] HCA 76; (1993) 177 CLR 423  *Neill v NSW Fresh Food and Ice Pty Limited* (1963) 108 CLR 362  *Nelson v John Lysaght (Australia) Limited* [1975] HCA 9; (1975) 132 CLR 201  *Nestle v National Westminster Bank Plc* [1993] 1 WLR 1260  *New South Wales v Fahy* [2007] HCA 20; (2007) 232 CLR 486  *Oriental Commercial Bank v Savin* (1873) LR 16 Eq 203  *Pacific Brands Sport & Leisure Pty Ltd v Underworks Pty Ltd* [2005] FCA 288  *Parker v Tucker* [2010] FCA 263; (2010) 77 ACSR 525  *Permanent Building Society (in liq) v Wheeler* (1994) 11 WAR 187  *Photo Production Ltd v Securicor Transport Ltd* [1980] AC 827  *Rankine v Rankine* (unreported, Sup Ct, QLD, de Jersey CJ, 3 April 1998)  *Re Miller’s Deed Trusts* (1978) 75 LSG 454  *Re Ransome* [1957] Ch 348  *Re Turner’s Will Trusts* [1937] Ch 15  *Re Whiteley* (1886) 33 Ch D 347  *Roman Catholic Church Trustees for the Diocese of Canberra and Goulburn v Hadba* [2005] HCA 31; (2005) 221 CLR 161  *Romeo v Conservation Commission of the Northern Territory* [1998] HCA 5; (1998) 192 CLR 431  *RPS v The Queen* [2000] HCA 3; (2000) 199 CLR 620  *Segelov v Ernst & Young Services Pty Ltd* [2015] NSWCA 156; (2015) 89 NSWLR 431  *Speight v Gaunt* (1883) 22 Ch D 727  *Speight v Gaunt* (1883) 9 App Cas 1  *Spread Trustee Co Ltd v Hutcheson* [2012] 2 AC 194  *Swain v Waverley Municipal Council* [2005] HCA 4; (2005) 220 CLR 517  *Swick Nominees Pty Ltd v LeRoi International Inc (No 2)* [2015] WASCA 35; (2015) 48 WAR 376  *Target Holdings Ltd v Redferns (A Firm)* [1996] AC 421  *The Commonwealth of Australia v Cornwell* [2007] HCA 16; (2007) 229 CLR 519  *Trade and Transport Incorporated v Iino Kaiun Kaisha Ltd* [1973] 1 WLR 210  *Tszyu v Fightvision Pty Ltd* [2001] NSWCA 103; (2001) 104 IR 225  *Vozza v Tooth & Co Limited* [1964] HCA 29; (1964) 112 CLR 316  *Vrisakis v Australian Securities Commission* (1993) 9 WAR 395  *Weissensteiner v The Queen* [1993] HCA 65; (1993) 178 CLR 217  *Westpac Banking Corporation v Bell Group Ltd (in liq) (No 3)* [2012] WASCA 157; (2012) 44 WAR 1  *Whitehouse v Carlton Hotel Pty Ltd* [1987] HCA 11; (1987) 162 CLR 285  *Wilkins v Hogg* (1861) 31 LJ Ch 41  *Wingecarribee v Lehman Bro*s [2012] FCA 1028; (2012) 301 ALR 1  *Wyong Shire Council v Shirt* [1980] HCA 12; (1980) 146 CLR 40  *Youyang Pty Ltd v Minter Ellison Morris Fletcher* [2003] HCA 15; (2003) 212 CLR 484  Dawson F, “Fundamental Breach of Contract” (1975) 91 LQR 380  Heydon JD and Leeming MJ, *Jacobs’ Law of Trusts in Australia* (8th ed, LexisNexis Butterworths Australia, 2016)  Queensland Law Reform Commission, *A Report of the Law Reform Commission on the Law Relating to Trusts, Trustees, Settled Land and Charities* (QLRC 8, 16 June 1971)  Queensland Law Reform Commission, *A Review of the Trusts Act 1973 (Qld): Interim Report* (WP No 71, June 2013)  Queensland Law Reform Commission, *A Review of the Trusts Act 1973: Report* (Report No 71, December 2013)  The American Law Institute, *Restatement of the Law Third, Trusts Vol 3* (American Law Institute Publishers, 2007) |
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| Date of hearing: | 29-31 August, 1-2, 5-9, 13, 23 September, and 27-28 October 2016 |
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| Date of last submissions: | 1 November 2016 (Second and Third Respondents) |
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| Registry: | Queensland |
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| Division: | General Division |
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| National Practice Area: | Commercial and Corporations |
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| Sub-area: | Corporations and Corporate Insolvency |
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| Category: | Catchwords |
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| Number of paragraphs: | 543 |
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| Counsel for the First Respondent: | Mr RJPS Jackson QC and Ms A Nicholas |
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| Solicitor for the First Respondent: | Bartley Cohen |
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| Solicitor for the Second and Third Respondents: | James Conomos Lawyers |
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| Counsel for the Fourth Respondent: | Mr KA Barlow QC and Mr G Coveney |
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| Solicitor for the Fourth Respondent: | HW Litigation |
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| Counsel for the Fifth Respondent: | Mr D Clothier QC and Mr D Piggott |
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| Solicitor for the Fifth Respondent: | Tucker & Cowen |

ORDERS

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|  | | QUD 596 of 2014 |
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| BETWEEN: | AUSTRALIAN SECURITIES AND INVESTMENTS COMMISSION  Applicant | |
| AND: | PETER CHARLES DRAKE (and others named in the Schedule)  First Respondent | |

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| JUDGE: | EDELMAN J |
| DATE OF ORDER: | 23 DECEMBER 2016 |

THE COURT ORDERS THAT:

1. The application against each of the first, second, and third respondents be dismissed.
2. The applicant pay the costs of the first, second, and third respondents to be taxed if not agreed.

Note: Entry of orders is dealt with in Rule 39.32 of the *Federal Court Rules 2011*.

REASONS FOR JUDGMENT

EDELMAN J:

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# TABLE OF KEY PERSONNEL AND ABBREVIATIONS

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| **ASIC** | Australian Securities and Investments Commission. The applicant in this proceeding. |
| **BARNETT, Luke** | Development Manager of the Maddison Estate development at LMIM with a background in mechanical engineering and land development. A member of the PAM team since November 2011. He reported to Mr Tickner and, once Mr Tickner left, to Mr Fischer and Mr King. He resigned on 22 May 2013. |
| **DARCY, Lisa** | Initially the fifth respondent. Part way through the trial, ASIC abandoned its case against Ms Darcy. She was Executive Director of LMIM from September 2003 until her resignation on 21 June 2012. Ms Darcy was CFO until recruiting and training Mr Fischer for the role in March 2008. She was also the chair of the MPF Credit Committee and a member of the LMIM board. Whilst at LMIM, Ms Darcy worked closely in the process of instructing legal, signing off on serviceability analysis for all fund loans (including MPF loans), and assisting with Mr Drake’s personal finances. She worked closely with Mr Drake, and was the main contact with Ernst & Young. |
| **DRAKE, Peter** | The first respondent. The Executive Director, sole owner and CEO of LMIM. Chairman of the LMIM board, and a voting member of the MPF Credit Committee. Sole director, secretary and shareholder of LMIM Asset Management Pty Ltd. Sole director and secretary of Maddison Estate. Ultimate beneficial ownership of the shares in Maddison Estate was held by the corporate trustee (LMIM Asset Management Pty Ltd, of which Mr Drake was the sole director and secretary) of a discretionary trust, the beneficiaries of which included Mr Drake. From April 2010, director of Coomera Ridge Pty Ltd. |
| **ERNST & YOUNG** | The auditors of all of LMIM’s funds except for the MPF. Ernst & Young and WPIAS worked with the PAM team and the finance team to look at the feasibilities of development projects. Ernst & Young produced a draft and then final report concerning Maddison Estate, commissioned by Suncorp, in July and then September 2011. |
| **ESTATE MASTER** | A proprietary software program used by the PAM team to prepare feasibility reports. Estate Master required the input of numerous variables and various assumptions such as escalation rates from which it calculated a net present value of the development. |
| **FISCHER, Grant** | An accountant with qualifications in commerce. The CFO of LMIM from March 2008 to August 2012, where he was responsible for the overall financial management of LMIM and its managed investment schemes. As CFO, Mr Fischer had a finance team working for him comprising between five and 11 staff. He reported directly to Mr Drake.  Mr Fischer was an Executive Director of LMIM from 14 March 2012 to 12 August 2012, and a member of the MPF Credit Committee. Thereafter, he worked as a consultant to LMIM until January 2013. He only attended one formal LMIM board meeting as a director (on 13 July 2012). |
| **KING, Scott** | An acquisition manager with qualifications in property valuation and economics, and applied finance and investment. Employed as a Development Manager in the PAM team from November 2010 to February 2013. Worked on several projects at LMIM, including ad-hoc involvement in the Maddison Estate development. His involvement included assisting Mr Barnett with the feasibility review in June 2012 after the departure of Ms Scott, at the request of Mr Drake and Mr Fischer. Mr King was a voting member of the MPF Credit Committee. |
| **KINGSTON, Bronwyn** | Employed in LMIM as a paralegal in the commercial lending department, and then in the PAM team. Her role included the provision of organisational and administrative support to the MPF Credit Committee. |
| **KOP, David** | Employed by Suncorp as a Relationship Manager in the property finance department. This position entailed helping Suncorp resolve its portfolio of “non-core” loans via repayment when Suncorp decided to exit the property loan market. Mr Kop was responsible for the management of the Suncorp loan to Maddison Estate from September 2011 to 2013. Mr Kop’s main contacts at LMIM were Mr Tickner and Mr Fischer. |
| **KURBATOFF, Mark** | Employed by Suncorp as a Relationship Manager in the development finance section. Mr Kurbatoff was responsible for the management of the Suncorp loan to Maddison Estate from December 2010 to September 2011 (when it was transferred to Mr Kop). |
| **LANDMARK WHITE** | Commissioned by Young Land Corporation and Suncorp to conduct valuations of Pimpama Land. The valuations were contained in reports dated 6 March 2008 and 28 July 2008. |
| **LM COOMERA PTY LTD** | LM Coomera Pty Ltd was the predecessor company of Maddison Estate. It was incorporated on 14 September 2007. |
| **LMA** | LM Administration Pty Ltd. Incorporated in 1992. Trustee of the LMA Trust. LMA entered into an agreement on 1 July 2005 with LMIM whereby LMA agreed to provide LMIM with services for LMIM’s funds management operations (including the employment of staff). |
| **LMA TRUST** | LM Administration Trust, created on 30 June 2003. LMA was the trustee of the LMA Trust. |
| **LM GROUP** | The LM Group was comprised of various related companies, including LMIM, Oceanboard Pty Ltd, LMA, Maddison Estate, LM Coomera Holdings Pty Ltd and LMIM Asset Management Pty Ltd. LMIM was the principal company of the LM Group. |
| **LMIM** | LM Investment Management Ltd. LMIM was a responsible entity for a number of managed investment schemes, and, in particular, the responsible entity and the trustee of the MPF. Mr Drake was the Executive Director, sole owner and CEO of LMIM.  LMIM was made up of a number of teams, including the PAM team (led by Mr Tickner), the finance team (led by Ms Darcy and then Mr Fischer), the marketing team (led by Ms Mulder), the global operations team (led by Ms Phillips), the portfolio management team (led by Mr van der Hoven and Mr Petrik), the foreign exchange team (led by Mr van der Hoven), and the in-house legal team. |
| **LMIM ASSET MANAGEMENT PTY LTD** | LMIM Asset Management Pty Ltd was incorporated on 14 September 2007. Mr Drake was its sole director, secretary and shareholder. It held ultimate beneficial ownership of the shares in Maddison Estate. |
| **LOUGH, Caroline** | Paralegal in the PAM team. |
| **MADDISON ESTATE** **DEVELOPMENT** | A large residential and recreational development located at Pimpama on the Gold Coast. The plan for Maddison Estate was to sell blocks of vacant land via community title in a large setting which would consist of high tech recreational venues and a town centre. Maddison Estate was previously known as LM Coomera, One, and Arrowtown. |
| **MADDISON ESTATE** | Maddison Estate Pty Ltd. A company related to LMIM who was the receiver of the loan that is the subject of these proceedings. The loan was for a large development project on the Gold Coast (see **Maddison Estate**). |
| **McDONALD, Greg** | Worked for LMIM as a Development Manager. He was a member of the PAM team, and worked on the Maddison Estate development. |
| **McCALLUM, Ann** | Employed in LMIM as a loans analyst in the PAM team. She was a member of the MPF Credit Committee. |
| **MPF** | The Managed Performance Fund. The MPF was established around 2002 as an unregistered managed investment scheme which operated as a unit trust. LMIM was the trustee of the fund. The MPF was only open to investment by wholesale or sophisticated investors. On 1 November 2011, the MPF information memorandum described it as having 90% of its assets invested in Australian commercial loans. The largest of the commercial loans, $142 million, was a single loan of more than half of the size of the fund.  The MPF was governed by the **MPF Constitution**. |
| **MPF Credit Committee** | A committee of the MPF which assessed loans proposed as investments for the MPF and considered any required action for existing loans. The committee met as required and sometimes informally. Meetings were often preceded by an emailed information synopsis.  On 19 May 2011, the committee was comprised of Ms Darcy (the chair), Mr Drake, Mr van der Hoven, Mr Tickner, Ms Mulder, Mr King, Mr McDonald, and Mr Fischer. By 2013, there were six voting members: Ms Mulder, Mr Drake, Mr van der Hoven, Ms Phillips, Mr King, and Mr Petrik.  The MPF Credit Committee was alternatively described as “CC”, “Credit Committee”, “MPF Credit Committee”, “MPF Investment Committee” and “MPF Investment CC”. |
| **MPF Constitution** | A deed between LMIM and the members of the MPF as they were constituted from time to time, which governed the MPF. The original MPF Constitution was dated December 2001. Variations were made periodically until October 2012. |
| **MULDER, Francene** | The second respondent. Employed by LMA from 1999. She was appointed as Executive Director and Marketing Director of LMIM in September 2006. Not as actively involved in the asset management side of MPF as other directors. Her involvement was more with client communication. Member of the MPF Credit Committee. |
| **PAM team** | The Property Asset Management (**PAM**) team which assisted LMIM. The team was headed by Mr Tickner, although Mr Fischer took over for three to four months after Mr Tickner retired as director in 2012. It had at most 25 staff with lending, development, town planning and general property skills. The PAM team was divided into three parts, individually responsible for: (i) identifying investment opportunities for the funds; (ii) assessing the assets and working to progress the projects; and (iii) administering the loans. The PAM team reported to the various committees, including the MPF Credit Committee.  In early 2011 to late 2012 the PAM team included Mr Tickner (as the head of the team), Mr Fischer, Mr Parker, Mr King, Mr Barnett, Mr McDonald, Mr Young, Ms Scott, Ms Chalmers, Ms Kingston, Ms Lough, and Ms McCallum. |
| **PARKER, Michael** | A Commercial Lending Manager in the PAM team. He was responsible for considering and obtaining funding opportunities, proposing them to credit committees, and (if the MPF Credit Committee agreed) contracting with and lending money to developers. Mr Parker was a member of the MPF Credit Committee. |
| **PETRIK, Andrew** | Employed in LMIM as Portfolio Manager in about 2009, taking over from Mr van der Hoven. He was a member of the MPF Credit Committee. |
| **PHILLIPS, Katherine** | Employed in the London office of LMIM until around 2011. She was an Executive Director of LMIM from 13 July 2012 to 20 June 2013, as well as head of global operations. Ms Phillips liaised with all LM offices and staff on a regular basis in relation to fund and business operational issues, and was also heavily involved in marketing. She was a voting member of MPF Credit Committee. |
| **SUNCORP** | Suncorp-Metway Limited. Holder of a first mortgage in relation to its loan for the Maddison Estate development. |
| **SCOTT, Katherine** | An accountant with approximately 18 years’ experience. Initially employed by Young Land Pty Ltd, then by LMA from January 2010 to May 2012. She worked in the finance team as a management accountant, and then later moved into the PAM team. |
| **TICKNER, Simon** | Initially the fourth respondent. Part way through the trial, ASIC abandoned its case against Mr Tickner. He worked for LMIM from 2002 as Business Development Manager. He was a member of the MPF Credit Committee, Executive Director of LMIM and head of the PAM team from September 2008 until he resigned on 13 July 2012. After his resignation, Mr Tickner was re-employed as a consultant for the PAM team. |
| **VAN DER HOVEN, Eghard** | The third respondent. Employed by LMA in 2003 as Portfolio Manager until around 2009 or 2010. Executive Director of LMIM from 22 June 2006 until 30 June 2013. A voting member of the MPF Credit Committee. |
| **WILLIAMS, Reginald** | Accountant. Managing partner of WPIAS. Worked on the WPIAS audit of the MPF financial statements in 2011 and 2012 and attended the meeting on 17 July 2012. |
| **WOOLLEY, Hugh** | Funds investment manager with over 31 years’ relevant financial services experience. Called by ASIC to give expert evidence. |
| **WPIAS** | Williams Partners Independent Audit Specialists. Accountants with specialised experience in building, construction, aged care and the audit of managed funds. Specialised knowledge of the Gold Coast property market. Engaged to audit the financial reports for the MPF for the years ended 30 June 2011 and 30 June 2012. WPIAS’ main contact from LMIM was Mr Fischer. |
| **YOUNG, David** | From November 2006 to April 2010, Mr Young was a director of Young Land Corporation Pty Ltd and Coomera Ridge Pty Ltd. From April 2010 until January 2012, he was a consultant on the Maddison Estate Development and worked in the PAM team. |

# Introduction

1. This trial concerned allegations by ASIC of breach of directors’ duties against five directors of a corporate trustee of a managed investment scheme. This introduction explains, in very broad outline, the reasons why I have dismissed ASIC’s case in its entirety. The reason why ASIC’s case is dismissed requires an appreciation of how ASIC ran its case, and the rejection of the entirety of the evidence of the principal expert called by ASIC.
2. ASIC’s case, in very broad outline, was concerned with an investment made by LM Investment Management Ltd (**LMIM**) as a responsible entity and trustee of numerous funds. LMIM had offices all over the world from which its funds were marketed. Its main office was on the Gold Coast.
3. One of LMIM’s funds was an unregistered managed investment scheme established in 2002, the LM Managed Performance Fund (the **MPF**). This was an aggressive fund with reasonably high risk. It was aimed at wholesale and sophisticated investors who accessed the fund through financial planners. As one of the former directors of LMIM explained, the MPF was a fund that could have a number of assets including second mortgages and direct property interests. It had a very broad investment mandate. It was marketed as an aggressive fund with higher returns than what was on offer from some other funds including other funds managed by LMIM. After the global financial crisis, some of the MPF loans required a focus upon development because the borrowers in those loans had begun to default on their mortgages. The MPF investments were marketed through means which included information memoranda. The sophisticated investors would have been immediately aware from the information memoranda and investment application that the fund was far from low risk. For instance, on 1 November 2011, the MPF information memorandum described the MPF as having 90.75% of its assets invested in Australian commercial loans. The largest of the commercial loans, $142 million, was a single loan of more than half of the size of the fund. That is the loan which is the subject of these proceedings.
4. The particular investment by LMIM (as trustee for the MPF) with which this case is concerned was a loan made to a related company which became called **Maddison Estate**. The loan, secured by two mortgages, was for a large development project on the Gold Coast (the **Maddison Estate development**). The interest rate was eventually set at 25%. The interest rate was designed to ensure that Maddison Estate, which was a special purpose vehicle, did not obtain any of the profit from the development. ASIC did not allege that the loan involved any breach of duty although ASIC alleged that it was, in effect, a disguised equity participation in a development.
5. The loan from LMIM to Maddison Estate (the **Maddison Estate loan**) was made in November 2007 with an initial limit of $40 million. In 2008 the limit of the loan was increased to $58 million. In 2009 the limit was increased to $70 million. In 2010 it was increased to $95 million. In 2011 it was increased to $115 million. Again in 2011 it was increased to $180 million. Then, in August 2012, it was increased to $280 million (the **August 2012 Variation**).
6. aSIC did not allege that the loan was imprudent. Nor did ASIC allege that the loan was made by the directors of LMIM without care and diligence. Nor did ASIC allege that there was any breach of duty arising from the approval of the loan variations in 2008, 2009 or 2010. After the conclusion of the evidence, ASIC also abandoned any allegation of breach arising from the loan variation in 2011, and therefore abandoned the whole of its case against the fourth and fifth respondents, Mr Tickner and Ms Darcy respectively. ASIC’s case against the remaining three respondent directors of LMIM, **Mr Drake**, **Ms Mulder**, and **Mr van der Hoven** (the first, second and third respondents respectively), was solely based upon the variation which increased in the loan limit in 2012.
7. The abandonment of ASIC’s case against Mr Tickner and Ms Darcy, and its case concerning the 2011 loan variation, was likely due to the evidence of ASIC’s final witness, the expert witness Mr Woolley. As I explain later in these reasons, Mr Woolley’s evidence was, in the literal sense, incredible. Senior counsel for ASIC very properly accepted that the Court should not accept any of the evidence from Mr Woolley other than where it was essentially unchallenged. Even on those points where there was little or no challenge, ASIC placed very limited reliance upon Mr Woolley. My concerns with Mr Woolley’s evidence were so serious that I do not accept his evidence on any contested matter, even if it was not the subject of any substantial cross-examination. Mr Woolley’s evidence did not merely cause a substantial impairment of ASIC’s case in relation to the 2011 variation. It created substantial gaps in the whole of ASIC’s case.
8. The decision by ASIC not to allege any breach of duty in making the loan, or any breach of duty in any of the series of variations to the loan limit before 2012, was likely to have been based on the nature and terms of the MPF. As I have explained, the fund was reasonably high risk and was only open to wholesale or sophisticated investors who invested through financial advisers.
9. ASIC’s allegations against the three remaining directors were that the directors breached their duties of care and diligence under s 180(1) of the *Corporations Act 2001* (Cth)in causing or permitting LMIM to approve the August 2012 Variation. This breach by each director was based on the allegation that each caused LMIM to breach its duties by failing to act as a prudent trustee and that each exposed LMIM to a foreseeable risk of harm, namely civil proceedings by unitholders in the MPF.
10. ASIC’s case concerning why LMIM did not act as a prudent trustee shifted a number of times which made it very difficult to follow. The shifting nature of ASIC’s case was perhaps due to ASIC’s case having been dependent upon Mr Woolley’s evidence. At times during the trial it appeared that ASIC’s case was either that the breach by LMIM, or (at least) a crucial part of the breach by LMIM, was its failure to obtain an independent feasibility report before approving the August 2012 Variation. For instance, ASIC’s expert, Mr Woolley, said that “other than obtaining an independent feasibility analysis of the anticipated future cash flows from the Maddison Estate development, no further inquiries or steps needed be taken by a prudent trustee” ([211], see also [223]-[225]). During oral submissions, senior counsel for ASIC accepted that the allegation of a lack of an independent feasibility report was “crucial” to ASIC’s case (ts 648). Presented in this way, this was an allegation of imprudence by LMIM in the *process* of approving the August 2012 Variation.
11. An allegation of imprudence in *process* is a different case from one which alleges imprudence in *outcome*. In the course of argument, the example I gave to senior counsel was as follows (ts 724). Suppose, in 1976, a trustee decided to invest a large part of a trust fund in a stock beginning with the letter “A”. The trustee seized randomly upon a stock named “Apple”. Suppose also that, at the same time, the world’s most brilliant analysts would have reached the same conclusion by a prudent process of careful data analysis. Objectively, the *decision* by the trustee was not imprudent but the *process* of reaching it was imprudent.
12. At other points during the hearing, senior counsel for ASIC submitted that ASIC’s case was not, or was not merely, a process case. It may be that ASIC presented its case in this alternative way because, as senior counsel recognised, imprudence merely in *process* would have required a “leap” to reach the conclusion that there was a risk of action by unitholders which was a pleaded basis for the breach (ts 724). Unitholders would be likely to bring an action only if there was a prospect of recovering compensation, which requires proof of causative loss. It is extremely unlikely that they would bring a costly civil action merely to expose defects in a *process* relating to a past decision that caused no loss. Hence, senior counsel for ASIC ultimately put ASIC’s case on the basis that the imprudence by LMIM was makingthe *decision* to approve the August 2012 Variation. In other words, ASIC’s allegation was imprudence in the outcome.
13. The difficulty with the submission about imprudence in outcome (ie imprudence in the decision taken) is that ASIC never explained what a prudent trustee in LMIM’s position *would have done.* ASIC constantly reiterated that LMIM *should not have* made a decision to approve the August 2012 Variation. But despite numerous requests for ASIC to explain what decision *should have* been made, ASIC did not present any such case.
14. There were two possible alternatives concerning what a prudent trustee in LMIM’s position *should* have done instead of approving the application to vary the limit of the loan. ASIC did not present a case on either basis. The first alternative was that the decision whether to approve the August 2012 Variation application, on the same or different terms, should have been deferred. The second alternative was that the August 2012 Variation application should have been refused.
15. An explanation of what a prudent trustee would have done required ASIC to examine whether a prudent trustee would have taken one of these alternatives. That required an assessment of the circumstances in which LMIM as trustee for the MPF found itself on 7 August 2012 when the MPF Credit Committee was asked to approve an extension of the loan limit of an additional $100 million. Those circumstances included the following:
16. Maddison Estate already owed more than $150 million to LMIM as trustee for the MPF (the precise amount is very difficult to determine due to retrospective entries in the loan accounts arising from later transactions);
17. the bank financing the loan, Suncorp-Metway Limited(**Suncorp**), had a prior security to LMIM, securing a debt of around $22 million;
18. Suncorp wanted to exit its loan but LMIM had not been able to find a replacement funder;
19. an “as is” valuation in July 2011 of the land acquired for the Maddison Estate development had assessed the value at between $35 million and $40 million, so a foreclosure by Suncorp would leave little, if any, of the $150 million or more for LMIM as trustee for the MPF;
20. work had commenced on site, but until refinancing was obtained, the work could not continue in the absence of further funding from LMIM;
21. Mr Fischer, the CFO of LMIM and one of ASIC’s key witnesses, had told others that the best prospect of recovery of the Maddison Estate loan was to find another funder to take out MPF’s position. The goal was for this to occur after completion of Stage 1 of the development which required further LMIM funds; and
22. the use of the additional $100 million loan would only involve around $16.5 million of funds actually leaving the MPF, because the remainder was capitalised interest and other additions to the loan (including a loan re-establishment fee), which would increase the amount of the loan but would not involve any existing funds being spent.
23. ASIC mentioned very few of these circumstances. Instead, ASIC focused heavily upon matters such as: (i) the number of previous loans (none of which was alleged to involve a breach of duty); (ii) the absence of any explanation for why the additional increases in limit had not previously been foreseen; (iii) delays in the progress of the development; (iv) a hotly disputed report by Ernst & Young (which was not tendered for the truth of its contents); and (v) the LMIM process in relation to feasibility reports which supported the additional $100 million loan, including the lack of what was described by ASIC as an “independent feasibility report”.
24. A consideration of *all* of the relevant circumstances in August 2012, on the limited evidence before the Court including the position in which LMIM found itself, suggests that if a prudent trustee had to make a decision either to *approve* the loan variation or to *refuse* it then approval would have been given.
25. The alternative of deferral is not as simple although, unfortunately, the details of this alternative were not explored in evidence or submissions. If ASIC had brought its case on the basis that the decision to grant the August 2012 Variation should have been deferred (for example, until an independent feasibility report was obtained or so that the proposal could be amended such as to reduce the limit of the loan), then it would need to have led evidence and made submissions concerning the nature of the deferral and the considerations relevant to that decision by a prudent trustee in LMIM’s position. Putting to one side ASIC’s failure to explain precisely what was meant by an “independent feasibility report”, what would the cost be for an independent feasibility report? How long would such a report take to produce? What were the risks to LMIM in the meantime, including the possibility of default under the loan from the first mortgagee? Could those risks have been managed pending the deferred decision? The answer to these questions would all inform an explanation of what a prudent trustee in LMIM’s position would have done. But none of these matters was explored. To the extent that it is possible to assess any of these options, I conclude that there are also significant reasons which might suggest that deferral might not have been a prudent option.
26. Apart from these factual obstacles to ASIC’s case of imprudence by LMIM as trustee, there was a significant legal obstacle. The legal obstacle was that the trust instrument had excluded the duty to act prudently. ASIC submitted that in Queensland, although not in any other State which has similar legislation upon which the Queensland legislation was modelled, this duty could not be excluded. I do not accept that submission. Further, the failure of ASIC to prove that any loss was caused by any act of imprudence is a further reason why ASIC’s claim based on breach of trust must be dismissed.
27. In broad terms, therefore, ASIC’s case in relation to the alleged breaches by all three respondents of directors’ duties of skill and diligence must be dismissed because (i) no breach of trust was proved, and (ii) no reasonable alternative open to LMIM or the directors was proved. Further, to the extent to which there was information before the Court to assess the alternative choices, ASIC failed to prove that a reasonable director of a company in LMIM’s circumstances, with the responsibilities of each respondent, would have refused to approve the August 2012 Variation.
28. Separately to the allegations of breach of s 180(1) of the *Corporations Act*, ASIC also made another allegation against Mr Drake. This allegation was that by causing or permitting the August 2012 Variation in a manner which caused LMIM to commit a breach of trust against the MPF, Mr Drake acted for an improper purpose, and to gain an advantage for himself and a different trust. The improper purpose and advantage was increasing the cash flow to a separate trust from which he withdrew funds to maintain an extravagant lifestyle.
29. This “improper purpose” allegation was also tied to ASIC’s allegation of breach of trust. The failure of the breach of trust claim means that the improper purpose case must also fail. In any event, however, ASIC failed to prove the improper purpose.
30. The application against each of the remaining three respondent directors of LMIM must be dismissed.

# ASIC’S PLEADED CASE AGAINST THE REMAINING THREE RESPONDENT DIRECTORS

1. In one respect, ASIC’s case in relation to all breaches was consistent, although the premise of ASIC’s case might be doubted. ASIC consistently alleged that in order for each of the directors to be liable for breach of their duties to LMIM it was necessary for LMIM to have committed a breach of trust. In other words, and as I explain further below, in order for the directors to have breached s 180(1) of the *Corporations Act*, ASIC’s case was that it first needed to prove a breach of trust by LMIM as trustee.

## ASIC’s pleaded case concerning s 180(1) of the *Corporations Act*

1. ASIC pleaded that the directors breached their duties under s 180(1) of the *Corporations Act* because they caused or permitted LMIM to commit a breach of trust, and exposed LMIM to a foreseeable risk of harm, namely civil proceedings by unitholders in the MPF. ASIC essentially pleaded that this foreseeable risk of harm was greater than that to which a director, exercising his or her powers and discharging duties with the required care and diligence, would have permitted.
2. As for that part of the s 180(1) plea that the directors “caused or permitted LMIM to commit a breach of trust”, ASIC’s case was that LMIM breached its duty to exercise the care, diligence, and skill that a prudent person engaged in the profession or business of acting as a trustee or investing money would exercise in managing the affairs of other persons. This duty was pleaded in two ways: (i) as a statutory duty under s 22(1)(a) of the *Trusts Act 1973* (Qld) (***Trusts Act***), and (ii) as an equitable duty.
3. In some respects ASIC’s case was opaque. The matters which were not clear were (i) *how* LMIM breached its duties as trustee, and (ii) *how* each respondent breached his or her duties as director under s 180(1) of the *Corporation Act*. Each is addressed separately later in these reasons. It suffices to observe at this point that at times ASIC alleged that it was not required to prove how any breach had occurred.
4. As to LMIM’s alleged breach of its duties as trustee, ASIC pleaded:
5. numerous circumstances that existed at the time of the August 2012 Variation ([147]-[151]);
6. that in those circumstances, LMIM exposed the MPF to a foreseeable risk of capital loss by approving the August 2012 Variation ([153]); and
7. that in those circumstances, the degree of risk to which the MPF was exposed was greater than the risk to which a trustee exercising its powers of investment with the degree of care, diligence and skill that a prudent person engaged in the business of acting as a trustee or investing money would permit the MPF to be exposed ([154]).
8. Separately from those circumstances, ASIC also pleaded that:
9. a trustee exercising its powers of investment with the degree of care, diligence and skill that a prudent person engaged in the business of acting as a trustee or investing money would have obtained an independent feasibility analysis of the anticipated future cash flows from the Maddison Estate development ([152]).
10. Early in ASIC’s case, I asked questions about the nature of ASIC’s pleaded case. ASIC appeared to plead two cases concerning the alleged breach of trust by approving the August 2012 Variation. The first case was a process case. It was an allegation that, irrespective of whether the August 2012 Variation would have been approved by a prudent trustee, the breach consisted of the failure by LMIM to follow a prudent process in making its decision to approve the variation. The second case was an outcome case. It was an allegation that the approval itself was imprudent (ts 87).
11. After a short adjournment, senior counsel for ASIC explained that the two aspects of the alleged breach were “cumulative”, and that only a single breach of trust was alleged. The single breach of trust alleged was the act of approving the August 2012 Variation. ASIC’s case was that the failure to obtain an independent feasibility report was just one factor which contributed to the breach. So, *even if* an independent feasibility report might have concluded that approval was a reasonable option, the other circumstances were still such that approval should not have been given (ts 89-90).
12. Several points about ASIC’s pleading should be noted:
13. ASIC did not plead *any* possible alternative course that a prudent trustee *would* have adopted other than not to approve the August 2012 Variation. ASIC did not allege that a prudent trustee would have deferred the decision, preferring to wait to obtain an independent feasibility report. Nor did ASIC plead that a prudent trustee would have refused to approve the August 2012 Variation. ASIC’s case was that a prudent trustee would not, in the circumstances, have made the decision to approve the August 2012 Variation but it refused to say which of the two possible alternatives a prudent trustee would have taken.
14. A crucial circumstance relied upon by ASIC as a reason why a prudent trustee would not have approved the August 2012 Variation was LMIM’s failure to obtain an independent feasibility report (ts 647-648). The absence of the independent feasibility report was important to ASIC’s case because its absence was said to increase the foreseeable risk of capital loss.
15. Although ASIC’s case was that a prudent trustee would not have approved the August 2012 Variation, ASIC did *not* deny that a variation to allow the same further $100 million loan would not have been made in any event. ASIC did not lead any evidence about what an independent feasibility report might have concluded. In other words, ASIC accepted that it was possible that an independent feasibility report might have concluded that a reasonable course would have been to grant a variation permitting the proposed variation.
16. In closing submissions, ASIC submitted as follows ([274]):

ASIC’s case on breach of trust is simply this. A prudent trustee in [the] circumstances would not have approved the advance. The approval of that advance breached the duty prescribed by s 22 of the *Trusts Act* and exposed the MPF to a foreseeable risk of capital loss, being the risk of default by the borrower if the estimated cash flows generated by the development did not eventuate.

## ASIC’s pleaded case of Mr Drake’s improper purpose

1. ASIC pleaded its allegations of Mr Drake’s contravention of s 181(1) and s 181(2) of the *Corporations Act* as based upon a plea of improper purpose. That plea was expressed in ASIC’s statement of claim as follows ([167]):

in causing and/or permitting LMIM to approve the August 2012 Variation and agreeing to advance to Maddison Estate a further $100 million in a manner which caused LMIM to commit a breach of trust against MPF, [Mr Drake] exercised his powers and discharged his duties as a director and officer of LMIM for the purpose of maximising the cash flow available to LMA as trustee for the [LMA] Trust to fund the loans to [himself] (**Improper Purpose**).

1. This improper purpose is pleaded as amounting to a failure by Mr Drake to exercise his powers and discharge his duty as a director and officer of LMIM in good faith in the best interests of LMIM or for a proper purpose; and improper use by Mr Drake of his position as a director of LMIM to gain an advantage for himself and for the LMA Trust (defined below).

# THE FACTUAL BACKGROUND

## Relevant entities, persons, and relationships

### Outline of the various entities

1. On 31 January 1997, LMIM was incorporated. Mr Drake was appointed as director of LMIM at the time of incorporation. In June 2006 and September 2006 respectively, Mr van der Hoven and Ms Mulder were also appointed as directors of LMIM.
2. Separate from LMIM was another company, called LM Administration Pty Ltd (**LMA**), which was the trustee for the LM Administration Trust (the **LMA Trust**) which was created on 30 June 2003.
3. LMA (as trustee for the LMA Trust) and LMIM entered into a service agreement (**LMA Service Agreement**). The service agreement was provided in Sch 1 to be effective from 1 July 2005 although, curiously, the cover page bore the date 1 July 2010. In the LMA Service Agreement, LMA agreed to provide LMIM with services for LMIM’s funds management operations. Those services included the provision of staff, equipment, and other services for the proper management and administration of LMIM’s business including matters such as payment of operating costs, debt collection, preparation of financial statements, and contract negotiation. The cost for the services was agreed to be (i) a percentage of LMA’s total expenses, and (ii) all management fees earned by LMIM as the manager of its managed investment schemes.
4. The personnel who assisted LMIM (but were employed by LMA not LMIM) were organised into teams. There was a lack of clarity in some of the evidence and submissions concerning who employed these various personnel. I accept the evidence of Mr Fischer and Ms Mulder that employees were employed by LMA and not by LMIM (see also the LMA Service Agreement which I discuss below). Further, ASIC’s statement of claim, in paragraph [10], alleged that LMA employed Mr Drake, Ms Mulder, Mr van der Hoven, Mr Tickner, Ms Darcy, Mr Barnett, Mr Fischer, Mr King, and Ms Chalmers.
5. One of the teams which assisted LMIM was the Property Asset Management (**PAM**) team which contained employees of a related company, LMA. The PAM team was led by Mr Tickner. Another team was the finance team led by Ms Darcy and then Mr Fischer. A third was the marketing team led by Ms Mulder. A fourth was the global operations team led by Ms Phillips. A fourth was the portfolio management team led by Mr van der Hoven and Mr Petrik. A fifth was the foreign exchange team led by Mr van der Hoven. And a sixth was the in-house legal team.
6. The PAM team had around 25 staff. Their skills included areas of lending, development, town planning and general property. The team was divided into three parts responsible for: (i) identifying investment opportunities for the funds; (ii) assessing the assets and working to progress the projects; and (iii) administering the loans. The PAM team reported to the various committees, including the MPF Credit Committee (discussed further below). In 2012, when Mr Tickner retired as a director, Mr Fischer became the leader of the PAM team.
7. On 4 December 2001, LMIM entered a deed which produced a constitution for the MPF. The MPF Constitution was expressed as a deed between LMIM and the members, as they were constituted from time to time, of the MPF. The MPF was described as the “Scheme”. It was a unit trust to which members could subscribe by application following an offer or invitation to subscribe. The MPF Constitution was amended on a number of occasions after 4 December 2001.
8. On 4 May 2007, the MPF entered into a loan agreement granting a loan to Mr Drake. Although the loan agreement document was not in evidence at trial, its existence can be inferred from a variation deed that was in evidence. Mr Drake immediately drew down $8 million of the loan. By 30 June 2011, he had drawn down more than $15 million ($15,226,498.65).
9. On 14 September 2007, **LMIM Asset Management Pty Ltd** was incorporated. Mr Drake was its sole director, secretary and shareholder.
10. On 14 September 2007, Maddison Estatewas incorporated. It was then known as LM Coomera Pty Ltd.

### The MPF

1. The MPF was only open to investment by wholesale or sophisticated investors. As Mr van der Hoven explained, the MPF funds were only sold to investors via a network of financial advisers. LMIM conducted “Introducer Days” in Australia and overseas at which presentations would be given by directors and other LMIM staff.
2. It is important to reiterate the point I made in the introduction to these reasons that the sophisticated investors and their advisers would have been immediately aware from the few pages of the information memorandum and investment application that investment in the MPF involved considerable risk. Returns, however, were high. They were around 25% per annum. As an example, the 1 November 2011 MPF information memorandum and application form for investors contained six pages of information entitled “About the LM Managed Performance Fund” and “LM Managed Performance Fund”. Those pages explained that the MPF invested in “commercial loans, direct real property, and cash” and had around $274 million of assets. Those $274 million of assets included around $248 million invested in Australian commercial loans. The largest of the commercial loans was described as being $142 million, more than half of the size of the fund.

### The MPF Credit Committee

1. The MPF investment decisions were made by an LMIM committee called the **MPF Credit Committee**.
2. Mr Drake, Ms Mulder, and Mr van der Hoven were all members of the committee. Ms Darcy was the chair until her resignation from LMIM on 21 June 2012. Other persons who were members of the credit committee included Ms McCallum (a member of the PAM team who served as a loans analyst) and Mr Parker (who was responsible for obtaining loans). Paralegal staff from the PAM team, Ms Chalmers and Ms Kingston, would organise and facilitate the meetings, and would take minutes. Development managers would also attend the committee meetings from time to time.
3. The role of the MPF Credit Committee was to assess loans proposed as investments for the MPF and to consider any required action for existing loans. The procedure involved preparation of a synopsis paper which was circulated to the committee members at the meeting. The meeting papers generally also included a feasibility model prepared by the development manager from the PAM team. The MPF Credit Committee would review the information and if a decision could not be made, the meeting was adjourned.
4. There were documentary guidelines and procedures for the MPF Credit Committee. One guideline was that “LM Directors require that all [MPF Credit Committee] decisions are to be made at a meeting as opposed to email voting (unless the topic for decision is a very simple, non-material matter)”. However, occasionally a decision would need to be made without a physical meeting and members would vote electronically through their email response.

### Mr Drake

1. In an information memorandum and application dated 1 November 2011, Mr Drake’s position and responsibilities were described as follows:

**Peter Drake**

**Chairman and Chief Executive Officer**

Peter founded LM in 1998, after 20 years’ experience in Australia’s financial services and life insurance sectors. As 100 per cent shareholder and CEO, Peter is principally responsible for the strategic vision, direction and structured growth of LM. Since its inception, Peter has been actively involved with LM’s expansion to ten international offices, now servicing beyond 60 countries. Peter is particularly active in the design and marketing of LM’s Australian dollar and currency hedged investment products. Working closely with LM’s Portfolio Manager to manage the growth of funds under management, Peter also plays an integral role in LM’s Funds Management Committee. With significant experience in direct property and joint venture property developments across Australia, Peter is also a member of LM’s Credit/Investment Committee, responsible for approving and setting the conditions of loans within LM’s mortgage portfolio. Peter’s vision of an innovative and prudential funds manager holds true as LM continues its dynamic growth in Australia’s financial services, business and property sectors. Peter is a member of LM’s Credit/Investment Committee, Funds Management Committee and Property Research and Analysis Committee.

A similar biography was provided in other information memoranda produced by LMIM from 2009 to 2012.

1. Mr Drake can comfortably be described as the prime mover behind the Maddison Estate development. The extent of his control is plain from the diagrammatic relationship of all of the relevant entities, set out later in these reasons. But his involvement was far more comprehensive than these formal roles. As I explain below, the Maddison Estate development became closely associated with his conception and vision for it, including as Mr Barnett described, Mr Drake’s desire to have a development which was different from anywhere else in the world.

### Mr van der Hoven

1. In the same information memorandum and application described above in relation to Mr Drake, Mr van der Hoven’s position and responsibilities were described as follows:

**Eghard Van Der Hoven**

**Executive Director, Portfolio Manager**

In 2003 Eghard joined LM as Portfolio Manager, responsible for the monitoring and ongoing performance of LM’s various funds. As Executive Director, Eghard’s sound understanding of the investment industry spanning almost 20 years includes extensive experience in stock broking, auditing, investment analysis, business strategy and policy planning. As the Chair of LM’s Funds Management Committee, Eghard is responsible for joint decisions in relation to the asset allocation, geographic spread allocation, cash flow, delivery rate forecasting and budgeting of LM’s funds. He holds a Master of Commerce, majoring in Economics, and a Bachelor of Commerce (Hons) in Economics, from University of Pretoria, South Africa. Eghard is a member of LM’s Property Research and Analysis Committee, Credit/Investment Committee and Arrears Committee.

1. Mr van der Hoven commenced employment with LMA (the service provider to LMIM) in late 2003 as Portfolio Manager, and held this position until around 2009. As Mr van der Hoven explained, as Portfolio Manager he was primarily responsible for monitoring and managing the funds’ cash flows and measuring their profitability (which could determine the distribution rate that could be paid to investors). Mr van der Hoven was the Portfolio Manager of the MPF until Mr Petrik took over in about 2009. Despite this, Mr van der Hoven continued to be involved in the portfolio management process.
2. On 22 June 2006, Mr van der Hoven was appointed as Executive Director of LMIM. Also around this time, he was appointed as the head of LMIM’s Foreign Exchange team. His focus shifted to managing the foreign exchange activity of the various funds. He explained that his role as Executive Director did not change his core focus on portfolio management and foreign exchange management. However, he consequently became more involved in other parts of the business.
3. As an Executive Director, Mr van der Hoven sat on the board of directors and reported to the board on foreign exchange dealing, and was involved in making company decisions that were brought to the attention of the board. Mr van der Hoven was a voting member of the MPF Credit Committee and other committees including the Property Research and Analysis Committee.
4. Mr van der Hoven was paid a salary and bonuses. His bonus was calculated as 2.5% of the profit of the LM Group. Mr Fischer explained that the bonus was paid from the operating cash flow of the LM Group. ASIC submitted, without dispute, that his salary and bonuses (relevant to the business judgment rule upon which he relied) were as follows, with his salary apparently calculated by subtracting his bonus from total taxable income:
5. 2010: salary $209,460; bonus $95,574;
6. 2011: salary $244,066; bonus $129,811; and
7. 2012: salary $244,047; bonus $236,786.
8. Mr van der Hoven gave evidence. He was cross-examined vigorously, although fairly. He was measured in his evidence and I consider that he was entirely truthful and, to the extent to which he could recall detail, reliable.
9. ASIC submitted that parts of Mr van der Hoven’s evidence had been contrived after he observed Ms Mulder give evidence before him. In particular, it was submitted that Mr van der Hoven’s affidavit evidence had referred only to auditors assessing the Maddison Estate development’s feasibility generally. In cross-examination, Mr van der Hoven’s evidence about his belief concerning the auditors became more precise. He said that he believed that the auditors were reviewing escalation rates (ts 683). ASIC submitted that this precision came only after he had heard similar questions asked in cross-examination of Ms Mulder.
10. Mr van der Hoven was a respondent to very serious allegations. He was present for much of the court hearing, which was entirely appropriate and to be expected given the gravity of the allegations against him. He could not possibly be criticised for observing Ms Mulder give evidence. I do not understand ASIC’s submission to have suggested this. However, ASIC’s submission misconstrues Mr van der Hoven’s increased precision in his answers as a basis upon which it could be said that his evidence had been moulded following his observations of Ms Mulder’s questions. I do not accept this submission about a witness who presented as honest and measured. As I explain later in these reasons, there is also an independent basis to accept Mr van der Hoven’s evidence concerning his belief in the role of the auditors.

### Ms Mulder

1. In the 1 November 2011 information memorandum and application, Ms Mulder’s position and responsibilities were described as follows:

**Francene Mulder**

**Executive Director, General Manager Distribution/Product**

Francene commenced with LM in 1999, following a 20 year career in the commercial, legal and securities sectors. Prior to joining LM, Francene held managerial positions focused on the areas of commercial mortgages, conveyancing and the property sector. Specific experience in mortgage securities and the marketing of financial products provided a solid background for Francene to successfully undertake her role within LM. As Executive Director, Francene is primarily responsible for the marketing and expansion of distribution of LM’s products on a wholesale and retail basis, throughout Australia and international markets. Francene takes an active role in the direction of all client communication, company communication, corporate literature and service. Francene is also a member of LM’s Property Research and Analysis Committee, Funds Management Committee, Credit/Investment Committee and Arrears Committee.

1. Ms Mulder explained that after secondary school, she commenced work at various law firms, primarily in conveyancing and then general mortgages. In August 1999 she commenced working as marketing manager at LMIM within a small treasury division, although she was employed by LMA.
2. After having worked at LMIM for 7 years, Ms Mulder was appointed as Executive Director and Marketing Director of LMIM on 30 September 2006. Ms Mulder explained her duties as follows:

I was appointed Executive Director and Marketing Director of LMIM on 30 September 2006. As Marketing Director, I managed the marketing/business development teams, communications team, and the team that put the product disclosure statements together. After transitioning from Marketing Manager to Director I was still heavily involved in dealing with daily marketing activities. As such, though I was a member of various committees, I travelled frequently and often did not attend committee meetings. During this time, LMIM established further satellite offices and I was involved in assisting the teams with growing market presence in regions those offices were servicing.

…

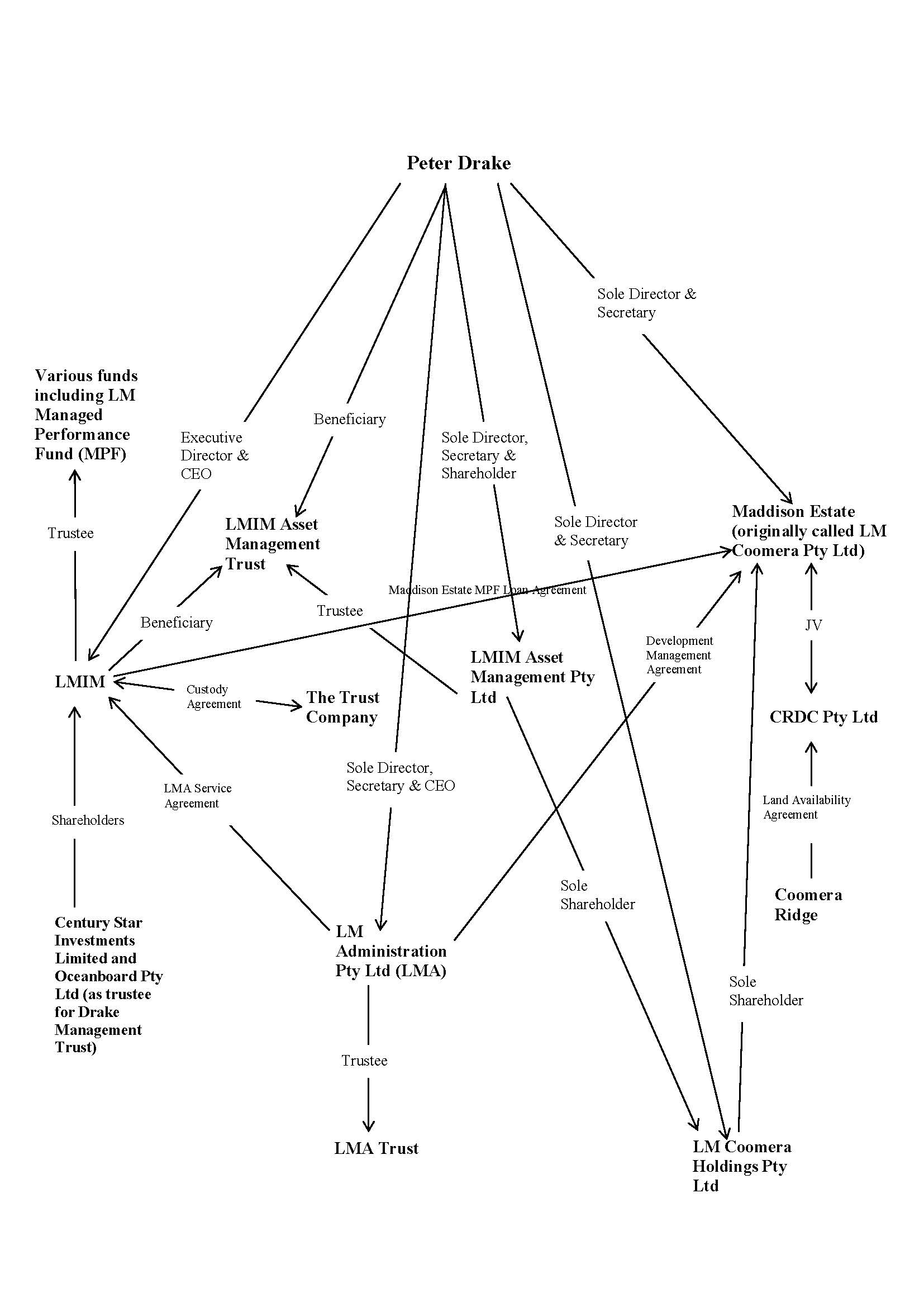
In my role as Director, Marketing Manager and in publishing information intended for financial advisors relating to disclosure or particular assets of the fund, I was reliant on information reported to me by the finance team and the CFO. In a similar manner, I was reliant on information reported by the PAM Team in credit committee meetings in relation to fund assets… LM had processes and experienced senior people in place in each department and I was comfortable with that and relied on their expertise to assist me in making decisions as a Director and Marketing Manager. I discuss this in further detail below with respect to Maddison Estate.

I was an active working director. LM was a large organisation and my daily involvement was within the Marketing and Communications teams.

1. As Ms Mulder explained, her main focus from 2011 until the end of 2012 was the First Mortgage Income Fund. During this time, the other directors were working across the other areas of the business to allow Ms Mulder to focus on the First Mortgage Income Fund. Ms Mulder explained that she generally did not read valuations, loan documents, feasibility models or advices as that was not her area of expertise or her role. She said, and I accept that she believed, that it was the role of the expert individuals in the specialised in-house PAM team to understand these documents and to present the relevant information to decision-makers. She trusted their experience and expertise.
2. Like Mr van der Hoven, Ms Mulder was paid a salary and bonuses (calculated in the same way as Mr van der Hoven’s). ASIC submitted, without dispute, that her salary and bonuses (relevant to the business judgment rule upon which she relied) were as follows (again, apparently by calculating salary by deducting bonus from total taxable income):
3. 2010: salary $178,620; bonus $104,142;
4. 2011: salary $244,066; bonus $129,811; and
5. 2012: salary $208,784; bonus $236,786.
6. Ms Mulder gave evidence. She was also cross-examined vigorously, although again fairly. ASIC submitted that an inference should be drawn that Ms Mulder was deliberately evading being committed on any matter of detail beyond what she relies upon for her defence. I do not accept this submission. I have no doubt at all that Ms Mulder was a thoroughly honest witness and that she answered all questions truthfully and to the best of her ability. Like Mr van der Hoven she had a limited recollection of matters that were discussed at MPF Credit Committee meetings. To the extent that she did recall those meetings, I consider that her answers were truthful and reliable.

## The Maddison Estate joint venture

1. On 12 September 2007, the MPF Credit Committee considered a proposal for a $36.75 million loan by the MPF to a special purpose vehicle, LM Coomera JV Pty Ltd, for the Maddison Estate development. This was the genesis of the loan which was at the heart of the proceedings in this case.
2. A synopsis dated 11 September 2007 was sent to the MPF Credit Committee describing how LM Coomera JV Pty Ltd would on-lend funds to a company in the Young Land Group called Coomera Ridge Pty Ltd(**Coomera Ridge**) under joint venture agreements, or to another joint venture special purpose vehicle as part of the Young Land Group. Coomera Ridge had an entitlement to 31 parcels of land at Coomera, sometimes described as the “**Pimpama Land**”.
3. The 11 September 2007 synopsis explained that the proposal was for the MPF to enter a joint venture with a company owned by **Mr Young** (a director of the Young Land Corporation) to develop and sell the Pimpama Land into a residential subdivision comprising approximately 1532 residential lots (combining (i) some land sales, and (ii) some house and land packages). Mr van der Hoven explained that the expected gross revenue was said to be $577.8 million, and that the expected net profits to each joint venturer was said to be $65 million.
4. The security for the loan was described as “generally secured by way of second mortgage”, and a fixed and floating charge over all of the assets of the joint venture special purpose vehicle company.
5. On 13 and 14 September 2007, the members of the MPF Credit Committee approved the proposal for a loan of $36.75 million. The loan, which somehow became $40 million, was made from the MPF to a company which became known as Maddison Estate.
6. On 19 November 2007, several agreements gave effect to the joint venture:
7. a joint venture development agreement was entered into by Maddison Estate and CRDC Pty Ltd (**CRDC**). CRDC was incorporated in September 2007 by Mr Young for the purpose of participating in a joint venture with Maddison Estate to develop the Pimpama Land. Mr Young was CRDC’s sole director and secretary until October 2010. The agreement provided for the equal sharing of proceeds and provision of $40 million by Maddison Estate. It was signed by Mr Drake for Maddison Estate and by Mr Young for CRDC. Curiously, it provided for a contribution from Maddison Estate of $40 million;
8. a land availability agreement was entered into by Maddison Estate (signed by Mr Drake), Coomera Ridge, and CRDC (both signed by Mr Young); and
9. a development management agreement was entered into by Maddison Estate, CRDC, and Young Land Project Management Pty Ltd (**Young Land Project Management**) to engage Young Land Project Management as the development manager.
10. As Mr Young had conceived it, the Maddison Estate development was for: (i) initial sales of land only; (ii) subsequent sales of house and land packages; and (iii) eventual sales of town houses and units. The plan involved approximately 1,458 dwellings on 700 residential lots with another 700 attached dwellings. This plan had obtained preliminary development approval from the Gold Coast City Council on 16 November 2009. It received final approval on 6 May 2010.
11. However, by 2010, the property market on the Gold Coast and other parts of Queensland had declined, in part due to the global financial crisis. Mr Young’s companies, including Young Land Project Management, were unable to meet their liabilities. Mr Young became personally bankrupt. Mr Young and Mr Drake agreed that Maddison Estate and CRDC would terminate the joint venture. Around April 2010, a number of agreements were entered to terminate the joint venture.
12. around the time of the termination of the joint venture:
13. Maddison Estate entered into a development management agreement with LMA (**LMA Development Management Agreement**). LMA agreed to provide development services, effectively replacing Young Land Project Management. Mr Young, Mr Fischer and other former employees of Young Land Project Management were employed by LMA. Under the LMA Development Management Agreement, LMA would receive a monthly development management fee which commenced at $250,000 (plus GST) a month, and increased to $300,000 (plus GST) a month from July 2011. The LMA Development Management Agreement provided that the agreement would terminate on 30 June 2015.
14. Mr Young transferred his interest in the Maddison Estate development to Mr Drake, and Mr Drake became the sole director of Coomera Ridge.
15. Also following termination of the joint venture, Maddison Estate was substituted as the sole borrower under the Suncorp loan facility (explained further below).
16. Some of these matters, and the relationships between the relevant entities, are represented in the diagram below.



## The loans to the joint venture

### The Suncorp loan in January 2008

1. In January 2008, Suncorp extended a finance facility to Maddison Estate and CRDC with a limit of $6,464,000. The facility was secured in part by first ranking charges over the assets and undertakings of Maddison Estate and CRDC.
2. On 23 January 2008, $5,836,377.50 was drawn down under the Suncorp loan facility. The loan facility was subsequently increased. By October 2011 the loan was drawn down to around $34 million. However, by March 2012 it had been reduced to $26 million.
3. Young Land Corporation and Suncorp commissioned valuations of the Pimpama Land on an “as is” basis. The valuations by **Landmark White** were dated 6 March 2008 and 28 July 2008 respectively. The valuations valued the Pimpama Land at around $54 million in March 2008, and $72.5 million in July 2008. The 28 July 2008 valuation noted that the total area of the 32 parcels of land was 109 hectares. It observed that at the date of valuation all of the properties were being used as rural homesteads and that a number of the lots had limited development potential due to town planning restrictions.

### The Maddison Estate MPF Loan Agreement on 13 November 2007

1. On 13 November 2007, LMIM as trustee for the MPF entered a loan agreement with Maddison Estate (the **Maddison Estate MPF Loan Agreement**). In that agreement, LMIM agreed to lend $40 million to Maddison Estate to give effect to the joint venture.
2. The date for repayment was the date when LMIM demanded payment from Maddison Estate. The Maddison Estate MPF Loan Agreement did not provide for any guarantor. It provided that Maddison Estate would indemnify LMIM against any expense, loss, loss of profit, damage or liability which LMIM may suffer as a consequence of any default by Maddison Estate.
3. The Maddison Estate MPF Loan Agreement provided for an interest rate to be determined by LMIM on the basis that Maddison Estate should have no distributable income at the end of each financial year. Interest instalments were to be paid monthly. The interest rate provision (Item 6) provided:

Such rate as is determined by [LMIM] in its absolute discretion from time to time (with the intent that such rate results in [Maddison Estate] having no distributable income at the end of each financial year), or in default of such determination by the Lender, 18% per annum.

1. The Maddison Estate MPF Loan Agreement was executed by Mr Drake and Ms Darcy as directors of LMIM. It was executed also by Mr Drake as the sole director of Maddison Estate.
2. One of the recitals provided that LMIM entered into the agreement only in its capacity as trustee for the MPF.
3. The Maddison Estate MPF Loan Agreement did not initially provide for any security. Security was subsequently provided under a deed of variation on 11 November 2008 where Maddison Estate agreed to provide a charge over “all the property, assets and undertaking of [Maddison Estate] of whatsoever nature and kind and wheresoever situated, present and future”.
4. On 20 May 2010, the interest rate was varied to be a “rate of 25% per annum, provided that such rate may be adjusted in the absolute discretion of the Lender on each anniversary of the loan, to equal the market rate for loans of such nature, to be determined by the Lender in its absolute discretion. If no adjustment is made the rate will remain at 25%”. The interest rate was set at 25% to ensure that Maddison Estate did not make a profit. Legal advice was received about the propriety of the interest rate increase in light of Mr Drake’s potential conflict of interest.

#### The variations to the Maddison Estate MPF Loan Agreement and the feasibility reports

1. The Maddison Estate loan limit could not have been intended to cover all of the costs of the Maddison Estate development and capitalised interest. There was little evidence on this point. ASIC asserted that the variations to the limit showed that LMIM’s “track record of properly forecasting development and other costs and adhering to budgeted projections was abysmal”. In contrast, Ms Mulder and Mr van der Hoven submitted that there was no evidence that the loan and variations were required to be a “once only loan”.
2. The evidence does not reveal whether the MPF Credit Committee ever considered the extent to which the initial limit and subsequent variations would need to be increased again in the future. Any conclusion about what maximum limit would be needed might have been extremely difficult to reach. One reason for the uncertainty is that the scope and detail of the project changed as it progressed and it seems that these changes were welcomed. Another reason for the uncertainty is that the limit of the loan would depend on how long the development took, which would be extremely difficult to estimate. The longer that the development took, the more capitalised interest would add to the loan amount. At 25%, the capitalised interest only on a $60 million loan would require $15 million per annum. A third reason for uncertainty is that LMIM’s exit plan, at least from late 2011, was to be bought out. This could only occur when a purchaser could be found to whom the debt could be assigned. When that occurred, no further limit would be needed by LMIM.
3. There are strong reasons why the initial limit, and variations, might reasonably not have been expected to be the permanent limit to the loan. It is notable that the independent lender, Suncorp, was prepared to lend with an initial limit of $6.4 million in January 2008 but to allow that limit to increase to around $34 million by October 2011.
4. One reason why the initial loan, and subsequent variations might not have been expected to be permanent is that the synopsis dated 17 September 2008, which supported an increase of the loan from $40 million to $58 million, described the purpose of the loan to be to “acquire 32 parcels of land, consolidate and re-develop into a residential Master Planned community comprising approx 1500 dwellings”. The synopsis explained that the “total purchase price of the land lots is $73M + fees + stamp duty + interest”. Even with the Suncorp loan, the first extension to $58 million would barely cover the costs associated with acquiring all 32 parcels of land, still less the costs of the massive development until revenue streams began. The synopsis also observed that the initial $40 million loan did not apply to ongoing costs, and that the increase to $58 million was necessary “to allow for ongoing *budgeted* payments” (emphasis added).
5. The inference that at least some of the limits which were varied by subsequent variations were not expected to be permanent is also supported by the fact that some of the variations were expressed as applying only for a particular period. For instance, the September 2011 variation was agreed on the basis that it would only provide the funding required until the end of March 2012. There was no evidence that any of the members of the MPF Credit Committee considered it surprising at that time that the additional $65 million limit was needed although it would only provide short term funding for six months (to the end of March 2012) up to a limit of $180 million. At least in relation to this variation, rather than suggesting an “abysmal” track record of forecasting as ASIC had submitted, the MPF Credit Committee was potentially quite accurate. By the end of March 2012, the loan balance of the Maddison Estate MPF Loan Agreement was $177,766,781.23 (to the extent that the loan balance can be relied upon despite retrospective additions to it based on later events).
6. The Maddison Estate MPF Loan Agreement was varied on the following occasions:
7. An increase from $40 million to $58 million (with MPF Credit Committee approval on 18 September 2008) by a deed of variation entered on 11 November 2008. The variation took effect on 18 September 2008.
8. An increase from $58 million to $70 million (with MPF Credit Committee approval on 5 August 2009) by a deed of variation entered on 6 October 2009. The variation took effect on 30 July 2009.
9. An increase from $70 million to $95 million (with MPF Credit Committee approval on 25 February 2010) with a deed of variation executed on 14 April 2010. The variation took effect from 11 December 2009.
10. An increase from $95 million to $115 million (with MPF Credit Committee approval on 28 July 2010) with a deed of variation executed on 28 June 2011. The variation took effect on 14 February 2011.
11. An increase from $115 million to $180 million (with MPF Credit Committee approval on 25 September 2011) with a deed of variation executed on 19 October 2011. The variation took effect on 15 February 2011.
12. An increase from $180 million to $280 million (with MPF Credit Committee approval on 7 August 2012) with a deed of variation executed on 1 July 2012 (the August 2012 Variation). The variation took effect on 30 June 2012.
13. Prior to each variation of the loan, feasibility reports were prepared and used to provide a synopsis for the MPF Credit Committee.
14. The feasibility reports were prepared by the PAM team using a proprietary software program called “Estate Master”. Estate Master required the input of numerous variables from which it calculated a net present value of the development. The variables which were inputted by members of the PAM team included projected revenue data, projected expense data and various assumptions such as escalation rates (the rates by which the value of lots might escalate in price during the timeframe of the development).
15. Ms Phillips explained that the revenue and expense inputs were not all externally obtained. Some, such as sales prices and valuations, were researched from independent reports and other research such as market sales prices, real estate agents, and sales reports. Those valuations were scrutinised by the board of LMIM in informal meetings.
16. Other inputs were externally obtained. Mr Barnett gave evidence that information was derived from external consultants concerning council fees, consultants’ fees and construction cost estimates from engineers and landscape architects. Mr Young also said in his affidavit and in his oral evidence that he obtained estimates of development costs from companies such as Mortons Urban Solutions (ts 413).
17. Mr King explained that apart from these cost and revenue inputs, the escalation rate was the remaining variable (although discount rates also needed to be applied to the model). As Mr Barnett explained, the escalation rates are an increment by which the value of the property is multiplied to estimate the amount by which the value of the property will improve over time. The increment is applied annually to estimate the amount by which property will increase in value from year to year. The values of property to be released through Stage 1 were the baseline. The escalation rates were applied to that baseline.
18. Mr Barnett said that it was usual to obtain the escalation rates from an independent property analyst. He and Mr King used a report from BIS Shrapnel entitled “The Outlook for Residential Land in Gold Coast”. Mr Barnett also subsequently referred to sales revenue escalation rates from a third party property consultant called RP Data.

#### The abandonment of the allegations concerning the September 2011 loan variation

1. From the inception of the case until shortly after ASIC’s evidence concluded, ASIC alleged breaches by the respondents in relation to the September 2011 loan variation. Although the allegations were abandoned, it is necessary to explain the background to that variation in a little more detail because ASIC continued to rely on that background in a slightly opaque submission that, although the variation was not said to be a breach of duty, it could somehow cast a shadow over the August 2012 Variation which was said to be a breach of duty.
2. By 18 September 2011, the loan balance of the Maddison Estate loan was around $140 million. This exceeded the previously approved limit of $115 million. A synopsis dated 22 September 2011 sought an increase to $200 million. The members of the MPF Credit Committee discussed, and approved, an increase in the limit of the advance from $115 million to $180 million a few days later.
3. On 25 September 2011, Mr Tickner sent an email to the members of the MPF Credit Committee (including the respondents) which attached the 22 September 2011 synopsis. The email said:

Attached is the synopsis regarding the increase to the maximum Approved Loan Amount.

This was discussed by ST LD PD EVH and FM and agreed to an amount of $180M based upon the funding required until end March 2012 on the basis of anticipated project related costs, Suncorp’s amortisation requirements interest and also MPF’s interest.

Can you please confirm your acceptance by voting.

1. The initials refer to, respectively, Mr Tickner, Ms Darcy, Mr Drake, Mr van der Hoven, and Ms Mulder. However, Ms Mulder’s evidence was that this loan was approved at a meeting when she was in Hong Kong, and too unwell to attend the meeting. I accept Ms Mulder’s evidence. In any event, Ms Mulder would have become aware of the approval shortly afterwards.
2. In the synopsis which was provided to the MPF Credit Committee to assist them in considering the variation to the loan, it was observed that the loan balance was more than $140 million (which exceeded the approved limit of $115 million). The synopsis noted that development approval had been granted and further applications were being made for the first stage of subdivision, although the number of proposed dwellings and lots would be subject to further feasibility and cash flow analysis once the approvals progressed. It was also noted that Suncorp held a first mortgage which secured a $38 million debt. It was observed that Suncorp was not continuing with development loans, was reducing all of its facilities, and had requested a paydown of the loan facility of $2 million a month for the six months which commenced in August 2011. The increase in the loan would “cover the principal reductions ($2M per month) and interest on the Suncorp loan (approx $350K p/m), interest on the MPF facility (currently $2.5M p/m and capitalising) and development costs for Stage 1 completion”.
3. ASIC’s claim initially alleged that the September 2011 loan variation was a breach of trust by LMIM, and a breach of s 180(1) of the *Corporations Act* by the directors. But, after the evidence of Mr Woolley, ASIC abandoned this allegation. Nevertheless, ASIC’s pleading and submissions still relied upon circumstances surrounding the September 2011 variation which had previously been pleaded in the context of the allegations of breach of trust, in particular:
4. the respondents’ possession of a report produced by Ernst & Young in January 2011 which was critical of the development;
5. the respondents’ knowledge of the Landmark White preliminary valuation for Suncorp in July 2011 which assessed the “as is” value of the Pimpama Land as between $35 million and $40 million based on its “highest and best use”;
6. LMIM’s previous increases in the loan from $40 million in November 2007; and
7. the respondents’ awareness that construction on the development had yet to commence.
8. ASIC was right to abandon the allegations of breach in relation to the September 2011 loan variation. But it continued to rely upon these circumstances in relation to the August 2012 Variation. I do not consider that they cast any great shadow upon the decision to approve the August 2012 Variation. In particular: (i) the Ernst & Young report was not relied upon for the truth of its contents, which were hotly disputed by the respondents at the time and subsequently; (ii) the Landmark White preliminary valuation was on an “as is” basis but the land was not intended to be sold “as is”; (iii) the previous increases in the loan – which were not said to be any unreasonable breach of duty – show, at best, that the development had proceeded more slowly than expected because, as ASIC submitted, “a major portion of each of the previous loan increases, since November 2007, was also the result of capitalising interest”; and (iv) as I explain later, although construction had not commenced in September 2011 there were dramatic changes to the project between September 2011 and August 2012 and it had begun to move apace.

#### The parties to the August 2012 Variation

1. The variation in August 2012 was the final variation. It increased the loan to $280 million. It was executed by Maddison Estate (as borrower), The Trust Company (PTAL) Ltd (**The Trust Company**) (as lender), and Coomera Ridge (as mortgagor). It was not executed by LMIM. The reasons for that are as follows.
2. On 4 February 1999 a custody agreement was entered into between LMIM and The Trust Company (then named Permanent Trustee Australia Ltd) (**Custody Agreement**). The Custody Agreement was amended numerous times after 1999, but relevantly it was amended on 1 November 2011 to include the assets of the MPF.
3. The 1 November 2011 amending deed to the Custody Agreement was between LMIM and The Trust Company. It provided in Recital E that LMIM and The Trust Company agreed to amend the Custody Agreement to appoint The Trust Company as custodian of the MPF. It was common ground that this was a legal assignment of LMIM’s legal interest as lender in its position as trustee for the MPF. The Custody Agreement obliged The Trust Company to hold the assets of LMIM, clearly identified by reference to the relevant Scheme, separately from The Trust Company’s assets (cl 4.9). The Trust Company was also authorised to act (cl 5.2):

on Instructions in writing which bear or purport to bear the signature or a facsimile of the signature of any of the Client’s Authorised Persons or Instructions provided by electronic means using the security codes or procedures agreed between Permanent and the Client.

1. Since the Custody Agreement vested the assets of the MPF in The Trust Company on 1 November 2011, the final deed of variation of the Maddison Estate MPF Loan Agreement was executed by The Trust Company as lender. All other previous deeds of variation had been executed by LMIM as lender.
2. The final deed of variation was signed by Mr Franklin for The Trust Company (“Manager Property Infrastructure and Custody Services”) and by Mr Drake for Maddison Estate and Coomera Ridge, with the word “Sole” handwritten in parentheses after the word “Director” below his signature.
3. Although the deed of variation was prepared by the property department of LMIM (ts 347) after the MPF Credit Committee meeting on 7 August 2012, LMIM was not a party to the deed. It may have been intended that LMIM should be a party because of the provisions of cl 15 which refer to LMIM’s obligations under this deed. For instance, cl 15.1 provided that:

Trustee – [LMIM] enters into this Deed, the Loan Agreement and each other Security and the other parties to this Deed acknowledge that they are aware that [LMIM] enters into this Deed, the Loan Agreement and each other Security, in its capacity as the Trustee of the Fund, pursuant to the Fund’s Constitution and the other parties to this Deed are aware of the limited scope of [LMIM]’s obligations and powers under such Fund.

#### The date of execution of the August 2012 Variation

1. The August 2012 Variation was dated 1 July 2012. Mr Drake submitted that it may have been backdated. A difficulty with this submission is that if the final deed of variation was backdated substantially then this would mean that Mr Franklin, who did not give evidence, must have signed a document on behalf of The Trust Company which was dated months earlier.
2. Another apparent anomaly is that in an entry dated (Saturday) 30 June 2012, the loan account for the MPF provided for $9,800,000 as a loan “re-establishment fee”. In other words, the amount of the re-establishment fee was recorded in the loan account on the same day as the date of the variation, and not two months’ later when ASIC submitted that the variation was executed. It is possible, however, that this entry in the loan account for the MPF was also backdated. Clause 6 of the variation had provided that LMIM will capitalise this amount “to the Loan Amount on the Effective Date [30 June 2012]”. Indeed, the loan balance described in the synopsis on 25 July 2012 did not include the capitalised establishment fee of $9,800,000. And the transaction number for the re-establishment fee appears to fit in a sequence shortly after 30 July 2012, and prior to 9 August 2012.
3. On the other hand, there are strong reasons to conclude that the final deed of variation was executed and backdated some time after 1 July 2012. One of them is the transaction number of the re-establishment fee. Another is the amount of the re-establishment fee in cl 6 of the loan variation deed: $9,800,000 (3.5%). At the MPF Credit Committee meeting on (Friday) 29 June 2012, the amount which had been agreed was a fee of 3.75% ($10,005,792). As Ms Chalmers said, there had been discussion of the fee at that meeting. Subsequently, Mr Drake asked Mr Fischer to investigate the re-establishment fee by considering the fees charged by other equity lenders and mezzanine financiers, including a company called Alceon which had proposed a re-establishment fee of 3% to 3.5%. Mr Drake told Mr Fischer that MPF would charge Maddison Estate a similar re-establishment fee. At a meeting with Williams Partners Independent Audit Specialists (**WPIAS**), a sizeable auditor who had local property experience, on (Monday) 9 July 2012, a re-establishment fee of 3.5% ($9,800,000) had been included in the proposal.
4. Although it is likely that the deed of variation was backdated some time after 1 July 2012, it is unclear when the backdating occurred. It certainly occurred no later than 29 October 2012, when Ms Chalmers and Ms Kingston for LMIM wrote to The Trust Company, saying that LMIM “authorizes and directs [The Trust Company] to execute the following documents: 1. Deed of Variation (in duplicate)”. Ms Chalmers said in her letter that LMIM confirmed that The Trust Company is acting on the direction of LMIM and in their role as custodian. She asked that after execution, the documents be couriered to Ms Kingston of the LMIM office. Curiously, Ms Chalmers did not give any oral evidence about these matters.
5. On (Tuesday) 30 October 2012, the executed deed of variation was sent from The Trust Company with a letter requesting that an acknowledgement be signed and dated. The executed deed which was enclosed was not an exhibit at trial. It was unclear whether the executed deed was returned or whether the return was only the two pages which were included as an exhibit. Those two pages bear a striking resemblance to the signature pages of the executed deed dated 1 July 2012 with the exception that the word “Sole” under Mr Drake’s signatures on behalf of each of Maddison Estate and Coomera Ridge is not present.
6. On balance, I consider that it is likely that the final variation deed was signed by Mr Drake very shortly after the 7 August 2012 MPF Credit Committee meeting, and then backdated. It would have been executed by The Trust Company some time after that, no later than 30 October 2012.

## Suncorp’s concerns

### Suncorp seeking repayment of its Maddison Estate loan

1. From mid-2011, Suncorp began to take steps to recover its loan. By 22 September 2011, LMIM had recorded in a synopsis Suncorp’s desire for a “paydown” of its $38 million loan at a rate of $2 million a month for six months. Suncorp had told LMIM that it was not continuing with development loans and was reducing all of its facilities. It had commissioned Ernst & Young and Landmark White in the context of its desire to obtain substantial capital reductions, and for the loan to be repaid.
2. Each of Mr Drake, Ms Mulder, and Mr van der Hoven was aware of Suncorp’s desire to reduce, and obtain repayment of, its loan.

### The draft and final Ernst & Young reports and the responses

1. In January 2011, Suncorp commissioned Ernst & Young to analyse the Maddison Estate development. In July 2011, Ernst & Young provided Suncorp with a draft report. The draft report raised concerns about the proposed development. One concern was that the development was said to be targeted at first home buyers (who are typically price sensitive) rather than luxury second, third and fourth home buyers (who are typically attracted to community titled developments). They said that there may be difficulty selling the houses when there is an extensive supply of affordable housing in nearby competing developments that are not subject to community management schemes. The draft report raised concerns about getting the market to accept the product, including the layered community management scheme structure, due to expected competing developments in better locations. It was also suggested that the highest and best use was lower density housing.
2. On 21 June 2011, Mr Kurbatoff from Suncorp sent the draft report to Mr McDonald at LMIM. On 28 June 2011, Mr Kurbatoff emailed Mr McDonald saying that Suncorp’s main concerns were:
3. the designation of the Maddison Estate development for apartment use (high density) given competition to be provided in 3 to 5 years from land closer to Coomera town centre;
4. apparent inflexibility in the Preliminary Development Approval and allowable uses and densities for the site; and
5. the use of community title as opposed to outright freehold title.
6. Despite several follow up emails from Mr Kurbatoff, LMIM did not respond to the draft report until 29 July 2011. On that date, Mr McDonald responded with a report prepared by Matusik Property Insights Pty Ltd (**Matusik**) for LMIM, which was commissioned by Mr Young in response to the draft Ernst & Young report. Matusik had previously provided Young Land Corporation with a report in September 2007 and March 2011. As Mr Young told Mr Drake and others, he was “deeply disappointed” with the Ernst & Young report, thinking that they had not grasped the concept of the development (ts 418). Mr Young was engaged in the PAM team when he commissioned the Matusik responsive report.
7. The Matusik responsive report made various criticisms of the draft Ernst & Young report including the use of a case study by Ernst & Young which was said to confuse residential supply with resort and holiday accommodation, and to confuse the modestly priced product of the Maddison Estate development with a premium waterfront or golf-course product.
8. In 2011, Mr Young also commissioned two reports from RPS. One report, dated 28 July 2011, concluded that the Maddison Estate development, upon completion, would house approximately 3,645 people. Assuming that half of those people would require full time employment, there would be a demand for 1,823 jobs of which Maddison Estate would provide 840.
9. I accept the submission by ASIC that the purpose of the RPS reports and Matusik responsive report was to undermine the Ernst & Young report. The reason why these reports were obtained to undermine the Ernst & Young report was because the directors at LMIM considered that the Ernst & Young report was misconceived. These opinions were strongly held. Mr Young’s “deep disappointment” in the Ernst & Young report was shared by Mr Tickner, who emailed Mr Drake, Mr van der Hoven and others describing a “number of areas in which [the] draft report was severely lacking” and the alleged misunderstanding of “some very basic fundamentals”.
10. On 2 September 2011, a final version of the Ernst & Young development analysis report was sent to Mr Kurbatoff. Shortly afterwards, Mr Kurbatoff sent the report to Mr McDonald and Mr Tickner. The conclusions in the final Ernst & Young report were extremely similar to the draft report. There is little evidence that Ernst & Young had considered and responded to the Matusik responsive report in the final report. Although the covering letter bore the date 2 September 2011, the cover page of the final report purported to be a report dated June 2011.
11. It should be emphasised that the draft Ernst & Young report and the final Ernst & Young report were not admitted for the truth of their contents. Rather, they were admitted simply as matters about which the respondents were aware. However, the strength of the views within LMIM that the draft Ernst & Young report was based on misunderstandings, coupled with the responses of RPS and Matusik in their responsive reports, mean that, in the absence of proof of the contents of the reports, I do not accept that there were “serious concerns” (as ASIC submitted) arising from the Ernst & Young reports which should have led LMIM to undertake an independent assessment of committing trust funds to the development.

### The July 2011 preliminary valuation

1. In July 2011, after the draft Ernst & Young report had been obtained, Suncorp obtained a preliminary valuation from Landmark White which assessed the “as is” value of the Pimpama Land at between $35 million and $40 million based on a “highest and best use value”.

### The reductions in Suncorp’s loan

1. As Mr Kop explained, the loan from Suncorp was reduced from around $33.9 million in September 2011 to around $21.9 million in April 2012. The repayments to Suncorp were from the MPF. In the meantime, as Mr Fischer explained, LMIM unsuccessfully sought new financiers to refinance the Suncorp loan during late 2011 and early 2012.

## LMIM’s exit plan and the course of the development

### LMIM’s exit plan

1. On 16 August 2011, Mr Fischer replied to an email from Mr Tickner in which Mr Tickner was critical of the Ernst & Young report. Mr Fischer suggested that the MPF needed to refinance the Suncorp loan at the first available opportunity. Mr Fischer replied, telling Mr Drake and Mr van der Hoven and others that senior debt would be difficult to obtain. But additional debt was obviously necessary to advance the project. Therefore, the MPF needed to consider lending more money. Mr Fischer explained that the development team had said to him that a good approach was to get the project moving, and to start some early sales and marketing to generate income. He had also expressed this view to the directors (ts 372).
2. Although LMIM was aware that it needed to lend to get the project moving, it was also looking to exit the development. Mr Fischer explained that in late 2011 and through 2012, LMIM (and in particular Mr Fischer and Mr Ticker) was looking for new financiers to take over the Suncorp loan and also to pay out the Maddison Estate loan to Maddison Estate. The intention was that the MPF would be bought out (ts 325). Mr Fischer thought that obtaining a funder to take out MPF’s position was in the best interests of the MPF (ts 325). In the circumstances in which the MPF found itself, that view seems to have been reasonable. Indeed, in the audited financial reports for the year ended 30 June 2012, the auditors observed that LMIM “is currently in due diligence discussions and has received a conditional letter of interest from an offshore financier to fully repay the Suncorp facility on March 31, 2013 and also finance the full construction of the project to completion”.

### An enhanced and developed concept for the Maddison Estate development, and rapid improvement in 2012

1. As I have explained, Mr Young’s original vision for the Maddison Estate development involved 1,458 dwellings with initial land only sales, followed by house and land packages, and eventually sales of town houses and units. This vision continued for some time after the joint venture was terminated in April 2010. The Gold Coast City Council approved an amended plan on 6 May 2010.
2. By November 2011, Mr Drake began to enhance and develop the concept of the Maddison Estate development. Mr Drake’s plan became to sell blocks of vacant land via community title in a large setting. There would be a significant increase in the density of the buildings. The setting would comprise a number of public areas, including parks with a high level of embellishments, high tech recreational venues, and a town centre. Mr Drake planned a swim school headed by an ex-Olympian Ms Samantha Riley, a beach volleyball centre also headed by an ex-Olympian Ms Natalie Cook, and landscaping undertaken by a celebrity landscaper, Mr Jamie Durie. Later, Mr Drake added plans for a new model world first wave pool branded with a world renowned surfer, Mr Kelly Slater.
3. The minutes of a meeting on 23 November 2011 record the evolving changes which were being implemented by Mr Drake. They refer to Ms Riley and Ms Cook’s involvement through facilities leased by the Council. The sports facilities would be a “point of difference”. Mr Drake wanted to “go over thoroughly the entire design and Big Picture”; he wanted plans in Stage 1 for Village Square & Retail precinct, and public open space with an amphitheatre.
4. Unfortunately, there had been considerable delays. In late 2011, Mr Barnett, the development manager, was brought in to replace Mr Young and Mr McDonald and to get things moving (ts 208-209). Senior people within LMIM had considered Mr Young to have failed in his responsibilities, and to have caused the development to languish. Mr Fischer said that, by November 2011, there was mounting frustration amongst his senior colleagues with Mr Young’s inability to deliver the project (ts 297). On 16 November 2011, Mr Drake sent an email to Mr Tickner, Ms Darcy and Mr Fischer saying “Totally wasted 15 weeks. I am assuming control… Young is wasting our time and money”. Mr Tickner replied, saying a new employee would start in two weeks, and that “The plan is that he will control and manage the project and introduce the disciple David [Young] lacks”.
5. Mr Barnett said that before he started work for LMIM in late 2011, no work had been done on the development site at Pimpama. New approvals were needed for the proposed changes to the town centre and for earthworks (ts 209-210). From late 2011, Mr Barnett brought far more efficiency to the development. He was an impressive operator.
6. On 13 February 2012, Mr Barnett told Mr Drake and others that he had been advised by “all consultants and operators” that “the current internal location of the town centre is problematic and not desirable”. He said that the relocation of the town centre would be a “significantly improved outcome with respect to sale / lease success of the centre”. His initial thoughts were that the project construction and release timing may not be too adversely affected if the current approvals could be used.
7. By March 2012, Mr Barnett was on the cusp of receiving Stage 1 tree clearing approval. He had obtained the Stage 1 change of ground level approval. And the relocation of the town centre was approved in principle. Mr Barnett was also involved with negotiating long term arrangements with the celebrities who were associated with the embellishments. He negotiated in-principle agreements with Ms Riley and Ms Cook, signed a Memorandum of Understanding with Mr Slater, and engaged Mr Durie.
8. On 19 April 2012, Mr Barnett sent an email to various LMIM personnel including the respondents, saying that work was to commence on site in two weeks. He explained that the work would include tree clearing and demolition works for Stage 1. The total cost of the work was around $543,000 and the period of work would be two months.
9. The commencement of this work took around four weeks longer than expected. On 23 May 2012, Mr Barnett emailed various people including the respondents with an approval permit from the Gold Coast City Council authorising the commencement of the tree clearing works. Mr Barnett said that this would occur in the next two days. The respondents were jubilant. The work started on 25 May 2012.
10. Mr Barnett also obtained approvals for bulk earthworks to commence in February 2012, subject to approval from Suncorp. However, the date for commencement of the bulk earthworks was delayed to June 2012 due to funding issues (ts 214-215). The site was steep so the bulk earthworks would be expensive (ts 61; 305). Mr Barnett explored alternatives to the expensive process of earthworks such as “cut and fill” (ts 210). During the three months of financing delays, Mr King constantly asked Mr Fischer when the earthworks could commence. There was a growing need for the limit of the MPF loan to be increased to allow for this financing.
11. Between May and July 2012, as the respondents were aware, Mr Barnett entered into a non-disclosure agreement and exclusive dealing period with the Kelly Slater Wave Company and planned a preliminary configuration of the Kelly Slater Wave Pool. Also, as Mr Drake informed the other respondents in July 2012, “Sam Riley is locked in for the fitness and swim centre. Natalie Cook is the same for the beach volleyball… Have also signed up Jamie Durie for all landscape and tv advertising… Also we have an exclusive agreement with Kelly Slater for a world first never ending Wave park to go into the estate. This completely puts Australia, LM and the Managed performance fund onto the world stage”.
12. In May or June 2012, there had also been discussion between the directors about increasing the density of the Maddison Estate development to increase its profitability. The suggestion had been that increased density would be around the area of the wave pool (ts 213). Mr Barnett gave evidence, which I accept, that by May or June 2012, the Gold Coast City Council was happy to accept the proposed increased density for the development (ts 219). Mr Barnett, who was a reasonable and measured witness, reasonably considered that the higher density in the order of around 800 extra dwellings was potentially of very significant advantage to the profitability of the Maddison Estate development (ts 214).

## The August 2012 Variation and the circumstances preceding it

### The early 2012 synopses

1. From February 2012, not long after the approval of the September 2011 loan variation, Mr Barnett also prepared synopses proposing another variation to the Maddison Estate MPF Loan Agreement. As I have explained, the September 2011 loan variation had been explained in the email from Mr Tickner on 25 September 2011 as being an extension “based upon the funding required until end March 2012 on the basis of anticipated project related costs, Suncorp’s amortisation requirements interest and also MPF’s interest”.
2. The first of the synopses produced by Mr Barnett was dated 27 February 2012. This proposal was to increase the loan from $180 million to $290 million. Mr Barnett was assisted by Ms Chalmers, Ms Lough, Mr King and Ms Kingston.
3. Mr Barnett subsequently assisted to prepare a revised synopsis dated 30 March 2012 that was then provided to the MPF Credit Committee. The synopsis included the following:

* The development is to be undertaken in stages. Stage 1 is anticipated to commence April 2012 with completion of Stage 1 anticipated 12 months from commencement.
* The revenue from Stage 1 is approximately $35M, these inflows should start around December 2012.
* First Mortgage funding is with Suncorp with a current debt of $23.8M. Suncorp are not continuing with development loans and are reducing all of their facilities. Suncorp have agreed to extend the term to 31.5.12.

…

* Marketing meetings are being held fortnightly in preparation for the large campaign due to commence later this year.

…

* The Development team believe that once the Suncorp facility is down to $22M, a refinance will be able to take place with another financier.

1. A key part of the 30 March 2012 synopsis was in the same terms as the synopsis for the September 2011 variation. That is that the purpose of the increase was again to cover the principal reductions and interest on the Suncorp loan, interest on the MPF facility (“currently $3.5M p/m and capitalising”) and marketing, consultants’ costs, civil works and development costs for Stage 1 completion.
2. The 30 March 2012 synopsis said that the “positives” of a SWOT analysis included: (i) significant uplift in land values anticipated; (ii) development profits; and (iii) a strategic large development parcel in the Coomera region identified for future urban growth by State and local governments. The only “negative” of the SWOT analysis was the current property market conditions.
3. ASIC submitted that the proposed August 2012 Variation was significantly different from the September 2011 loan variation because the latter was described in the 22 September 2011 synopsis as (with emphasis added) “to increase the loan *in the short term*, to keep the loan compliant”. In contrast, ASIC said, the 30 March 2012 synopsis described the request as “to increase the loan *for Stage 1 completion*, to keep the loan compliant”. I accept this submission. As Mr Ticker had said in his email on 25 September 2011, the September 2011 variation was only intended to provide funding through until the end of March 2012. Another difference was that the 22 September 2011 synopsis anticipated refinancing of the Suncorp loan in February 2012. This had not occurred, so payments of principal and interest of $2.35 million a month were continuing at 30 March 2012.
4. Unlike the 22 September 2011 synopsis for a variation for a $200 million loan, the 30 March 2012 synopsis attached a “cash flow”. That “cash flow” showed the manner in which the proposed extension from $180 million to $280 million would be used to provide project funding. The title “cash flow” is misleading. Substantial amounts of cash did *not* “flow” at all. For instance, the “cash flow” showed monthly capitalising interest on the Maddison Estate loan increasing from around $3.4 million in March 2012 to more than $5.6 million in March 2013. The total amount contained in the “cash flow” which did not flow *from* the MPF between October 2011 to March 2013 was $74,759,809. None of this amount would be paid from the MPF to Maddison Estate. They simply represented a book entry increase in the loan.
5. Another notable feature of the cash flow is that it was projected that $14,214,629 in funds would be needed to make repayments of interest and principal for the Suncorp first mortgage. The respondents could reasonably have expected that if there was default on the Suncorp mortgage, and Suncorp foreclosed and sold the property before Stage 1 had been completed or another financier found, then there might be little chance of recovery of any of the loan.

### The MPF Credit Committee meeting on 4 April 2012

1. By the end of March 2012, the loan balance of the Maddison Estate MPF Loan Agreement was $177,766,781.23. This was very close to the approved limit of $180 million which was granted for the period up to the end of March 2012. This conclusion is drawn from the synopsis which was prepared for the MPF Credit Committee at the end of March 2012. It is not drawn from the ledger for the loan account which was an exhibit at trial but which was not a contemporaneous record of the loan. As I have explained above, the ledger included backdated entries which affected the running balance but which were based on later events.
2. On 4 April 2012, there was a meeting of the MPF Credit Committee. Those attending included Ms Mulder and Mr van der Hoven. The minutes of the meeting described the purpose of the meeting being “to enable forward movement of Stage 1 (134 lots) and interest coverage”. The minutes recorded the following:
3. discussion in relation to Suncorp (as senior funder) and proposals for a future senior funder. The synopsis presented to the MPF Credit Committee prior to the meeting had observed that it was considered that it would be difficult to get senior funding at this point in the project but that this would be more likely once Stage 1 was complete;
4. construction documents were still to be finalised although construction costs had been tendered; and
5. active marketing was starting in June or July 2012 (which was a delay from the expected late 2011 marketing date in the September 2011 synopsis for the previous loan extension).
6. The MPF Credit Committee deferred approval of the proposed loan variation pending a meeting to be held one week later. The minutes explained that the MPF Credit Committee took the view that “being a related party transaction, it is premature to approve such a large increase at this point and advised that that it would like to review an updated whole of site feasibility cashflow”.

### The informal meeting on 4 June 2012

1. Mr Fischer’s evidence, which I accept on this point, was that on 4 June 2012, as Chief Financial Officer, he had a meeting with Mr Drake, Mr Tickner, Mr van der Hoven and Ms Darcy (but not Ms Mulder). Mr Fischer wrote minutes of the meeting immediately afterwards.
2. At the 4 June 2012 meeting, Mr Fischer said that the LM Group could not sustain its current level of expenses. He said that the amount of money accounted as prepaid fees ($25 million) was not sustainable, and that the closed funds owed $4 million to LMIM as trustee for the MPF. He proposed an action plan involving matters which included:
3. placing more of the MPF assets on the market to provide liquidity;
4. taking a fee of 3% for the MPF;
5. drawing fees of over $6 million;
6. restructuring staffing and ceasing the profit sharing arrangement; and
7. selling the Sydney office.

### Mr Fischer’s 14 June 2012 report

1. The meeting of 4 June 2012 was followed by a written report by Mr Fischer which was dated 14 June 2012 and which I am satisfied was sent to the other directors of LMIM by email, including Mr Drake, Ms Mulder, and Mr van der Hoven. Mr Fischer’s report observed:
2. there was a backlog of current cash payments owed by the LM Group totalling “$2,552,000+”, and that it was “at a critical point and must be repaid” with a plan Mr Fischer formulated;
3. current cash requirements for the LM Group averaged $2.5 million per month;
4. the closed funds owed the LM Group $3.9 million in management and loan fees;
5. the MPF had taken fees of $25 million which needed to be expensed;
6. LMIM had not charged “any real management fees that we are entitled in that fund for over 3 years”;
7. if a full management fee were taken up by the MPF then group earnings before interest and tax would be $20 million; and
8. it was imperative to reduce expenses across the board by at least 35%.

### The June feasibility reports from Mr King and Mr Barnett

1. Some time after Ms Scott was made redundant in May 2012, Mr Fischer instructed Mr King and Mr Barnett to produce a revised feasibility report using the Estate Master software. Mr King and Mr Barnett worked on this feasibility report from May to July 2012. They produced numerous iterations of a draft feasibility model.
2. The mechanical part of Mr King and Mr Barnett’s work on the model involved inputting project costs and revenues. As I have explained above, the cost figures were obtained from consultants, and the revenue inputs were researched by the sales team from independent reports and other research such as market sales prices, real estate agents and sales reports.
3. As I have explained, apart from the cost and revenue inputs, the remaining variables were the escalation rates and discount rates. Mr Barnett’s evidence was that, in his experience, it was usual to obtain the escalation rates from an independent property analyst. On 2 July 2012, Mr Barnett sent Mr King an Excel spreadsheet entitled “Price Escalation Analysis”. The spreadsheet contained preliminary historical research on Gold Coast escalation rates obtained from the independent agencies RP Data and BIS Shrapnel.
4. One of the first feasibilities produced by Mr King and Mr Barnett was a “Land Only” feasibility. The escalation rates used were between 0% and 15% per year, with an average of 8% per year. Mr Fischer described this feasibility as an “alternative” (ts 307). Although Mr Fischer was generally a careful and considered witness, I do not accept that this was an “alternative” in anything other than an Armageddon scenario. A “Land Only” project was never a realistic alternative for LMIM. As Mr Fischer conceded, if a land only sale had ever been a realistic option then the loan from the MPF would have been impaired (that is, not fully recoverable) as soon as it was made. But it was never recorded as impaired and the Maddison Estate development was always promoted as involving a full build (ts 307). The Land Only feasibility was nothing more than to understand the value of a last resort, uncontemplated, sale of the land without development. When Mr Fischer brought the Land Only feasibility to a feasibility meeting in June 2012 Mr Drake said that he was not interested in a land only subdivision and sale because the site was going to be developed.
5. A more realistic feasibility produced by Mr King and Mr Barnett was a “Land and Build Out” feasibility. That feasibility used the same growth rates as the Land Only feasibility. Mr King said that it resulted in a net present value of around $150 million to $160 million, which was below the outstanding loan balance owed to the MPF at that time (potentially close to $190 million).

### Mr Fischer’s concerns at the Sheraton hotel on 20 June 2012

1. On 20 June 2012, Mr Fischer raised his concerns about the financial position of the LM Group at a directors’ finance meeting at the Sheraton hotel. He said, and I accept, that all the directors attended this meeting. Mr Fischer took minutes and he recorded an action plan from this meeting, which was sent to the directors.
2. Mr Fischer’s minutes described how:
3. LMIM was forecast to take $31 million in management fees from the MPF in the 2012 financial year;
4. the only revenue from the fund during the year was the development management fee income from Maddison Estate; and
5. the group profit for the LM Group was estimated at $8.4 million for the 2012 financial year which included a 4% loan re-establishment fee.
6. Mr Barnett gave evidence, which I accept, that at the meeting he and Mr King presented escalation rates of “between 4% and 6% initially, and peaking at 15% following the delivery of major infrastructure, parks and facilities within the development”. Mr Drake and Mr Tickner proposed escalation rates much higher than this. Mr King and Mr Barnett said that the higher escalation rates were too aggressive.
7. Ms Darcy resigned as a director on 21 June 2012, the day after the meeting, for what was only described as personal reasons.

### The MPF Credit Committee meeting on 29 June 2012

1. On 29 June 2012, the MPF Credit Committee met again to consider an increase in the loan limit of the Maddison Estate loan. Mr Drake and Ms Mulder attended the meeting.
2. The loan balance at that time had already exceeded the $180 million limit by over $10 million. Mr King emailed the members of the MPF Credit Committee ahead of the meeting, attaching a synopsis prepared by Mr Barnett for a proposal to increase the limit of the loan from $180 million to $280 million.
3. The synopsis, dated 28 June 2012, was considerably more developed than the synopsis which was dated 27 February 2012. The extended limit had been reduced from $290 million to $280 million. The synopsis noted that the loan increase was to cover the following:
4. the then current loan balance of $190,902,442;
5. interest on the Suncorp loan facility until November 2012 of $1,073,784;
6. interest on the MPF loan facility until 30 June 2013 of $59,430,410;
7. anticipated development costs until 30 June 2013 of $15,414,490; and
8. capitalisation of a loan re-establishment fee of $10,005,792 payable by Maddison Estate.
9. The final amount, the $10 million loan re-establishment fee, was not mentioned in the 27 February 2012 synopsis that Mr Barnett prepared (with the help of others including Mr King). The loan re-establishment fee had not been charged for any previous variation. Mr Fischer’s evidence, which I accept on this point, is that Mr Drake instructed Mr Fischer to charge a re-establishment fee to the MPF. At the time of the 20 June 2012 meeting at the Sheraton, the fee that Mr Drake had suggested was 4%. Mr Drake asked Mr Fischer to investigate a percentage for the fee (ts 308). It was reduced to 3.75% in June and then to 3.5% in August (ts 178). Ultimately, the amount which was agreed was 3.5%.
10. The 28 June 2012 synopsis also referred to numerous new matters:

* Phase 1 Tree clearing and demolition has commenced on site… These works due to complete mid July 2012 with bulk earthworks programmed to commence at that time;
* Stage 1 will deliver a total of 120 residential lots, 7 commercial properties and 3 parks;
* The Sales Office is 70% complete and we anticipate a launch date in the last quarter of 2012…;
* Natalie Cook has committed to operate a Sandstorm Beach Volleyball facility in the central park – MOU being drafted;
* Sam Riley has committed to operate a Sam Riley Swim School also located within the central park – MOU being drafted;
* Jamie Durie shall be appointed as the lead landscape design consultant;
* Kelly Slater Wave Company – MOU and Exclusive Dealing Period Agreement signed 28.6.12 – proposed JV; and

…

* … We are also working towards having the Suncorp debt repaid/refinanced in approximately November, 2012 through the Canadian capital raising.

1. The 28 June 2012 synopsis also noted that the feasibility for the whole project was being reviewed and should be finalised by 6 July 2012.
2. The minutes of the MPF Credit Committee meeting on 29 June 2012 show that the committee noted the proposal to use the Canadian capital raising to pay out the Suncorp loan. There were also queries raised by the committee about the “swim centre, volleyball centre, wave pool centre and commercial component and what supporting data have been obtained to support the feasibility”.
3. Mr Fischer’s evidence, which was generally very impressively and carefully given and which I accept, was that he expressed concerns that there was no current external land or project valuation. He said that the assessment of value was based on a projected value of the completed development, and that the feasibility figures must be independently reviewed. Ms Chalmers’ evidence, which I also accept on this point, was that Mr Drake said that the feasibility did not take into account enough new features of the project and that it should be redone.
4. The MPF Credit Committee’s comments on the synopsis show that the committee considered that comprehensive due diligence was required to be finalised before initial settlement, and that the due diligence would include: (i) detailed risk assessment; (ii) financial analysis; (iii) legal sign off; (iv) engagement of experienced professional personnel as required; (v) compliance with internal compliance program; and (vi) set up of processes for ongoing monitoring and managing assets. There was committee approval, although not final approval, for a 3.75% re-establishment fee (which was later reduced to 3.5%). The committee also gave preliminary approval for the loan expiry date to be amended to 30 June 2013 (rather than 13 November 2014) so that the loan could be reviewed annually. The MPF Credit Committee resolved to meet on 6 July 2012 by which time a feasibility and supporting information could be reviewed in more detail.
5. Seven of nine MPF Credit Committee members approved the proposal in principle including Mr Drake (as chair), and Ms Mulder. After the meeting, however, Mr Fischer sent an email to Ms Chalmers saying that he wanted to see a feasibility report before he voted. However, as Ms Chalmers said, Mr Fischer had not told those at the meeting that he was not voting (ts 176). Ms Chalmers, prompted by Mr Tickner, also subsequently considered legal advice concerning whether Mr Drake should have voted.

### Preparation of further feasibility reports prior to 11 July 2012

1. In early July 2012, there were numerous meetings held between the directors, including Mr Drake, Mr van der Hoven, and Ms Mulder. Numerous feasibility models were also prepared by Mr King and Mr Barnett and presented to various directors.
2. A matter of significant dispute concerned the instructions given to Mr King and Mr Barnett for the preparation of these further feasibilities. As I have explained, the first feasibility that they had produced (other than the almost irrelevant Land Only feasibility) had resulted in a net present value of around $150 million to $160 million, falling below the outstanding loan balance of potentially $190 million owed to the MPF.
3. Mr King’s evidence was that Mr Fischer instructed him and Mr Barnett to prepare a scenario showing what assumptions would be required to recover the outstanding balance so Mr Fischer could then discuss it with the other directors. Mr King said that shortly after this, Mr Drake paid a visit to him and Mr Barnett. Mr King said that Mr Drake told them that the directors were talking to Pacific Alliance Group and Wall Street First Capital to obtain external funding so Mr Barnett and Mr King should prepare the feasibility model on the assumption that it would be completely funded.
4. There are difficulties with Mr King’s evidence on this issue. One of them is that Mr Drake could not have told Mr King in this conversation about Pacific Alliance Group and Wall Street First Capital. Those lenders were not approached until September 2012 (ts 80-81) and November 2012 (ts 81-82) respectively. Mr Fischer, who was generally an impressive and careful witness, gave evidence which I consider was generally more reliable than that of Mr King. Mr Fischer said that Mr Drake told him that the feasibility report for the Maddison Estate development should be based on achieving “full recoverability”, or “full recovery”. The feasibility report which was later emailed from Mr King to the directors on 11 July 2012 contained the words “Full Recovery” in the file name. I am satisfied that Mr Drake told Mr Barnett and Mr King (both directly at meetings, and indirectly by telling Mr Fischer with the intention that Mr Fischer would tell Mr Barnett and Mr King) that a feasibility should be prepared on the basis of full recovery. “Full recovery” meant that the whole of the outstanding loan would be recovered. This required gross revenue of $1 billion.
5. There was a reason why Mr Drake attached considerable importance to the prospect of full recovery. If the feasibility report did not predict full recovery then accounting standards had the effect that the loan would need to be impaired (ts 311). This would also mean that the unit price of units in the MPF would be reduced. This was a consequence which Mr Drake was very keen to avoid.
6. Mr King described the process by which he and Mr Barnett adjusted the feasibility report so that it showed what was needed for full recovery as Mr Drake had suggested. They knew that an escalation rate of 8% compounding per year was not enough to recover the loan balance. So they tried 10%, then 15%, and increased the rate until they arrived at an approximate 20% to 25% per annum compounding escalation rate which recovered the loan balance. Mr King then told Mr Fischer that the escalation rates had to be approximately 20% to 25% per annum to recover the loan balance.

### The 11 July 2012 meeting of the LMIM directors and others

1. On 11 July 2012, a meeting was held to discuss the Maddison Estate feasibility which showed full recovery of the loan. The room was full, with 12 or more people present. The attendees included Mr Drake, Ms Mulder, Mr van der Hoven, Mr Tickner, Mr King, Mr Barnett and Mr Fischer. Mr O’Sullivan and Ms Phillips were also there.
2. The meeting lasted for less than an hour. Different versions of the meeting were given in evidence although there were some matters which were common to all accounts. The lack of recollection of specifics is unsurprising given the elapse of years. But there were some matters at that meeting which were very significant and which were generally remembered by those to whom the matters were the most significant.
3. Mr King’s recollection of the meeting was the clearest and on this issue, I am satisfied, the most reliable. As he explained, the meeting commenced with a presentation by Mr Barnett updating the attendees about the various celebrity endorsements. Mr Barnett and Mr King then described the assumptions that would be required for the feasibility model to achieve full recovery. They explained that 20% to 25% per annum compound growth rates meant that block prices and apartment prices would exceed $1 million by the end of the cash flow period. Mr Drake said that he thought this was conservative.
4. In his presentation at the meeting, Mr King compared the 31 December 2011 feasibility report with the 30 June 2012 feasibility report. This comparison would have involved an explanation that the 31 December 2011 feasibility had used compound growth rates of around 6% to 7%, and an average end block price of $452,550. In contrast, the feasibility produced six months later on 30 June 2012, had used compound growth rates of around 20% to 25% and an average end block price of $1,191,571 to show recovery of the loan. Mr Drake nevertheless remarked that the latter feasibility was a conservative estimate.
5. Much of the meeting then concerned a discussion about the escalation rates. Although Mr Barnett had a very poor recall of the specific details of the meeting, I accept his evidence that the discussion became heated. Mr Barnett informed the directors that he was not comfortable with the escalation rates, and that he could not find anything comparable to support those rates. Mr Drake said that the feasibility, which must have been a reference to the 31 December 2011 feasibility, did not account for the true value of the new features of the development (ts 256). Someone, probably Mr Drake, remarked that once the various enhancements were delivered, there would be a huge uplift to the project and so the escalation rates would be highest following those years. Others expressed concerns about the escalation rates. I accept Mr van der Hoven’s and Ms Mulder’s evidence that they asked questions but did not support the escalation rates. Neither felt that he or she had the experience or knowledge to take a position in relation to the escalation rates. Mr van der Hoven had also been away on holidays before the meeting and felt that there had been discussion on the topic of escalation rates while he had been away, to which he had not been a party.
6. One of the others at the meeting, possibly Mr Fischer, told Mr Barnett and Mr King to vary the escalation rates for the feasibility model so that they would *range* from 4% to 50% per annum. Others, including Mr Drake and Mr van der Hoven, also observed that there was a need to vary the discount rate from 25% to 16% over the life of the project because the project would “de-risk over time”.
7. Mr van der Hoven, whose evidence I accept, said that on the same day, some time after the meeting had concluded and Mr van der Hoven returned to his office, Mr Drake came into Mr van der Hoven’s office. Mr Drake invited Mr van der Hoven to join another meeting. The second meeting lasted only about 20 minutes. Mr Fischer, Ms Scott and Mr Barnett were also there. Mr Drake then said that he would leave the room so that he could not influence the meeting. He left. Mr van der Hoven made some comments about the interest rate on the screen where the feasibility was shown. Mr van der Hoven thought that the interest rate was concerned with cost of capital but, in fact, it was concerned with the discount rate. There was discussion about the escalation rates. Mr van der Hoven asked questions about how the escalation rates worked and the impact of the changes to it. He did not offer any opinion.
8. Mr van der Hoven and Mr Fischer then had a further discussion as everyone was leaving the second meeting. Mr Fischer asked Mr van der Hoven what he thought, which Mr van der Hoven took to be a reference to the feasibility. Mr van der Hoven replied that he did not know but that once the project commenced then there would be hard numbers which would need to be adjusted daily. Mr Fischer suggested to Mr van der Hoven that they should not approve the loan increase unless the MPF auditors had first looked at the feasibility and were comfortable with it. Mr van der Hoven agreed. Mr van der Hoven had a discussion with Ms Mulder to the same effect.
9. Following the first meeting, Mr King revised the feasibility report and, in an email at 5.40pm on 11 July 2012, he sent the revised report to Mr Drake, Ms Mulder, Mr van der Hoven, Mr Tickner, Ms Phillips and Mr Fischer, and said:

Please find the latest model as discussed today incorporating your comments. The growth rates have been adjusted as [Mr van der Hoven] suggested which results in back end prices of $1.05 million for a typical block and $1.47 million for the larger blocks. Apartments are around $1.4m to $1.5m in 2018.

... The average compound growth rate is around 21% per annum for land and 24% for apartments.

…

Feel free to give me a buzz if you want a hand driving the model.

…

As mentioned, the model assumes Suncorp is paid out in November by an external funder, who then funds all project costs from December 2012 onwards at an interest rate of 11%. Senior debt peaks at $59.15m in August 2015. This is based on [Mr Tickner’s] advice regarding the Canadian capital raising LM is currently undertaking.

MPF continues to fund Suncorp’s interest up-to an [sic] including November 2012. MPF’s lending commitments total around $15.14 million over the next 5 months or around $3 million per month. Inflows into the fund commence in October 2013 and total around $23.1 million for the 2013/14 financial year based on the assumptions. That figure increases to $90 million in the 2013/14 financial year and is solely dependent on sales success at the prices assumed.

Over to you to advise what changes you would like to make to finalise the Directors’ valuation.

1. Although Mr King referred to Mr van der Hoven’s suggestions about growth rates, I consider that it is unlikely that this remark was made by Mr van der Hoven. In his affidavit Mr King said that he cannot recall who had “said what”. In oral evidence, Mr King eventually conceded that he could not recall Mr van der Hoven saying this at the time of his evidence (ts 100). It may have been that Mr van der Hoven’s remarks about the discount rates led Mr King to incorrectly attribute to Mr van der Hoven the suggestion of using lower and higher growth rates to achieve the average of around 25%. But, whatever the reason, I am satisfied that Mr King’s reference in his email to Mr van der Hoven, albeit shortly after the meeting, was an error. This was the first time Mr van der Hoven had seen a working feasibility model. Mr van der Hoven gave evidence, which I accept, that he did not correct the email because he was not sure what was meant by growth rates (ts 682).
2. Mr King’s email attached the revised feasibility. ASIC tendered a feasibility which was said to be the one attached to Mr King’s email. But Mr King was uncertain whether this was the correct feasibility. The feasibility is 113 printed pages. It shows a net present value of $235,969,222. This was considerably greater than the $204 million shown in the 30 June 2012 feasibility report which had also shown full recovery (ts 311). The discount factor had been reduced from 25% to 16%. The escalation rates for the first five years for residential lots were: 4%, 50%, 50%, 30%, and 15%. Thereafter the escalation rates were 5% per annum. The escalation rates for the first five years for apartments were the same as those for residential lots. Mr King was uncertain that the feasibility was the one attached to his email because he did not recall producing a feasibility with a net present value of more than $235 million.
3. As Mr Barnett explained, this and subsequent feasibility models were entitled “Directors’ Valuation” because of the concerns that he and Mr King had about the escalation rates. Mr Fischer also had concerns about whether the escalation rates could be supported but he accepted that this was not his area of expertise (ts 312). He told the other directors of his suggestion that the model should be considered by the MPF external auditors (ts 312). The others agreed.
4. On 13 July 2012, Mr Tickner resigned as a director.

### The audits by WPIAS and its 12 July 2012 consideration of a feasibility report

#### The knowledge that the auditors had of the Maddison Estate development

1. Mr Fischer chose a sizeable auditor, WPIAS, who had local property experience to consider a feasibility model of the Maddison Estate development. By the time that WPIAS considered the feasibility model in July 2012, WPIAS had significant background knowledge of LMIM and Maddison Estate.
2. By a letter dated 5 October 2011, WPIAS had been engaged to audit the financial reports of the MPF for the financial year ending 30 June 2011. As Mr Williams explained, it was not within the scope of WPIAS’s engagement to audit or verify any projects associated with MPF’s loans, or any development feasibilities. However, as he recognised, the Maddison Estate loan was the largest loan in the MPF loan book. Indeed, it was the largest by a long way. WPIAS was provided with Estate Master feasibility models relating to the Maddison Estate development, and was given a presentation on the development on 12 December 2011. WPIAS undertook a high level review of a sample of the project feasibilities associated with MPF loans to determine whether any of those loans showed any indications of impairment. The Maddison Estate development was considered. No impairment was found.
3. The WPIAS audit considered a development feasibility for Maddison Estate. The feasibility was dated 17 January 2012 and it showed projected sales revenue escalation figures of between 5% and 15% per annum, compounding monthly. WPIAS considered whether the costs appeared reasonable, whether the sales projections appeared overstated, and whether there were any anomalies such as unusual discount rates. Mr Williams said that he considered that the 25% discount rate was medium to high, and therefore conservative (ts 465). However, Mr Williams also said that he thought that the projected sales revenue escalation figures of between 5% and 15% were on the high side, and that they would need to be justified if WPIAS were ever instructed to audit the Maddison Estate development. A file note by Ms Blank recorded the advice about an audit of the Maddison Estate development (which the board of LMIM did not consider necessary) but the file note did not mention any concern about the escalation rate. Curiously, in oral evidence Mr Williams said that he considered that the end sale prices were supported by market analysis (ts 465). The end sale prices were the prices *after* escalation. I do not accept Mr Williams’ evidence that *at the time* he thought the projected sales revenue escalation figures of between 5% and 15% were on the high side. That evidence is more likely to have been the product of a determination after the event of the collapse of the Maddison Estate development.
4. Mr Williams accepted that although the 2011 audit considered the Maddison Estate loan at a high level, it involved a careful consideration of the assumptions underlying the feasibility, both as to revenue and as to costs (ts 464). He said that whenever he looked at a client-prepared document he did so with a sceptical mindset (ts 467). WPIAS concluded that the Maddison Estate loan was not impaired (ts 466). The financial report was expressed as giving a true and fair view of the Scheme’s financial position. The auditors’ opinion was unqualified (ts 464).

#### The 17 July 2012 meeting with WPIAS

1. Prior to 12 July 2012, WPIAS had completed its audit of the MPF for 2011 and was preparing for the 2012 audit (discussed further below). Mr Williams and Ms Blank had also attended a meeting on 9 July 2012 for the 2012 audit.
2. On 12 July 2012, the day after the 11 July 2012 meeting, Mr Fischer emailed Mr Williams and Ms Blank at WPIAS (carbon copied to others including Mr Drake, Mr van der Hoven and Ms Mulder), and said:

We have the Maddison Feasibility in draft form to run through with you early next week if you are available.

Fran, Luke and myself will talk you through the updated financial feasibility and model drivers.

We will then submit the complete file for you to review and then meet again to talk further around the pitch and marketing coming off the discussions in the meeting with Peter when you were here last Monday.

1. As Mr Williams accepted in cross-examination, the purpose of the meeting was plainly to consider the Maddison Estate feasibility and for Mr Fischer to talk him through the updated feasibility and drivers (ts 467). He knew, and the LMIM directors could reasonably have expected that he would know, that the feasibility was to be considered in relation to the value of the loan from LMIM (ts 472).
2. A meeting was proposed by WPIAS for 17 July 2012.
3. I accept ASIC’s submission that neither this 12 July 2012 email, nor any conversation prior to 17 July 2012, had engaged WPIAS to audit the Maddison Estate development feasibility. It did not do so. Mr Williams explained, and I accept, that an audit of the Maddison Estate development would have involved examination and verification of as many inputs as possible (ts 491).
4. I also accept that at the meeting on 17 July 2012, neither Mr Williams nor Ms Blank was asked for any final opinion concerning the Maddison Estate development feasibility. Nor were Mr Williams and Ms Blank informed that any opinion they offered might be used by the MPF Credit Committee in considering a further loan to Maddison Estate.
5. Although the meeting could not reasonably have been understood as an audit nor even as a comprehensive assessment of the Maddison Estate development, Mr Drake, Ms Mulder and Mr van der Hoven would reasonably have been aware that Mr Williams was a very experienced accountant who (as he accepted) had significant familiarity with the Maddison Estate development from the 2011 audit. Mr Williams had even participated in a site visit on 1 March 2012. The directors would reasonably have realised that Mr Williams would have quickly been able to form a view about whether the escalation rates were reasonable or not. And Mr Williams did express views at that meeting.
6. On 17 July 2012, Mr Fischer, Ms Mulder and Mr Barnett met with Mr Williams and Ms Blank from WPIAS. The meeting considered the details of a feasibility in the context of a pending audit engagement. The email which requested the meeting was not framed in marketing terms. And it would have been clear at the meeting that the consideration of the feasibility was very important to the attendees from LMIM. Mr Fischer described it as “pivotal”.
7. I do not accept the evidence of Mr Williams and Ms Blank that the meeting was a marketing presentation. Whether or not they subjectively believed that it was, a reasonable auditor would not have understood it in that way, and a reasonable person in the position of Mr Fischer, Ms Mulder or Mr Barnett (or Mr Drake and Mr van der Hoven when they were later informed about the meeting) certainly would not have considered that the meeting was a marketing meeting.
8. I consider the evidence from the LMIM attendees about their recollections of this meeting to be more reliable than the evidence of Mr Williams or Ms Blank. The meeting was much more important to the LMIM attendees, and much more was dependent upon the meeting for them. Mr Williams also admitted that he could not recall the meeting well (ts 469). Of the LMIM attendees, the evidence of Mr Fischer was the most reliable. I also accept the evidence of Ms Mulder, particularly about the ultimate conclusions from the meeting and statements made at the meeting which were the most important to her. Both Mr Fischer and Ms Mulder were honest witnesses and the key points about which Ms Mulder gave evidence were matters which were of significant importance to her going into the meeting and would have impressed upon her memory. The other attendee at the meeting, Mr Barnett, was not a witness who I found to be as reliable in relation to that meeting. He was confused in his recollection of his role at the meeting. Initially he said that he did not give a presentation but later he accepted that he did. I am satisfied that his confusion was honest but his recollection of the meeting was not strong.
9. The meeting went for around two hours. There was discussion about the starting prices and the escalation rates. I accept Mr Fischer’s evidence that Mr Barnett gave an update on the development and spoke for about 30 minutes including about the development’s various attributes. Mr Fischer explained that for his presentation, he put parts of the feasibility model on a screen. I consider that those parts would have likely included the escalation rates which were a “model driver” to which reference was made in the email to Mr Williams on 12 July 2012. Mr Williams also accepted that escalation rates would have been discussed (ts 468). I am satisfied that there would have been a significant emphasis by Mr Fischer on these escalation rates in the presentation. One reason why these would have been emphasised by Mr Fischer was the debate which had occurred within LMIM about these rates. Mr Fischer gave evidence that he had made sure that the reason why he was speaking to the feasibility was because he wanted to point out clearly the figures that were driving the feasibility model (ts 342). Mr Fischer also accepted that these were the important figures, and that he was anxious to present the feasibility study in a clear, fair, and proper way, and was especially careful to tell WPIAS about the escalation rates that were built into the model (ts 343).
10. I am satisfied that the feasibility which was presented to WPIAS on 17 July 2012 was the one which was later attached in emails to Ms Blank on 24 July 2012 and 25 July 2012 (described below). That feasibility was for the Maddison Estate development with 780 lots, 41 additional duplexes, 591 apartments, and commercial operations.
11. This 17 July 2012 feasibility upon which I infer that Mr Fischer presented was different in some key respects from the 30 June 2012 feasibility or the 11 July 2012 feasibility. Although the 17 July 2012 feasibility included the same escalation rates for residential lots as the 30 June 2012 feasibility (4%, 50%, 50%, 30% and 15% for the first five years), the escalation rates for completed apartments were substantially reduced to 4%, 25%, 25%, 15% and 15% for the first five years and then 5% thereafter. The net present value was also substantially reduced from $235 million to just under $169 million. The gross realisation value was $1 billion.
12. In Mr Fischer’s presentation, he showed key aspects of the model including starting prices and escalation rates. Although Mr Williams could not recall details of the presentation, he said that a 50% escalation rate would have been a complete outlier which he would have noticed without the need to study Estate Master carefully (ts 469). However, I am satisfied that Mr Williams was referred to the escalation rates, and that they were put up on a screen during the presentation. Although none of the witnesses gave evidence that Mr Williams or Ms Blank was informed that the escalation rates had been the subject of dispute within LMIM, and although I conclude that Mr Williams and Ms Blank were not told this, I consider that Mr Fischer would have taken the attendees through the escalation rates carefully, in order to ensure an independent opinion. The escalation rates for sales were only a single page of the feasibility which clearly set them out. Mr Williams would have discussed them at the meeting. It is noteworthy that when he and Ms Blank later considered a Maddison Estate feasibility, a note (referred to below) by Ms Blank observed that LMIM had used “a high escalation of sales values due to completion of various facilities” but that the escalated “end sales values (in 7 years’ time) appear comparable to high end estates such as Sanctuary Cove”.
13. Although Mr Williams gave oral evidence that he would not have been able to see the screen during the presentation, I am not satisfied that his recollection of this is accurate. In any event, I do not accept that any impairment of his vision of the screen would have been apparent to any of the respondents. Ms Blank recalled seeing the feasibility model on the screen (ts 503) and if anyone had thought that Mr Williams could not see the screen then I am satisfied that he would have been given the opportunity to sit closer so that he could see it. The presentation was to obtain the opinion of him and Ms Blank. Mr Williams did most of the talking for WPIAS (ts 503).
14. During the meeting there was also discussion of the reduction of the discount rate from 25% to 16% as the project “derisked”. WPIAS agreed with that approach (ts 317).
15. Mr Fischer’s evidence was that Mr Williams said in the meeting that he was comfortable in principle with the feasibility. Although Mr Williams could not recall saying at the end of the presentation that he was comfortable with the feasibility (ts 469), and although others did not recall this, I am satisfied that he did say it. I am also satisfied that he said, as Ms Mulder gave evidence (and as was recorded in her contemporary emails), that the feasibility was “conservative”. As Mr Fischer explained, Mr Williams also recommended that the board obtain an independent valuation in the near future. The minutes of a board meeting held on 13 July 2012 said that “Williams Partners have asked that we eventually receive an external valuation of the project”. Mr Williams may have had personal concerns about the escalation rates used in the feasibility but he did not voice those concerns to anyone from LMIM. They were only mentioned internally within WPIAS (ts 471).
16. After the meeting Mr Fischer called Mr van der Hoven (who had not been at the 17 July 2012 meeting) in London. Mr Fischer told Mr van der Hoven that the meeting was successful. Mr Fischer was very positive about the meeting. As Mr van der Hoven said in his evidence, Mr Fischer told him “that the auditors had approved the approach taken in the feasibility and the accounting issues relating to the pre-paid management fee”.
17. After the 17 July 2012 meeting with WPIAS, on the same day, Ms Mulder sent an email to Mr Drake, Mr van der Hoven, Mr Fischer and others with the subject line, “Meeting with MPF auditors to discuss Maddison went incredibly well”. She said:

I am giving you a quick snapshot now, as Grant [Fischer] is so excited he has charged off to celebrate.

[WPIAS] are totally relaxed with the feasibility approach on Maddison. In fact I quote Reg [Williams], “it is a conservative approach”.

Grant presented extremely well, leading them through the variances from the Dec model to now and our approach going forward.

In relation to the prepaid management fee, they are also relaxed. They would like to see the interest charge remain at 17% pa to refute any investor protestation that those monies could have been utilised in the market for a return had they not come to us…

1. There was an atmosphere of excitement and relief. Ms Phillips responded saying “Great news!” Mr van der Hoven said “Excellent news!! Amazing what can happen in a couple of weeks!!” And Mr Fischer emailed Mr Barnett, copied to others, saying “Fran and I just wanted to send our sincere thanks for your support and presentation today to WPIAS auditors. This was a pivotal meeting for [LMIM] today and your contribution and management overview of Maddison to Reg [Williams] & Andrea [Blank] was invaluable”.
2. On 24 July 2012, Mr Fischer sent an email to members of the PAM team and the board which said that the Maddison feasibility had been approved in concept by the WPIAS auditors. An MPF Credit Committee synopsis dated 25 July 2012 observed:

Feasibility for the entire development has now been reviewed by the auditors [WPIAS] on 17th July, 2012 and they are comfortable with the concept.

1. On 24 July 2012, Mr Fischer sent an email to Ms Blank saying:

Please see attached Maddison Feasibility we presented last week. It is in Estate Master format which I think you have?

If not, please let me know and we can send excel format.

1. On 25 July 2012, Mr Barnett sent an email to Ms Blank, copied to Mr Fischer, saying:

Please find attached the Estate Master DF Model in excel for your records and reference. I will commence sending the supporting information in a more summarised (as per our discussion) over the next few days if that timing is ok for you?

Please call me if you have any queries.

1. In summary, the 17 July 2012 meeting with WPIAS was that an independent firm had the effect that a dispute between the directors concerning the escalation rates to use for the feasibility report had been resolved. Although the resolution was by a very high level review, as I explain later the determination of escalation rates is not a science; it is an exercise involving some uncertainty and some speculation albeit with the benefit of expertise. I reiterate that the escalation rates presented to WPIAS were different from those in the 11 July 2012 feasibility which had been produced to illustrate full recovery, and which showed a net present value of $235 million. The net present value of the 17 July 2012 feasibility was $169 million.

#### The WPIAS audit in 2012

1. During 2012, WPIAS was again engaged to audit the financial statements of the MPF for the financial year ended 30 June 2012. In respect of the 2012 audit, WPIAS sent a letter to the board of LMIM on 1 August 2012 confirming the terms of WPIAS’ engagement. That letter relevantly provided:

1 August 2012

…

The Board of Directors

LM Investment Management Ltd

…

You have requested that we audit the financial report of the **LM Managed Performance Fund** (“the entity”) as of and for the year ended 30 June 2012…

We will conduct our audit in accordance with Australian Auditing Standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial report is free from material misstatement. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor’s judgement, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial report.

Because of the inherent limitations of an audit, together with the inherent limitations of internal control, there is an unavoidable risk that some material misstatements may not be detected, even though the audit is properly planned and performed in accordance with Australian Auditing Standards.

In making our risk assessments, we consider internal control relevant to the entity’s preparation of the financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity’s internal control. However, we will communicate to you in writing concerning any significant deficiencies in internal control relevant to the audit of the financial report that we have identified during the audit.

You should not assume that any matters reported to you, or that a report that there are no matters to be communicated, indicates that there are no additional matters, or matters that you should be aware of in meeting your responsibilities.

…

Our estimate of the professional fee for the audit of the financial report of the entity is **$96,000 (exc GST)**…

1. Mr Williams gave substantial evidence in cross-examination about the 2012 audit (ts 472 onwards). He explained that WPIAS considered the feasibility report carefully. WPIAS undertook four different “what if” scenarios with a major concern for whether the Maddison Estate development had the capacity to permit repayment of the loan. Some of these scenarios involved substantial reductions in the escalation rates. The result showed recovery of between $199 million and $323 million. One scenario involved removing all the embellishments from the development. In summary the options which were based on the Maddison Estate development plan were as follows:
2. Option 1 was capped at 5% escalation. The recoverable balance was $199 million;
3. Option 2 was capped at 7.5% escalation. The recoverable balance was $238 million; and
4. Option 3 capped land and apartment values at $500,000. The recoverable balance was $323 million.
5. Mr Williams also asked a senior analyst at WPIAS to remodel completely the feasibility with the assumption that it had a high degree of inaccuracy. WPIAS concluded that the loan was not impaired (ts 484).
6. On 29 November 2012, Ms Blank produced a memorandum concerning the audit testing that had been conducted concerning the Maddison Estate loan. In the note she observed that the loan was $200 million which included $100 million of capitalised interest. Ms Blank’s emphasis on the amount of capitalised interest might be relevant to a matter to which I return in the conclusion to these reasons concerning the assumptions upon which this case was conducted. Ms Blank observed that in the high level review:

It was noted the Manager has included a high escalation of sales values due to completion of various facilities, both external & internal, over the period (eg swimming pools, wave park, coomera town centre etc). The end sales values (in 7 years’ time) appear comparable to high end estates such as Sanctuary Cove. The Gold Coast property market appears to be at the bottom of the market (2012 considered a base year), and property values are expected to increase over time due to, inter alia, the diminishing supply of vacant land.

1. The review of the feasibility study was described as “limited to a reasonability review to assess recoverability of the loan in the long term”. Mr Williams explained that WPIAS’ “major priority was to ensure that the project had the capability of repaying the loan back to the MPF” (ts 472). He concluded that the loan was recoverable (ts 474).

### The 7 August 2012 MPF Credit Committee meeting and surrounding circumstances

1. On 7 August 2012, the MPF Credit Committee met to consider the proposal to increase the limit of the advance from $180 million to $280 million. The proposal was set out in a synopsis dated 25 July 2012. The minutes of the 7 August 2012 meeting provided that they should be read in conjunction with the synopsis. It is necessary to reiterate five matters of immediate context to the 7 August 2012 MPF Credit Committee meeting.
2. First, by 7 August 2012, there had been substantial developments since around the time of the September 2011 loan variation which increased the loan from $115 million to $180 million. As I have explained, the Maddison Estate development concept had been enhanced and refined. There were a number of exciting embellishments which were endorsed by celebrities and would be run by those celebrities. There was a proposal for a significant increase in density of the buildings. Mr Barnett had been employed with a substantial increase in efficiency. And work had commenced on site.
3. Secondly, the MPF had been audited in 2011 and the loan was not found to be impaired. Many of the inputs for the feasibility presented at the 7 August 2012 meeting were obtained independently of LMIM. The only aspect of the feasibility reports which had initially been the subject of unresolved dispute was the escalation rates. The escalations appeared on a single page in the very lengthy feasibility report. They were not a matter which required substantial deliberation but instead were a matter which involved an evaluative conclusion based upon expertise and a detailed knowledge of the development. A dispute about the escalation rates used in the feasibility had led to a revised feasibility being presented to auditors who had a high degree of familiarity with the development. A positive response was given including a description of the feasibility as “conservative”, although the response was not made in a formal report, nor was it made with the knowledge that it was to be used to resolve a dispute or to make a decision to vary the terms of the loan.
4. Thirdly, very shortly before the 7 August 2012 meeting there had been strongly positive news and radio publicity. An article had been published on the front page of the Gold Coast Bulletin with the heading “Pimpama’s $1b Secret”. The article was a powerful advertisement for the Maddison Estate development. It described the embellishments and the celebrity endorsements including the tennis courts, netball and basketball courts, Jamie Durie landscape design, and world class sporting facilities. There were numerous references to the “billion dollar development”. Another article was published in The Australian newspaper with strong comments of endorsement from Mr Durie who described each precinct of the development as a “masterpiece”. A radio interview was given on the ABC concerning “Billion dollar Gold Coast Residential project fast tracked”.
5. Fourthly, Suncorp was a first secured lender with a debt of around $22 million. If the loan limit was not increased then Suncorp might foreclose and sell the development, placing at risk potentially all of the value of the $191 million balance of the loan.
6. Fifthly, an increase in the loan limit was a matter that was contemplated as necessary at the time of the September 2011 variation which provided funding only until the end of March 2012. More than four months had expired since, as predicted in September 2011, the limit contemplated by the September 2011 variation had been reached. But, as the minutes of the meeting noted, although the proposal to increase the loan had been considered on 29 June 2012 it had been deferred pending a review of the project feasibility, and the sales and marketing plan.
7. The 25 July 2012 synopsis for the meeting, which was prepared by Mr Barnett, repeated and updated much of the information from the 28 June 2012 synopsis. It added that the feasibility for the entire development had been reviewed by WPIAS on 17 July 2012 and that they were comfortable with the concept. The synopsis also noted that the loan increase was to cover the following:
8. the current loan balance of $191,733,047;
9. interest on the Suncorp loan facility until November 2012 of $1,073,784 (the synopsis noted that Suncorp as first mortgagee had a debt of almost $22 million and that Suncorp’s preferred position was to be taken out as soon as possible);
10. interest on the MPF loan facility until 30 June 2013 of $59,430,410;
11. anticipated development costs until 30 June 2013 of $15,414,490; and
12. a loan re-establishment fee of $9,800,000 payable by Maddison Estate.
13. Some aspects of these costs might not have presented much difficulty. As to (1), the extension was simply to cover an amount which was *already* owed. As to (3) and (5), this would not involve any payment by the MPF but if the limit of the loan were not increased then this interest and fee would not otherwise be received. The only actual payments from the MPF were approximately $16.5 million comprised of (2) and (4). Even then, if (2) had not been paid then upon sale of Maddison Estate it would have been recovered by Suncorp, holding the first security, before any funds could be paid to the MPF.
14. Those attending the 7 August 2012 meeting were Mr Fischer (as chair), Mr van der Hoven, Ms Mulder, Mr Petrik (a portfolio manager) and Mr Parker (a commercial lending manager in the PAM team). Mr Drake was described in the minutes as attending “by invitation”.
15. The reason why Mr Drake was not described as a member of the MPF Credit Committee on 7 August 2012 originates from legal advice provided to LMIM about the proper approach to the conflict between Mr Drake’s interest in Maddison Estate and his position as a director of LMIM and member of the MPF Credit Committee.
16. Ms Chalmers, who was a very efficient administrator and compliance manager, had developed an approach to be taken to conflict issues at MPF Credit Committee meetings. Although she had developed this policy with Mr Tickner, they had not always applied it strictly. An issue arose after the MPF Credit Committee meeting on 29 June 2012. After that meeting, Mr Tickner queried with Ms Chalmers whether Mr Drake could chair or vote at a meeting concerning the Maddison Estate loan. Ms Chalmers replied on 3 July 2012, explaining that she had read the legal advice and that she agreed that Mr Drake should not vote on any issue pertaining to the loan agreement.
17. It was in this context that, when Ms Chalmers assisted to assemble the MPF Credit Committee for the 7 August 2012 meeting, she took steps to ensure that Mr Drake was not described as a member of the committee, and that he was described as being present by invitation (ts 178).
18. Although Mr Drake was only present “by invitation”, I accept Ms Chalmers’ evidence that Mr Drake nevertheless voted at the meeting. Ms Chalmers was an honest witness and I am satisfied that this matter was of sufficient importance to her that her recollection of the meeting was likely to be accurate. When Ms Chalmers wrote the minutes of the meeting she did not say that Mr Drake had not voted. Instead, she wrote that “PD vote not counted for [MPF Credit Committee] purposes”. Mr Drake, who was far more senior to Ms Chalmers, would have spoken and voted at the meeting and it is unlikely that Ms Chalmers would have taken any steps to prevent this. However, acting properly after the meeting, she did not record his vote when subsequently recording the vote in the minutes.

### The deed of variation executed after August 2012

1. Although dated 1 July 2012, I conclude (for reasons explained above) that the deed of variation of the loan was executed some time after August 2012.
2. The opening paragraph of the deed reads “THIS DEED is made on 1st July 2012”. The words “1st July” are handwritten.
3. The deed was between The Trust Company as lender, Maddison Estate as borrower, and Coomera Ridge as mortgagor. The deed recites that: (i) LMIM as trustee for the MPF lent monies to Maddison Estate on the terms of the Maddison Estate MPF Loan Agreement; (ii) following settlement of the loan, The Trust Company was appointed as custodian of the MPF, and LMIM assigned the legal interest in the Maddison Estate MPF Loan Agreement and the security to The Trust Company; (iii) Maddison Estate acknowledges and consents to the assignment; (iv) Maddison Estate and Coomera Ridge has requested The Trust Company to consent to an amendment to the Maddison Estate MPF Loan Agreement; and (v) The Trust Company has agreed to the requested amendment on the terms of the deed.
4. The deed of variation records the increase in the Maddison Estate loan to $280 million (cl 3(a)), and the re-establishment fee of $9.8 million (cl 6).
5. By cl 3(b), the date for repayment was amended to 30 June 2013 with effect from 30 June 2012. The date for repayment had not previously been amended.
6. The variations took effect retrospectively on 30 June 2012.

# The alleged breach of trust by LMIM

## ASIC’s pleading

1. As I explained in the introduction to these reasons, ASIC’s case for contravention of s 180(1) of the *Corporations Act* against each respondent was premised upon the assumption that it needed to prove a breach of trust by LMIM as trustee. ASIC relied upon equitable and statutory obligations creating duties of care owed by trustees.
2. It is important to emphasise at the outset that these equitable and statutory duties of care alleged by ASIC involved breaches of duty in the performance of an *authorised* act. Different questions arise when liability for an unauthorised act is concerned: see *Youyang Pty Ltd v Minter Ellison Morris Fletcher* [2003] HCA 15; (2003) 212 CLR 484. Nor is this case concerned with any breach of *fiduciary* duty where, again, different considerations may arise.
3. The precise nature of the alleged breach of trust duty that ASIC accepted that it needed to prove was unclear from ASIC’s pleading. There were two possibilities.
4. The first possibility is that ASIC had pleaded, and accepted the onus of proving, a completely constituted cause of action for breach of trust. In other words, ASIC had to prove an *actionable* breach of trust. This was the assumption that I made when reading ASIC’s pleading. After setting out the circumstances of the August 2012 Variation, ASIC pleaded that LMIM “committed a breach of trust against MPF by approving the August 2012 Variation” ([155]). ASIC’s plea of breach of s 180 by the respondents then included, in [161], the claim that they exposed LMIM “to a foreseeable risk of harm, namely civil proceedings by the unitholders in the MPF” because the approval of the August 2012 Variation “caused LMIM to commit a breach of trust against MPF”. It is difficult to see how ASIC’s plea of breach of trust could mean anything other than an *actionable* breach of trust. In other words, how could a *non-actionable* breach of trust ever lead to civil proceedings by unitholders? Why would any unitholder ever attempt to bring proceedings for a breach of trust which was not actionable?
5. The second possibility is that ASIC’s pleading described a breach of a trustee’s duty, irrespective of whether it involved an actionable breach of trust. In written closing submissions, after all evidence had concluded, ASIC submitted that it was “not required to prove that an *actionable* breach of trust was committed. In other words, ASIC has not assumed the burden of proving actual loss”. Rather, ASIC said that it “has assumed the burden of proving the existence of a foreseeable *risk* that ‘civil proceedings by unitholders in the MPF’ might be brought.” ASIC said that its case on breach of trust was “simply this” ([274]):

A prudent trustee in those circumstances would not have approved the advance. The approval of that advance breached the duty prescribed by s 22 of the *Trusts Act* and exposed the MPF to a foreseeable risk of capital loss, being the risk of default by the borrower if the estimated cash flows generated by the development did not eventuate.

1. In other words, ASIC accepted that it must prove, as it had pleaded, that a breach of trust was committed by LMIM. However, it submitted that it need not prove an *actionable* breach of trust. It was sufficient, ASIC contended, to prove that a breach of trust arose which gave rise to a foreseeable risk of loss even if that breach of trust was not a cause of action.
2. ASIC therefore submitted that its pleading should be construed as alleging that there was a risk of civil proceedings for breach of trust *irrespective* of whether the breach of trust was actionable, and irrespective of whether it caused loss or not. I do not accept this submission. On any reasonable construction of ASIC’s pleading, the allegation of breach of trust would be understood as an allegation of a constituted cause of action for breach of trust, or an actionable breach of trust, which could be brought by a unitholder. With respect to the otherwise detailed and careful submissions by senior counsel for ASIC, I do not accept that ASIC’s pleading could reasonably have been understood as meaning that its case was dependent upon proving that there was a foreseeable risk of civil proceedings arising from a *non-actionable* breach of trust. ASIC’s case was (reasonably) not understood in this way by any of the respondents.
3. Even if ASIC’s pleading could be construed as an allegation that LMIM committed a breach of trust which *might* give rise to a cause of action, the discussion in this section of the reasons concerning the obstacles to a constituted cause of action by unitholders remains pertinent to my conclusions. This is because any action by unitholders (all of whom were sophisticated or wholesale investors) would be brought after legal advice. The legal advice would consider whether the unitholders had reasonable prospects of proving a constituted cause of action. In other words, the foreseeability, and the likelihood, of any action by unitholders would still require ASIC to prove that there was a reasonable prospect of the unitholders being able to establish an actionable breach of trust.

## The two issues and the answers in broad outline

1. Broadly, there are two obstacles to ASIC’s allegations of breach of trust.
2. The first obstacle is that the duty which LMIM had allegedly breached had been excluded, whether that duty arose in equity or under statute. The MPF Constitution, on its proper construction, excluded the trustee’s duty of care.
3. For more than 150 years, since *Wilkins v Hogg* (1861) 31 LJ Ch 41, equity has recognised that an appropriately drafted exclusion clause can exclude a trustee’s duty of care. ASIC submitted that the law in Queensland changed in 1999 with the introduction of a statutory duty of care in the Queensland *Trusts Act* , modelled closely on the equitable duty. ASIC submitted that the *Trusts Act* had this effect only in Queensland, unlike all the other States which were a model for Queensland’s legislation, and contrary to the plain structure of the *Trusts Act*. I do not accept that submission.
4. The second obstacle to ASIC’s allegations of breach of trust is that the breach of trust was not actionable. ASIC properly conceded that causation of loss is an essential constituent of an action for breach of a trustee’s duty of care. The second obstacle is that even if ASIC had proved a breach of duty by LMIM as trustee, ASIC did not prove that any loss was *caused* by any breach of duty. It was not proved that even if a breach of duty occurred, the loss would not have been suffered in any event.
5. These two obstacles are addressed in the following sections:
6. Legal principles concerning a trustee’s equitable duty of care.
7. Exclusion of the equitable duty and liability in the MPF Constitution.
8. Proof of loss is required to establish breach of a trustee’s equitable duty of prudence.
9. Was the equitable duty breached?
10. Section 22 of the *Trusts Act* was excluded.
11. Was the duty in s 22(1) of the *Trusts Act* breached?

## Legal principles concerning a trustee’s equitable duty of care

### The trustee’s equitable duty of care (the “prudent person” test)

1. ASIC submitted that the trustee’s equitable duty of care was encapsulated by Finn J in *Australian Securities Commission v AS Nominees Limited* (1995) 62 FCR 504, 516-518. I will return to that decision below. My discussion of the test for the duty of care commences, as Finn J did, with the observation that it is old and accepted law that in “managing a trust business the trustee should exercise the same care as an ordinary, prudent business person would exercise in conducting that business as if it were his or her own”.
2. The “prudent person” test is commonly attributed to the decisions in *Speight v Gaunt* (1883) 22 Ch D 727 (Bacon VC and, reaching a different conclusion, the Court of Appeal) and *Speight v Gaunt* (1883) 9 App Cas 1 (House of Lords). But this was not the first application of this standard in the context of acts by trustees. There were numerous earlier applications, including a decision a decade earlier also by Bacon VC in *Oriental Commercial Bank v Savin* (1873) LR 16 Eq 203, 206. The earliest application of the test in the context of trustees may have been on the other side of the Atlantic, by Putnam J in *Harvard College v Amory*,26 Mass (9 Pick) 446, 461 (1830), an approach which was subsequently adopted in legislation or decisions in most United States jurisdictions.
3. The statement of the test was, and is, intended to be flexible. As Heydon and Leeming observe, the standard “changes with economic conditions and contemporary thinking”: Heydon JD and Leeming MJ, *Jacobs’ Law of Trusts in Australia* (8th ed, LexisNexis Butterworths Australia, 2016) 356 [17-18].
4. However, there are two difficulties that can arise with the *application* of the prudent person test.
5. The first difficulty is that this flexible test was often applied in an inflexible manner or by adding glosses such as a need for caution. Many of the early decisions that considered the test in England, Australia, and the United States placed great importance upon the need for caution in trust investment. For instance, in *Learoyd v Whiteley* (1887) 12 App Cas 727, 733, Lord Watson said:

Business men of ordinary prudence may, and frequently do, select investments which are more or less of a speculative character; but it is the duty of a trustee to confine himself to the class of investments which are permitted by the trust, and likewise to avoid all investments of that class which are attended with hazard.

See also *Re Whiteley* (1886) 33 Ch D 347, 356-357 (Lindley LJ).

1. This approach was appropriate in an era where the trust was almost invariably used as a concept for preservation of the capital of the settlor, rather than as an investment vehicle. But this requirement for caution is very difficult to apply as a single, undifferentiated test in the context of the use of trusts in an almost infinite variety of businesses and business purposes. As the reporter of the third Restatement of the Law of Trusts, Professor Halbach, observed in The American Law Institute, *Restatement of the Law Third, Trusts* *Vol 3* (American Law Institute, 2007) 288:

Unfortunately, much of the apparent and initially intended generality and adaptability of the prudent-man rule was lost as it was further elaborated in the courts and applied case by case. Decisions dealing with essentially factual issues were accompanied by generalizations understandably intended to offer guidance to other courts and trustees in like situations. These cases were subsequently treated as precedents establishing general rules governing trust investments. Specific case results and flexible principles often thereby became crystallized into specific subrules prescribing the types and characteristics of permissible investments for trustees.

Based on some degree of risk that was abstractly perceived as excessive, broad categories of investments and techniques often came to be classified as “speculative” and thus as imprudent per se. Accordingly, the exercise of care, skill, and caution would be no defense if the property acquired or retained by a trustee, or the strategy pursued for a trust, was characterized as impermissible.

1. The rule in § 90 of the third Restatement of the Law of Trusts now provides for a general standard of prudent investment, but emphasises that the duty is one of a prudent investor “in light of the purposes, terms, distribution requirements, and other circumstances of the trust”. Subparagraph (a) also provides that the standard “requires the exercise of reasonable care, skill, and caution, and is to be applied to investments not in isolation but in the context of the trust portfolio and as a part of an overall investment strategy, which should incorporate risk and return objectives reasonably suitable to the trust”. This rule is in similar terms to the obligation in s 24(1)(a) of the *Trusts Act* which permits a trustee, when exercising a power of investment, to take into account “the purposes of the trust and the needs and circumstances of the beneficiaries”.
2. One rationale for the emphasis upon the purposes of the trust was described in the Restatement as follows (351):

some trust situations and beneficiary objectives justify more venturesome fiduciary investment policies. Even in these cases of less conservative investment strategy, however, prudent management of others’ properties still calls for sound and careful fiduciary behaviour (including “risk management”) in carrying out programs that deliberately involve the taking of higher risk in quest of greater return.

1. The short point is that the refrain in the older cases about caution and avoidance of hazard, if read in isolation, suggests a duty which is abstracted from the terms of the trust instrument and the nature of the trust business. But whether an investment is incautious due to its speculative nature, or impermissibly hazardous, may be affected by the terms of the trust instrument. To give a simple example, a trust established for the purposes of speculation, with terms requiring investment in speculative ventures, requires a different assessment of hazard from a trust which requires investment in government bonds. As Gummow J said in *Breen v Williams* [1996] HCA 57; (1996) 186 CLR 71, 137, describing the obligations of a trustee under a trust instrument to manage a trust business: “the trustee is required *both to observe the terms of the trust* and, in doing so, to exercise the same care as an ordinary, prudent person of business would exercise *in the conduct of that business* were it his or her own” (emphasis added).
2. A second difficulty with a single prudent person standard of care is that it does not differentiate between the degrees of skill required by different types of trustee. As ASIC submitted, a more precise approach is that of Finn J in *Australian Securities Commission v AS Nominees Limited* (517-518):

The standard of trustee care and caution of which I have been speaking so far does not differentiate between types of trustee. It is of general application. That standard, moreover, was settled a century ago and during a period when trust corporations were not used for the trading and investment purposes that are the commonplace in this country today. There is, in my view, a substantial question now to be answered as to whether a higher standard is not to be exacted from at least corporate or professional trustees (a) which hold themselves out as having a special or particular knowledge, skill and experience, and (b) which, directly or indirectly, invite reliance upon themselves by members of the public in virtue of the knowledge, etc, they appear so to have.

In *Bartlett v Barclays Trust Co Ltd (No 1)* [1980] Ch 515 at 534 Brightman J was prepared to impose such a higher duty of care on a trust corporation:

“a professional corporate trustee is liable for breach of trust if loss is caused to the trust fund because it neglects to exercise the special care and skill which it professes to have.”

This decision has been cited with apparent approval, though it was not in terms relied upon, by Gleeson CJ in *Gill v Eagle Star Nominees Ltd* (unreported, Supreme Court, NSW, Gleeson CJ, 22 September 1993). It is, in its own way, consistent with observations of the Privy Council in the Australian appeal *National Trustees Co of Australasia Ltd v General Finance Co of Australasia Ltd* [1905] AC 373 at 381, when refusing to excuse a trust company from a breach of trust. There is extensive United States case-law affirming such a higher standard. It is conveniently explained and exemplified in *Scott on Trusts*, par 174.1; see also *Fales v Canada Permanent Trust Co* [1977] 2 SCR 302 where the question is recognised but not answered by the Supreme Court of Canada; and see G G Bogert, *Law of Trusts and Trustees* (2nd revd ed, 1977), par 541.

If it were in fact necessary for me so to do (which it is not), I would be prepared to apply to the trustee companies in these proceedings a standard of care higher than that of the ordinary prudent businessperson.

1. With respect, I agree with these observations.
2. The ultimate foundation of the trustee’s duty of care in equity is the trustee’s objective assumption or undertaking of responsibility in the trust deed or acceptance of trust duties arising from a declaration of trust. The question is one of construction of all of the circumstances, including the general implication, arising from centuries of custom, that trustees are expected to take care. The foundational concept of assumption of responsibility has a long lineage in the law as the basis for imposition of liability: *Swick Nominees Pty Ltd v LeRoi International Inc (No 2)* [2015] WASCA 35; (2015) 48 WAR 376, 443-447 [368]-[381]. The recognition of liability on the basis of an assumption of responsibility is not unique to trustees. As long ago as 1964, Lord Devlin said in *Hedley Byrne & Co. Ltd v Heller & Partners Ltd* [1964] AC 465, 528-529 that there was “ample authority” to justify the statement that “the categories of special relationships which may give rise to a duty to take care in word as well as in deed are not limited to contractual relationships or to relationships of fiduciary duty, but include also relationships… where there is an assumption of responsibility”. And in *Henderson v Merrett Syndicates Ltd and Ors* [1995] 2 AC 145, 205, Lord Browne-Wilkinson said:

The liability of a fiduciary for the negligent transaction of his duties is not a separate head of liability but the paradigm of the general duty to act with care imposed by law on those who take it upon themselves to act for or advise others. Although the historical development of the rules of law and equity have, in the past, caused different labels to be stuck on different manifestations of the duty, in truth *the duty of care imposed on bailees, carriers, trustees, directors, agents and others is the same duty: it arises from the circumstances in which the defendants were acting, not from their status or description. It is the fact that they have all assumed responsibility for the property or affairs of others which renders them liable for the careless performance of what they have undertaken to do, not the description of the trade or position which they hold.*

(Emphasis added.)

1. Similarly, in *Permanent Building Society (in liq) v Wheeler* (1994) 11 WAR 187, 247, Ipp J (Malcolm CJ and Seaman J agreeing) explained that “the tortious duty not to be negligent, and the equitable obligation on the part of a trustee to exercise reasonable care and skill are, in content, the same”.
2. For this reason, any holding out by a trustee of a special or particular knowledge, skill and experience reflects an assumption of that special degree of responsibility. Again, the question is an objective one which is based upon the circumstances of the trust deed or declaration of trust and the acceptance of the obligation by the trustee.

### The difference between excluding a duty and excluding liability

1. There is a distinction that must be made between a clause excluding a duty and a clause excluding liability for breach of a duty. This distinction was recognised by Donaldson J in *Kenyon, Sons & Craven Ltd v Baxter Hoare & Co. Ltd* [1971] 1 WLR 519, 522-523. In that case, Donaldson J explained three different types of “protective conditions”, or exemption clauses, as follows:

Protective conditions are of three distinct types, namely, first, those which limit or reduce what would otherwise be the defendants’ duty; second, those which exclude the defendants’ liability for breach of specified aspects of that duty and third, those which limit the extent to which the defendant is bound to indemnify the plaintiff in respect of the consequences of breaches of that duty.

A condition which provided that a warehouseman should be under no obligation to take greater care of perishable goods than was appropriate to imperishable goods, would constitute a good example of the first category of protective conditions. Another example, in a different field, is provided by the well known clauses which exclude the conditions implied by the Sale of Goods Act 1893. If, in such a case, the warehouseman takes such care of perishable goods as would be appropriate had they been imperishable and damage results, he will escape liability not because the clause exempts him from liability for breach of contract (whether fundamental or otherwise), but because there has been no breach of contract.

1. Donaldson J’s explanation of the three categories of protective conditions was approved in *Trade and Transport Incorporated v Iino Kaiun Kaisha Ltd* [1973] 1 WLR 210, 230 (Kerr J) and *Gardiner v Agricultural and Rural Finance Pty Ltd* [2007] NSWCA 235 [214] (Basten JA); see also Dawson F, “Fundamental Breach of Contract” (1975) 91 LQR 380.
2. The distinction between clauses which exempt a duty and those which exempt liability is a distinction between clauses concerned with primary duties and those concerned with secondary duties. As Lord Diplock famously explained in *Photo Production Ltd v Securicor Transport Ltd* [1980] AC 827, 848-850:

…breaches of primary obligations give rise to substituted or secondary obligations on the part of the party in default, and, in some cases, may entitle the other party to be relieved from further performance of his own primary obligations. These secondary obligations of the contract breaker and any concomitant relief of the other party from his own primary obligations also arise by implication of law…

…an exclusion clause is one which excludes or modifies an obligation, whether primary, general secondary or anticipatory secondary, that would otherwise arise under the contract by implication of law.

1. Lord Diplock’s characterisation of primary and secondary obligations has been cited or adopted in *Pacific Brands Sport & Leisure Pty Ltd v Underworks Pty Ltd* [2005] FCA 288, [9] (Finkelstein J); *Tszyu v Fightvision Pty Ltd* [2001] NSWCA 103; (2001) 104 IR 225, 238 [59] (Powell JA); and *Kennedy Taylor (Vic) Pty Ltd v Baulderstone Hornibrook Pty Ltd* [2000] VSC 43 [24] (Beach J).

### Can the equitable duty be excluded?

1. The leading English case concerning exclusion of liability for the equitable duty of care is *Armitage v Nurse* [1998] Ch 241. The decision in *Armitage* was approved by the Privy Council, as representing English law, in *Spread Trustee Co Ltd v Hutcheson* [2012] 2 AC 194.
2. In *Armitage*, the question was whether a trustee exemption clause could validly exclude trustees from liability for gross negligence. A beneficiary had alleged that trustees had acted in breach of their duties in the management of trust property. One of the preliminary issues tried was whether cl 15 of the settlement absolved the trustees from liability. That clause provided that no trustee was liable for any loss or damage from any cause whatsoever “unless such loss or damage shall be caused by his own actual fraud”. The substantive reasons were delivered by Millett LJ (with whom Hutchison and Hirst LJJ agreed). Lord Justice Millett held that “actual fraud” meant what it says. It did not mean “constructive fraud” or “equitable fraud”. It excluded liability for breach of trust in the absence of a dishonest intention of the trustee (250). His Lordship then explained that a clause which excluded liability for gross negligence would not be invalid. He described the challenge by Lord Westbury LC to counsel in *Wilkins v Hogg*, 42, to cite a case where a court had found repugnant an indemnity clause protecting a trustee from his ordinary duty. No such case had been found, and none had been decided since (253). Lord Justice Millett concluded that the “duty of the trustees to perform the trusts honestly and in good faith for the benefit of the beneficiaries is the minimum necessary to give substance to the trusts” (253-254). A petition for leave to appeal to the House of Lords was dismissed (264).
3. ASIC conceded that the decision in *Armitage* was correct. ASIC’s concession on this point should be accepted as a matter of both authority and principle.
4. As a matter of authority, the decision in *Armitage* on this point has been followed or applied in Australia in cases for nearly two decades. See, for instance, *Rankine v Rankine* (unreported, Sup Ct, QLD, de Jersey CJ, 3 April 1998); *Green v Wildern Pty Ltd* [2005] WASC 83 [493] (Hasluck J); *Leerac Pty Ltd v Fay* [2008] NSWSC 1082 [23] (Brereton J); *Motor Vehicles Insurance Ltd v Woodlawn Capital Pty Ltd* [2014] NSWSC 1503; (2014) 290 FLR 285, 330 [323] (Stevenson J); *Segelov v Ernst & Young Services Pty Ltd* [2015] NSWCA 156; (2015) 89 NSWLR 431, 458-459 [145]-[146] (Gleeson JA; Meagher and Leeming JJA agreeing); and *Crossman v Sheahan* [2016] NSWCA 200 [307] (Ward JA, Payne JA agreeing).
5. As a matter of principle also, the decision must be correct. Unlike the duty not to engage in deceit or fraud, which are duties *imposed* by law, the foundation of a trustee’s equitable duty of care is the responsibility assumed by the trustee, manifest in any written trust deed or declaration of trust. Hence, as I have explained, a trustee who professes to have special care and skill will be held to that higher standard. In contrast, a trustee who disclaims a duty of care will not have assumed *that* duty (I say nothing of other duties including fiduciary duties and duties only to engage in authorised transactions). This is why, in *Hedley Byrne v Heller*, Lord Devlin said (533):

A man cannot be said voluntarily to be undertaking a responsibility if at the very moment when he is said to be accepting it he declares that in fact he is not. The problem of reconciling words of exemption with the existence of a duty arises only when a party is claiming exemption from a responsibility which he has already undertaken or which he is contracting to undertake.

## Exclusion of the equitable duty and liability in the MPF Constitution

### The exclusion of LMIM’s equitable duty of care

1. The MPF Constitution is expressed as a deed between LMIM and “the members as they are constituted from time to time of [the MPF]”. The document which was tendered was dated in typescript December 2001, with no day inserted in the blank space.
2. Clause 12.8 of the MPF Constitution provides as follows:

12.8 To the extent allowed by law:

(a) any restriction or prohibition imposed upon the Manager in relation to the investment from time to time of the Scheme Fund or any part thereof is hereby excluded from the obligations imposed.

(b) without derogating from the generality of the foregoing this exclusion specifically applies to any “Prudent Person Rule” or the like which may be implied by any future enactment of legislation.

1. ASIC submitted that cl 12.8 does not exclude the “prudent person” duty in equity because that duty was not a “restriction or prohibition imposed upon [LMIM] in relation to the investment”. Instead, ASIC submitted, the clause operates as a *prescription* requiring any such investment to be exercised with the standard of care described.
2. In some contexts it might be possible to construe a duty of care as not imposing a “restriction” in relation to investment, although it is difficult to see how a prescription which restricts the conduct of a trustee is not a “restriction”. However, in this case, as a matter of construction cl 12.8(b) plainly contemplates that a duty of care (including a “prudent person rule”) falls within the concept of a restriction “without derogating from the generality” of cl 12.8(a). Clause 12.8(a) purports to exclude the “prudent person” duty in equity and, to the extent possible, under the *Trusts Act.*

### The exclusion of LMIM’s liability for breach

1. Clause 18.1(a) of the MPF Constitution provides:

INDEMNITY AND LIABILITY

18.1 The following clauses apply to the extent permitted by law:

(a) The Manager is not liable for any loss or damage to any person (including any Member) arising out of any matter unless, in respect of that matter, it acted both:

(i) otherwise than in accordance with this Constitution and its duties; and

(ii) without a belief held in good faith that it was acting in accordance with this Constitution or its duties.

In any case the liability of the Manager in relation to the Scheme is limited to the Scheme Property, from which the Manager is entitled to be, and is in fact, indemnified.

1. During the trial, none of the respondents pleaded reliance upon cl 18.1(a). However, the respondents had relied upon a privilege against exposure to a penalty, and Mr Drake did not give or call evidence. When this issue was raised, ASIC did not object to an amendment to the pleading by the respondents to rely upon this clause.
2. As I have explained above, an exclusion of liability for breach, like a limitation of liability for breach, is concerned with the remedial consequences of a breach of duty. It does not negate the cause of action. It does not deny ASIC’s plea that LMIM had breached its duties as trustee, although it might have the effect that there are no legal consequences of that breach. As I explain later in these reasons, the potential lack of any legal consequences is a very material matter when assessing the foreseeability and likelihood of an action by unitholders.
3. ASIC submitted that it was not possible for a clause to exclude *liability* for the same reasons that it was not possible for a clause to exclude a *duty.* I have rejected that argument in relation to duty. But there is a further obstacle in relation to liability. Senior counsel for ASIC accepted in oral submissions that a logical corollary to ASIC’s submission was that liability could not even be limited (ts 722). Therefore, on ASIC’s submission, it would not have been possible for the MPF Constitution to contain a clause limiting the liability of LMIM for breach of its duty of care to, say, $10 million. ASIC was unable to point to any authority supporting such a restriction. I am not aware of any. Nor is there any textual basis for such a restriction in the *Trusts Act.*
4. Clause 18.1 establishes two preconditions for LMIM’s liability although *in any case* the liability of LMIM will be limited to the “Scheme Property”. Scheme Property is defined in the MPF Constitution as the assets of the Scheme, and various different types of asset are specified.
5. As for the two preconditions to exclusion of LMIM’s liability, ASIC submitted that these were matters that LMIM would be required to prove. ASIC relied upon the decision in *Currie v Dempsey* (1967) 69 SR (NSW) 116, 125 where Walsh JA said:

[T]he burden of proof [in the sense of establishing a case], lies on a plaintiff, if the fact alleged (whether affirmative or negative in form) is an essential element in his cause of action, e.g., if its existence is a condition precedent to his right to maintain the action. The onus is on the defendant, if the allegation is not a denial of an essential ingredient in the cause of action, but is one which, if established, will constitute a good defence, that is, an “avoidance” of the claim which, prima facie, the plaintiff has.

1. In *Gardiner v Agricultural and Rural Finance Pty Ltd*, in a passage which was not doubted on appeal to the High Court (see *Agricultural and Rural Finance Pty Ltd v Gardiner* [2008] HCA 57; (2008) 238 CLR 570), Basten JA said ([214]):

It is convenient to return to the question of onus of proof, in order to determine whether, if the matter were evenly balanced, the Appellant would fail because he bore the relevant onus. It is well established that, if cl 7 provided a true exception or exemption from liability, the Appellant would bear the onus of establishing that he fell within the exception: see *Glebe Island Terminals Pty Ltd v Continental Seagram Pty Ltd* (1993) 40 NSWLR 206 at 226–228 (Sheller JA, Handley and Cripps JJA relevantly agreeing, and applying *The Glendarroch* [1894] P 226 at 231 (Lord Esher MR)). The question, however, is whether cl 7 is to be identified as an exception, or as a provision defining the scope of the obligation under the contract. The distinction is well-established, and was helpfully expressed by Donaldson J in *Kenyon, Son & Craven Ltd v Baxter Hoare & Co Ltd* [1971] 1 WLR 519 at 522. After noting that the obligation of a bailee may be expressed either as a duty to redeliver the goods “in the like good order and condition as when received, subject only to such loss or damage as might arise despite the exercise of all reasonable skill and care in their preservation and custody,” or as a duty “to exercise all reasonable skill and care in the preservation and custody” of the goods, he preferred the former, because it better reflected the burden of proof.

1. As an exclusion or exception, the onus would be on LMIM to establish that it did not act otherwise than in accordance with the MPF Constitution and its duties, and that it did not act without a belief held in good faith that it was acting in accordance with the MPF Constitution and its duties. These issues were not the subject of substantial submissions. For example, there were few submissions made about the meaning of good faith or whether a breach of “its duties” would include a breach of the otherwise excluded duty of prudence (which the MPF Constitution in cl 12.8 excludes). However, the short point to which I will return later in these reasons is that LMIM had, at the very least, a reasonable argument that its liability for breach of its duty of prudence had been excluded by cl 18.1.
2. Even if the preconditions to exclusion of LMIM’s liability were not met, cl 18.1 limits the liability of LMIM *in any case* to the Scheme Property and gives LMIM an indemnity for that liability against the Scheme Property.
3. In relation to the August 2012 Variation, the variation was approved for the proceeds to be used for a number of purposes. Apart from the increased current loan balance of around $191 million (which exceeded the previous limit by $10 million) the other purposes were:
4. interest on the Suncorp loan facility until November 2012: $1,073,784
5. interest on the MPF loan facility until 30 June 2013: $59,430,410
6. anticipated development costs until 30 June 2013: $15,414,490
7. loan re-establishment fee (3.5%): $9,800,000
8. As I need to reiterate, neither (2) nor (4) was a *loss* that the MPF could suffer from the August 2012 Variation. The interest on the MPF loan facility was a loan to Maddison Estate to pay money to LMIM. If the loan had not been advanced then the interest would not have been paid. The same is true of the re-establishment fee: if the loan had not been advanced then the re-establishment fee would not have been paid.
9. The total possible loss to Scheme Property was therefore approximately $16.5 million. And this amount, if lost, would *in any event* be recoverable by LMIM from Scheme Property.

## Proof of loss is required to establish breach of a trustee’s equitable duty of prudence

1. ASIC initially submitted that a breach of a duty of care by a trustee was different from other duties of care. ASIC submitted that unlike duties of care owed by others, the duty owed by a trustee was actionable in the absence of damage. Ultimately, however, ASIC abandoned this submission and conceded that proof of loss was necessary to prove an actionable breach of trust in this case. For the reasons below, that concession should be accepted.

### The analogy with common law negligence

1. It is well established that an action for negligence at common law is not complete unless loss is suffered. In *Lochgelly Iron & Coal Co v McMullan* [1934] AC 1, 25, Lord Wright said:

In strict legal analysis, negligence means more than heedless or careless conduct, whether in omission or commission: it properly connotes the complex concept of duty, breach, and damage thereby suffered by the person to whom the duty was owing…

1. The same point was made in the majority joint judgment in *The Commonwealth of Australia v Cornwell* [2007] HCA 16; (2007) 229 CLR 519, 523 [5] (Gleeson CJ, Gummow, Kirby, Hayne, Heydon and Crennan JJ) where their Honours said that “to show the existence of a completely constituted cause of action in negligence, a plaintiff must be able to show duty, breach, and damage caused by the breach…” In *Brookfield Multiplex Ltd v Owners Corporation Strata Plan 61288* [2014] HCA 36; (2014) 254 CLR 185, 227 [124], Crennan, Bell and Keane JJ said that a “duty of care is a thing written on the wind unless damage is caused by the breach of that duty” (quoting *John Pfeiffer Pty Ltd v Canny* [1981] HCA 52; (1981) 148 CLR 218, 241 (Brennan J)).
2. As I have explained above, the foundation for the duty of care by a trustee is the same as the foundation of a common law duty of care, although in either case the content will depend upon the nature of the responsibility assumed. The foundational equivalence of equitable and common law duties is a strong reason why that the trustee’s equitable duty is also only actionable upon proof of loss. The same conclusion is supported by historical considerations. As I explained in *Agricultural Land Management Ltd v Jackson (No 2)* [2014] WASC 102; (2014) 48 WAR 1, 65 [339], 66-67 [347]-[349]*,* a breach of the trustee’s duty of care was enforced through the taking of an account on the basis of wilful default. On the taking of the account the plaintiff could “surcharge” the account with the amount that the trust should have contained but for the breach. But without a surcharge there was no liability for the trustee.

### The position in England

1. The leading modern authority in England is the decision in *Nestle v National Westminster Bank Plc* [1993] 1 WLR 1260. In that case, a bank trustee misunderstood the meaning of a clause of a testator’s will which created a trust fund for investment. The Court of Appeal held that the bank failed in its duty to review the investments regularly and failed in its duty to acquaint itself with the scope of its powers as trustee. The beneficiary of the trust sued the bank, alleging that if proper investment policies had been followed then the funds would have been worth many times their value. The beneficiary sought an inquiry as to the value that the trust funds would have had if they had been invested and managed with proper care and skill, and sought payment of the difference between that amount and the value of the actual trust funds. The Court of Appeal held that the beneficiary’s claim failed because the beneficiary failed to show that she had suffered any loss as a result of the bank’s breaches of duty. None of the breaches was actionable. Dillon LJ (at 1270) relied upon the decision of Sir Robert Megarry VC in *Cowan v Scargill* [1985] Ch 270, 294:

If trustees make a decision upon wholly wrong grounds, and yet it subsequently appears, from matters which they did not express or refer to, that there are in fact good and sufficient reasons for supporting their decision, then I do not think that they would incur any liability for having decided the matter upon erroneous grounds; for the decision itself was right.

1. Leggatt LJ said (at 1283-1284):

The essence of the bank’s duty was to take such steps as a prudent businessman would have taken to maintain and increase the value of the trust fund. Unless it failed to do so, it was not in breach of trust**.** *A breach of duty will not be actionable, and therefore will be immaterial, if it does not cause loss.* In this context I would endorse the concession of Mr. Nugee for the bank that “loss” will be incurred by a trust fund when it makes a gain less than would have been made by a prudent businessman. A claimant will therefore fail who cannot prove a loss in this sense caused by breach of duty. So here in order to make a case for an inquiry, the plaintiff must show that loss was caused by breach of duty on the part of the bank… Loss cannot be presumed, if none would necessarily have resulted. Until it was proved that there was a loss, no attempt could be made to assess the amount of it … Unless there was a loss, there was no cause of action. It was for the plaintiff to prove on balance of probabilities that there was, or must have been, a loss. If proved, the court would then have had to assess the amount of it…

(Emphasis added.)

1. In *Target Holdings Ltd v Redferns (A Firm)* [1996] AC 421, 434, Lord Browne-Wilkinson (the other Law Lords agreeing) cited *Nestle* with approval saying that “there does have to be some causal connection between the breach of trust and the loss to the trust estate for which compensation is recoverable, viz. the fact that the loss would not have occurred but for the breach”. See also *Re Miller’s Deed Trusts* (1978) 75 LSG 454.

### The position in Australia

1. In *Fouche v Superannuation Fund Board* [1952] HCA 1; (1952) 88 CLR 609, the High Court considered whether members of a statutory superannuation board had breached their obligations to the board. In a joint judgment, the three members of the Court, Dixon, McTiernan, and Fullagar JJ, held that the nature of the duty “does not differ materially from the duty which rests on trustees in relation to investments” (641). One issue concerned a loan of £41,500 granted by the board to Mr Fouche to finance the building of a hotel. The loan was in addition to an earlier loan of £3,500, both of which were granted on the security of the land. The board sought orders including declarations that the loan was ultra vires and that it had been made in breach of trust. The High Court explained that the investment was “of a hazardous and speculative nature”. The value of the security depended entirely on the success and prospects of the business to be carried on (633). However, no serious inquiries were made about important matters and “the most elementary precautions were neglected, and very special risks which were obvious seem to have been ignored” (634). The High Court also referred to evidence accepted by the primary judge from two expert witnesses, Mr Edney Moore and Mr Waldron. Their evidence was that a valuation was not possible because (i) there was no known market for the hotel in the country surroundings in which it would be built, and (ii) the value of the hotel could not be considered other than in connection with the business being conducted in it. The High Court referred to the “fate” of two luxurious country hotels in New South Wales (634).
2. a submission was made that no orders could be made against the members of the board because no loss had been suffered. The High Court did not reject this proposition on the basis that loss was not required. Instead the High Court held that the evidence showed a sufficiently strong probability of loss to justify a declaration (641-642):

It was said that no order could or should be made, because it was not proved that any loss had been or would be incurred, and that the only evidence as to the value of the land with the uncompleted building on it was that it was worth £55,000, which would indicate that there would be no loss. But, in the light of what was said by Messrs. Waldron and Edney Moore, this evidence as to value carries no weight. The evidence as a whole suggests a sufficiently strong probability of loss to justify making a declaration of liability against Messrs. Rule, Biggins, Wadley and White.

1. In *Elder’s Trustee and Executor Company Limited v Higgins* [1963] HCA 48; (1963) 113 CLR 426, the High Court considered whether the failure to exercise an option to purchase amounted to a breach of trust. The primary judge had concluded that it did and had made a declaration that “the defendant has been guilty of breaches of trust and negligence in the performance of its duties and in the exercise of its discretions as the sole trustee … particulars of which said breaches of trust and negligence are set forth in the statement of claim.” An enquiry was directed to ascertain the loss suffered (447).
2. The majority of the High Court (Dixon CJ, McTiernan and Windeyer JJ; Owen J dissenting) held that the trustee had breached his duties. However, the orders were defective because they left uncertain the “breaches of trust and negligences” that were found to have been committed and which were the subject of the enquiry (448). Dixon CJ, McTiernan and Windeyer JJ considered whether the trustee was liable for breach of trust separately from the question of loss. They agreed with the learned trial judge that the trustee must be held liable for a breach of trust (452). But the Court then said (453):

The next question is what is the relief to which the plaintiffs were entitled? The *liability of a trustee committing a breach of trust is measured by the loss or depreciation which his act or omission has caused to the trust estate.* He must make good any depreciation and damage which the estate has suffered.

(Emphasis added.)

### ASIC’s revised submission

1. In closing submissions ASIC conceded that a completely constituted cause of action for breach of trust based upon a trustee’s duty of care and skill required proof of loss caused by the breach of trust. That concession was the plain consequence of ASIC’s submission that it had proved a breach of duty (including a risk of loss) but had not proved that the breach of duty was actionable (ts 699-700). For the reasons I have explained, that concession should be accepted.

## Was the equitable duty breached?

1. Since I have reached the conclusion that the equitable duty was excluded, it is not necessary to consider whether, *if it had existed,* it would have been breached. Nor do I consider that it is appropriate to engage in a lengthy obiter dicta discussion of whether a breach would have occurred for four reasons.
2. **First**, in *Elder’s Trustee*, Dixon CJ, McTiernan and Windeyer JJ said that in considering whether a trustee duly performed his or her duties, the Court must look at the position as it would then have appeared to a prudent man acting as trustee of the testator’s estate. This assessment takes place at the timeof the alleged breach,and the court is (448):

not to judge what the trustee then did or failed to do by the light of later events that could not then have been surely foreseen. They are relevant in determining what loss resulted from the breach if there were one. They do not help to determine whether or not there was one.

1. An assessment of the circumstances as they appeared to a prudent trustee at the time of breach requires consideration of the costs of the alternative choices that the prudent trustee might have taken. For instance, what would a prudent trustee have assessed to be the consequences of delaying the decision while an independent feasibility study was obtained? What would have been the consequences of refusing the August 2012 Variation? As I explain later, these issues were not explored by ASIC in submissions. ASIC’s position seemed to be that (i) loss had been suffered, (ii) that there had been some lack of care, and therefore that (iii) the loss must have been caused by LMIM’s alleged failure to take care. But as Lindley LJ said in *In re Chapman* [1896] 2 Ch 763, 775, “a trustee is not a surety, nor is he an insurer; he is only liable for some wrong done by himself, and loss of trust money is not per se proof of such wrong”.
2. Although, for reasons I explain later, it is likely that even if the equitable duty had not been excluded I would have concluded that ASIC had not proved an actionable breach of equitable duty (in the sense of a constituted cause of action), it is undesirable to explore this issue in the absence of evidence and submissions which were directed at the alternatives open to a prudent trustee.
3. **Secondly**, although ASIC ran its case on the basis that it needed to prove that a breach of trust had occurred, I have serious doubts whether a breach of trust (whether actionable or not) needed to be proved for ASIC to succeed in a cause of action against the directors for breach of their duties under the *Corporations Act*. ASIC’s assumption that this was required was never explored in submissions although it is likely that ASIC proceeded on this basis as a matter of fairness and propriety because its case had been pleaded in this way from the outset. Unsurprisingly, the respondents accepted the assumption with alacrity and the whole case was run on this basis. But for the reasons I explained in *Australian Securities and Investments Commission v Cassimatis (No 8)* at [4]-[5], [834], it might be seriously doubted whether that consideration requires the Court to be satisfied that the corporation actually breached the duty about which it was foreseeable that it might breach. As I explain later in these reasons, and as all counsel accepted, an assessment of whether a director has breached a duty under s 180(1) of the *Corporations Act* involves consideration of the foreseeability of harm, the likelihood and magnitude of the harm, and the burden of alleviating precautions. It is hard to see why that assessment requires proof of a breach of another duty.
4. **Thirdly**, if the duty had not been excluded, any consideration of whether a breach of trust occurred would require an assessment of whether any equitable duty owed had been moulded or modified by the terms of the MPF Constitution. No submissions were made on this point.
5. As Mason J said in *Hospital Products Ltd v United States Surgical Corporation* [1984] HCA 64; (1984) 156 CLR 41, 102, it is now “acknowledged generally” that the scope of a fiduciary duty must be moulded according to the nature of the relationship and the facts of the case. Some authors have suggested that a trustee’s duty of care is a fiduciary duty: Heydon JD and Leeming MJ, *Jacobs’ Law of Trusts in Australia* (8th ed, LexisNexis Butterworths Australia, 2016) 356-357 [17-18]. But even if the trustee’s duty of care is not a fiduciary duty, as might be expected with a foundation being the same assumption of responsibility as the duty of care owed by non-fiduciaries, the assumption of responsibility which informs the duty must also be moulded by all the circumstances, particularly the terms of the Constitution by which responsibility is assumed.
6. **Fourthly**, there was an unresolved tension in ASIC’s case upon which few submissions were made which would have needed to be addressed in determining whether there was a breach of trust. ASIC submitted in its closing submissions (235-236) that “[i]nvestment in an asset that is inherently hazardous is not prudent and so not open to a person bound to invest in accordance with the standard applicable to a trustee” (citing *Wingecarribee v Lehman Bro*s [2012] FCA 1028; (2012) 301 ALR 1, 237). I have already explained why the notion of “inherent hazard” should not be assessed independently of all of the circumstances, including the purpose of the trust. However, ASIC’s submission would require an assessment of the “hazard” of the loan itself and all of the previous variations. It would be artificial to assess whether a final investment involving a variation of the loan is “hazardous” without assessing the hazard of the loan itself. But ASIC did not plead its case that way. There was no pleaded allegation of negligence in entering into the loan, or in any of the loan variations prior to August 2012 (the allegations in relation to September 2011 were abandoned).
7. In closing submissions ASIC appeared at times to imply that the making of the loan, or the earlier variations, were a breach of duty. ASIC said that “[n]o explanation was provided as to why the further increase had not previously been foreseen or why the previous synopses dealing with the earlier decisions did not anticipate the need for the further advance” ([280]). And ASIC referred to “what was by August 2012 a demonstrated and consistent failure by the borrower to properly forecast the finance required for the project or to adhere to previous budgets” ([281]). To the extent that they are accurate, I have considered these matters as background circumstances to the August 2012 Variation. However, it must be reiterated that (i) there was no allegation that the decision to make the loan or to grant any earlier variation was a breach of duty, and (ii) in any event, these submissions are not entirely accurate. As I have explained above, the loan and the variations were not expected to be “once and for all” amounts for the entire development. Indeed, in relation to the variation which was most proximate to the August 2012 Variation (the September 2011 variation), LMIM had predicted, with considerable accuracy (if the loan account is taken as accurate at that time), that a limit of $180 million would be needed until the end of March 2012.

## Section 22 of the *Trusts Act* was excluded

### The history and terms of s 22

1. Section 4(1) of the *Trusts Act* provides that “[e]xcept where otherwise provided, this Act applies to every trust, as defined in section 5, whether constituted or created before or after the commencement of this Act”. Section 5 of the *Trusts Act* defines “trust” as extending to implied, resulting, bare and constructive trusts.
2. Section 22 of the *Trusts Act* is in Part 3 of the Act. It provides:

**22 Duties of trustee in relation to power of investment**

(1) A trustee must, in exercising a power of investment—

(a) if the trustee’s profession, business or employment is, or includes, acting as a trustee or investing money for other persons—exercise the care, diligence and skill a prudent person engaged in that profession, business or employment would exercise in managing the affairs of other persons; or

(b) if the trustee’s profession, business or employment is not, or does not include, acting as a trustee or investing money for other persons—exercise the care, diligence and skill a prudent person of business would exercise in managing the affairs of other persons.

(2) A trustee must, in exercising a power of investment, comply with a provision of the instrument creating the trust that is binding on the trustee and requires the obtaining of a consent or approval or compliance with a direction for trust investments.

(3) A trustee must, at least once in each year, review the performance, individually and as a whole, of trust investments.

1. Section 22 was inserted by s 5 of the *Trusts (Investments) Amendment Act 1999* (Qld). In the second reading speech in support of the *Trusts (Investments) Amendment Bill 1999* (Qld), the Minister (Hon MJ Foley, 8 June 1999, 2179) said:

The Bill gives a trustee power to invest in any property, subject to the trust instrument, but at the same time he or she is required to exercise the care, diligence and skill that a prudent person of business would exercise in managing the affairs of others. A trustee whose profession, employment or business is acting as a trustee or investing money on behalf of others is required to exercise the care, diligence and skill of a prudent person engaged in that profession. This requires a higher standard for professional trustees.

1. Section 22(1) replaced a regime which prescribed a trustee’s statutory power to invest in various forms of security. As I explain below, this was known as the “statutory list” approach. Prior to the 1999 amendments, s 20 and s 21 of the *Trusts Act* were the opening provisions contained in Div 1 of Part 3 (“Investments”). Those sections provided:

**Application of part**

20(1) Subject to subsection (2) the provisions of division 1 shall apply if and so far only as a contrary intention is not expressed in the instrument (if any) creating the trust; and every power conferred by the provisions of division 1 shall be exercised according to the discretion of the trustee, but subject to any consent or direction required by the instrument (if any) creating the trust or by statute with respect to the investment of funds.

(2) The provisions of section 21(1)(a) (so far as relates to the parliamentary stocks or public funds or government securities of the Commonwealth or of the State) and section 21(1)(e) shall apply whether or not a contrary intention is expressed in the instrument (if any) creating the trust.

(3) The provisions of division 2 shall apply whether or not a contrary intention is expressed in any other Act or in the instrument (if any) creating the trust.

**Authorised investments**

21(1) A trustee may invest any trust funds in the trustee’s hands, whether at the time in a state of investment or not, in manner following, that is to say—

(a) in any of the parliamentary stocks, public funds or government securities of the United Kingdom, of the Commonwealth, of any State or Territory of the Commonwealth, or of the Dominion of New Zealand;

(b) on first legal or first statutory mortgage of an estate in fee simple in land in any State or Territory; or first statutory mortgage of Crown land held on perpetual lease in the State;

(c) in the purchase—

(i) of land in fee simple in any State or Territory; or

(ii) of leasehold land in the State held for a term of 40 years or more unexpired at the time of the purchase; or

(iii) subject to the provisions of the *Land Act 1994*, of any agricultural farm or grazing homestead freeholding lease of land held from the Crown under that Act;

(d) in debentures or other securities charged on the funds or property of the Brisbane City Council or of any local government in the State;

(e) in any 1 or more of the following, namely—

(i) on any interest bearing deposit in any financial institution;

(ii) on the security of a certificate of deposit issued by any financial institution;

(iii) on deposit in any financial institution;

(iv) on the security of a commercial bill of exchange accepted by a financial institution;

(f) with any dealer in the short-term money market, approved by the Reserve Bank of Australia, as an authorised dealer, who has established lines of credit with that bank as a lender of last resort;

(g) in any security in respect of which repayment of the amount secured and payment of interest thereon is guaranteed by the Parliament of the United Kingdom or the Commonwealth or any State or Territory of the Commonwealth or New Zealand;

(ga) in any investment with or security issued by the Queensland Industry Development Corporation;

(h) in any of the stocks, funds or securities for the time being authorised for the investment of cash under the control or subject to the order of the court;

(i) in any security authorised by, or under, any Act as a security in which a trustee may invest trust funds;

(k) in the purchase of shares in, or the deposit of money with, a building society approved for that purpose under the *Financial Institutions (Queensland) Act 1992*, section 27;

(ka) in a common fund established by a trustee corporation under the *Trustee Companies Act 1968* the investment of which is restricted to a class or classes of investment authorised by subsection (1)(a) to (k).

(2) A reference in any Act to an authorised investment under the provisions of section 4 of the repealed Acts shall be deemed a reference to an authorised investment under the provisions of this section.

### The duty under s 22(1) of the Trusts Act can be excluded

1. ASIC submitted that neither the duty imposed by s 22 nor the liability in equity for breach of s 22 can be excluded or modified. The strongest factor in favour of ASIC’s construction is that s 22(1) uses the word “must”. Read in isolation that word might appear to impose a duty and not to contemplate the possibility of varying that duty by provision in the trust instrument. However, the alternative possibility is that the word “must” creates a mandatory *default* rule or implication with which the trustee must comply, in the absence of a contrary intention expressed in the trust instrument. That alternative is the better interpretation in light of: (i) textual and structural considerations; (ii) the background to the amendment which introduced s 22(1); and (iii) the anomalies that would otherwise be the case. Each of these is considered below.

#### Textual and structural considerations

1. There are three significant textual indications why s 22(1) of the *Trusts Act* does not restrict exclusions or limitations of liability in the trust instrument. The first is an express term to this effect in relation to the power to which the s 22(1) duty relates. The second is the structure and sequence of express provisions in the Act concerning duties and powers which are subject to any contrary provision in the trust instrument. The third is the operation of s 23(3) of the *Trusts Act*.
2. The **first** textual indication is s 4(4) of the *Trusts Act*,whichprovides:

The powers conferred by or under this Act on a trustee are in addition to the powers given by any other Act and by the instrument (if any) creating the trust; but the powers conferred on the trustee by this Act, unless otherwise provided, apply if and so far only as a contrary intention is not expressed in the instrument (if any) creating the trust, and have effect subject to the terms of that instrument.

1. Although s 4(4) refers to *powers* rather than duties, the prudent person duty in s 22(1) is not independent of a trustee’s powers. The duty is one which arises *in exercising a power of investment*. The content of the duty depends upon the terms of the power. Hence, a prudent person would not exercise a power which requires investment in junk bonds by investing in government securities. And a prudent person would not exercise a power which requires investment in government securities by investing in junk bonds. The prudent person duty conditions the manner of exercise of the power but the content of the power determines the content of the duty.
2. In some contexts, therefore, it has been held that the reference in s 4(4) to “a contrary intention … expressed in the instrument” concerns not merely the *power* but also any terms upon which it is to be exercised and duties in relation to its exercise. On this approach, s 22(1) would fall within the provision in s 4(4) that the power (and associated duty) applies unless a contrary intention is expressed in the trust instrument.
3. A context in which this conclusion has been reached can be seen in the decision in *Re Turner’s Will Trusts* [1937] Ch 15. *Re Turner’s Will Trusts* concerned the exercise of a statutory power in s 31 of the English *Trustee Act 1925*,which is in similar terms as s 61 of the Queensland *Trusts Act*. That section conferred a powerfor trustees to apply trust funds including for the maintenance of an infant. That power was subject to a statutory duty which provided that the trustee was under a duty in particular circumstances in relation to income which did not vest in that the trustee “shall thenceforth pay the income of that property and of any accretions thereto…” (22). The trustee in *Re Turner’s Will Trusts* submitted that the statutory duty could be overridden by the trust instrument. The trustee relied upon s 69(2) (the equivalent English provision to s 4(4)), which provides that powers are subject to the contrary intention expressed in the trust instrument.
4. The question in *Re Turner’s Will Trusts* was whether the *duty* in s 31 could be excluded by the trust instrument even though s 69(2) permits this only in the instance of powers. Lord Justice Romer delivered the judgment of the Court of Appeal (which included Lord Wright MR and Greene LJ). His Lordship said that “it has, of course, to be conceded that in terms the sub-section refers only to ‘powers’ but it is necessary to ascertain precisely what it is that the Legislature intended by that word” (23). His Lordship concluded that the maintenance power in s 31 is like other powers in the Act which (27):

either confer powers upon trustees expressly, or contain provisions ancillary to the exercise of trustees’ powers, and correspond with what, when contained in settlements, would be comprehensively referred to by conveyancers as the Trustees’ Powers. This being so, the provisions of s. 31 may properly be called comprehensively the statutory powers of maintenance just as those of s. 32 may properly be called comprehensively the statutory powers of advancement. The fact that s. 31 contains provisions that are directory is immaterial. Powers of maintenance, in the comprehensive meaning of that term, usually do. Nothing is more common, for instance, than a direction to trustees to accumulate during the minority income not applied in maintenance. Such a direction is merely ancillary to the power of maintenance strictly so called, and may well be regarded as a part of the power of maintenance in its comprehensive sense … This statutory power of maintenance, that is to say, the totality of the provisions, to be found in s. 31 of the Act, is, in our opinion, one of the “powers conferred by this Act”.

1. The decision in *Re Turner’s Will Trusts* was thereforethat the power in s 31 *included* the ancillary duty to apply income in particular circumstances and could be overridden by the trust instrument. That decision was applied on a number of subsequent occasions before the English s 69(2) was copied and included in s 4(4) of the Queensland *Trusts Act*: *Re Ransome* [1957] Ch 348; *Inland Revenue Commissioners v Bernstein* [1960] Ch 444; *Inland Revenue Commissioners v Bernstein* [1961] Ch 399; and *In re Erskine’s Settlement Trusts* [1971] 1 WLR 162.
2. It was against this background, concerning the same provision as s 4(4), that the “prudent person” duty was included in the *Trusts Act* by the 1999 amendments.
3. ASIC submitted that the reasoning in *Re Turner’s Will Trusts*, and the cases which followed it, could be distinguished from the operation of s 22. ASIC said that, unlike s 21 and s 22 of the Queensland *Trusts Act*, the provisions considered in *Re Turner’s Will Trusts* revealed a legislative intention to render those provisions subject to the terms of the trust instrument. ASIC submitted that s 22 of the *Trusts Act* is “neither part of nor ancillary to the statutory powers conferred by s 21”, and that “s 22 applies more broadly to the exercise of any investment power; it is not limited in operation to apply only in respect of the statutory powers in s 21” (whereas s 3(1)(ii) of the *Trustee Act 1925* was ancillary to the statutory power of maintenance). These submissions require distinctions to be drawn between (i) duties which are ancillary to powers of maintenance or advancement, and (ii) duties which are ancillary to powers of investment. There are distinctions between these duties but the close association between powers and duties in various contexts of the *Trusts Act* is a relevant aspect of the historical background against which s 22(1) and s 4(4) fall to be construed.
4. ASIC also submitted that the use of “must” in s 22(1) showed that the legislature had “otherwise provided” for a circumstance where a contrary intention in the trust instrument would not override the legislation. However, as I explain in the second point below, the use of the word “must” is not a provision “otherwise” in Part 3. The provision otherwise in Part 3 is the express provision which provides that for Part 3, “Sections 29 to 30C apply despite anything contained in the instrument creating the trust”.
5. **Secondly**, and separately from s 4(4), there is another textual indication which would also lead me to reach the same conclusion. This is that, unlike s 22(1), other sections of the *Trusts Act* expressly entrench the statutory obligations by providing that, except where otherwise stated, the terms apply despite anything contained in the instrument creating the trust. Those other sections are the opening provisions in various Parts of the *Trusts Act*:
6. s 10 (applying the entrenchment to all of Part 2);
7. s 31 (applying the entrenchment to all of Part 4);
8. s 60 (applying the entrenchment to all of Part 5);
9. s 65 (applying the entrenchment to all of Part 6);
10. s 79 (applying the entrenchment to all of Part 7); and
11. s 111 (applying the entrenchment to all of Part 10).
12. Section 22(1) falls within Part 3. The opening provision of Part 3 of the *Trusts Act* is s 20. However, unlike the opening provisions in Parts 2, 4, 5, 6, 7, and 10, s 20does not extend to entrench all provisions in Part 3. It provides only that:

**20 Application of particular provisions**

Sections 29 to 30C apply despite anything contained in the instrument creating the trust.

1. In other words, the plain inference from s 20 as well as the opening section of each other Part is that ss 21 to 28 *are* subject to anything contained in the instrument creating the trust. As Heydon and Leeming observe, “It follows that, except where otherwise specifically indicated, ss 21-28 are subject to the trust instrument”: see Heydon JD and Leeming MJ, *Jacobs’ Law of Trusts in Australia* (8th ed, LexisNexis Butterworths Australia, 2016) 390 [18-07].
2. This conclusion is confirmed by the report of the Queensland Law Reform Commission (**QLRC**) which described the approach taken in the 1973 Act, which was replicated in the 1999 amendments. The report is admissible “extrinsic material” (*Acts Interpretation Act 1954* (Qld) s 14B(3)(b)). The 1971 report, written prior to the passage of the Bill that became the *Trusts Act*, set out the desirability in some respects of excluding the legislation’s operation (Queensland Law Reform Commission, *A Report of the Law Reform Commission on the Law Relating to Trusts, Trustees, Settled Land and Charities* (QLRC 8, 16 June 1971) 8):

It is also intended to permit a settlor to exclude provisions of the proposed Act which may appear controversial, such as the statutory power to invest in various forms of security other than government stocks, etc. To this extent the provisions of the trust instrument, if to the contrary of the provisions of the proposed Act, will apply; but there are many provisions which, as a matter of policy, must prevail over the terms of the trust instrument, e.g. the trustee’s powers of sale, disposition and other dealing with the trust property specified in Part IV of the Bill. *In the result, we have thought it advisable, in addition to cl. 4(4), to prescribe at the commencement of each Part the extent to which the provisions of that Part prevail over any contrary terms of the trust instrument.*

(Emphasis added.)

1. ASIC effectively submitted that the Court should construe Part 3 of the *Trusts Act* independently of the rest of the Act because the *Trusts (Investments) Amendment Act 1999* replaced the entirety of Part 3. Hence, ASIC submitted, “[n]or should the dissimilarity between s 20 and like provisions at the commencement of other parts of the *Trusts Act* be considered significant”. I do not accept this submission. It is well established that the construction of an Act requires consideration of the Act as a whole, a matter which the legislature is taken to have known when amending Part 3: *Commissioner of Stamps (South Australia) v Telegraph Investment Company Pty Limited* (1995) 184 CLR 453, 479 (McHugh and Gummow JJ).
2. **Thirdly**, s 22(1) appears in close proximity to s 23(3) of the *Trusts Act*. Section 23(3)provides:

A rule or principle of law or equity relating to a provision in an instrument creating a trust that purports to exempt, limit the liability of, or indemnify a trustee in relation to a breach of trust, continues to apply.

1. The function of s 23(3) seems to be the preservation of rules of law and equity concerning provisions in a trust instrument that exempt or limit a trustee’s liability. Those rules of law and equity sometimes restrict the operation of such clauses (for instance, a clause which purports to exempt liability for fraud will be void). Or, as we have seen, they can recognise the efficacy of such clauses. Section 23(3), which provides that such principles of law continue to apply, would be a curious provision if the previous provision, s 22(1), had excluded them.

#### Amendment context: position prior to the 1999 amendments

1. Section 22(1) should be construed in the context of the amendment that Parliament made to the *Trusts Act* by introducing the section in 1999. Prior to the introduction of s 22(1), the position in Australia, England, Canada, and New Zealand was that trustees owed a duty to act as a prudent person, but many authorities permitted the duty to be excluded in cases other than fraud (although there was controversy prior to *Armitage* concerning whether the liability could be excluded in cases of gross negligence). Those authorities may have originated with *Wilkins v Hogg*, where the Lord Chancellor, Lord Westbury, said that the trustee “was at liberty to say, ‘Your duty shall require no more of you than this’. The Court could not extend the office, or invest it with greater obligation” (43).
2. Prior to the introduction of s 22(1), the *Trusts Act* was consistent with such exclusion. The *Trusts Act* did not prescribe any duty. It only provided for a regime for authorised investments.
3. ASIC submitted that “the imposition of the general statutory duty in s 22 to exercise care, diligence and skill was the *quid pro quo* for providing a more permissive investment power”. There is some support for this submission in the second reading speech of the *Trusts (Investments) Amendment Bill 1999* (Qld) (Hon MJ Foley, 8 June 1999) 2179 (quoted above).
4. The difficulty with this submission is that trustees *already* had a more permissive investment power than the limited investments provided by the statutory list. The purpose of the amendments to the *Trusts Act* was not to abolish the possibility, which had existed for 150 years, of excluding the trustee’s duty of care. To the contrary, the amendments involved a move towards uniformity. The amendments to the *Trusts Act* occurred at a time when similar provisions had been enacted in other States or were being enacted in other States. Each other State permitted the prudent person duty to be subject to the terms of the trust instrument.
5. At the commencement of the second reading speech of the *Trusts (Investments) Amendment Bill*, the Minister explained that the primary purpose of the Bill was to alter the law relating to the investment of trust funds which is sometimes referred to as the “statutory list” approach (Hon MJ Foley, 8 June 1999, 2178-2179). He said that the other Australian States and the Northern Territory had used the statutory list approach but the approach was “not uniform amongst them”. The Minister explained that:

Over the last several years all of the Australian States and Territories have replaced, or are in the process of replacing, this list of authorised trustee investments. As I am informed, Queensland and the Australian Capital Territory are the last two remaining jurisdictions to remove this list and replace it with a new approach to investment called the “prudent person rule”.

1. Each of the Australian States and Territories to which the Minister referred had legislation which permitted the prudent person test to be excluded by the trust instrument: see *Trustee Act 1898* (Tas) s 7(1); *Trustee Act* *1907* (NT) s 6(1); *Trustee Act 1925* (NSW) s 14A(1); *Trustee Act 1925* (ACT) s 14A(1); *Trustee Act 1936* (SA) s 7(1); *Trustee Act 1958* (Vic) s 6(1); and *Trustees Act 1962* (WA) s 18(1). In particular, at the time that the *Trustee Act* was enacted:
2. the Tasmanian provision which was equivalent to s 22(1) began with the words “Subject to any provision to the contrary in an instrument creating a trust” (this provision commenced on 1 April 1998);
3. the Northern Territory provision which was equivalent to s 22(1) began with the words “Subject to the instrument creating the trust” (this provision commenced on 26 February 1996);
4. the New South Wales provision which was equivalent to s 22(1) began with the words “This section has effect subject to the instrument (if any) creating the trust” (this provision commenced on 13 March 1998);
5. the Australian Capital Territory provision which was equivalent to s 22(1) began with a subsection providing that “This section has effect subject to the instrument (if any) creating the trust” (this provision commenced on 21 May 1999);
6. the South Australian provision which was equivalent to s 22(1) began with the words “Subject to the instrument creating the trust” (this provision commenced on 1 July 1995);
7. the Victorian provision which was equivalent to s 22(1) began with the words “Subject to the instrument creating the trust” (this provision commenced on 1 January 1996); and
8. the Western Australian provision which was equivalent to s 22(1) began with the words “Subject to the instrument creating the trust” (this provision commenced on 16 June 1997).

#### The anomalous results if the Trusts Act were to prevent exclusion of the s 22(1) duty

1. If ASIC’s submission were correct there would be anomalies in the operation of the *Trusts Act.* These anomalies militate against ASIC’s construction.
2. **First**, the *Trusts Act* does not prevent a clause, appropriately drafted, from excluding fiduciary duties, which can occur provided that those duties do not constitute the core of the trust obligations. Indeed, s 23(1) of the *Trusts Act* contemplates this possibility. Section 23(1) provides:

A rule or principle of law or equity imposing a duty on a trustee exercising a power of investment continues to apply except so far as it is inconsistent with this or another Act or the instrument creating the trust.

1. It would be a curious result if s 22(1) of the *Trusts Act* entrenched obligations to act as a prudent person but did not entrench fiduciary duties, and permitted those duties to be modified by the trust instrument.
2. Fiduciary duties are shaped, and can be modified, by the trust instrument or an underlying contract. For instance, in *Kelly v Cooper* [1993] AC 205, 215, the Privy Council held that no breach occurred since the contract of agency envisaged that the fiduciary might have a conflict of interest. The decision in *Kelly v Cooper* was applied by Lord Browne-Wilkinson in *Henderson v Merrett Syndicates Ltd* where his Lordship said that “[a]lthough an agent is, in the absence of contractual provision, in breach of his fiduciary duties if he acts for another who is in competition with his principal, if the contract under which he is acting authorises him so to do, the normal fiduciary duties are modified accordingly” (206): see also *Chan v Zacharia* [1984] HCA 36; (1984) 154 CLR 178, 196 (Deane J). The decision in *Kelly v Cooper* has also been approved in Australia: *Australian Securities and Investments Commission v Citigroup Global Markets Australia Pty Ltd (No 4)* [2007] FCA 963; (2007) 160 FCR 35, 77 [278]-[279] (Jacobson J); and *Backwell IXL Pty Ltd v Robert Grant Hogg* [1998] VSC 155 [41]-[42] (Chernov J).
3. **Secondly**, s 22(1) of the *Trusts Act* is concerned only with the prudent person duty at a high level of abstraction. For instance, it is not concerned with remedies for breach of duty, including the rules concerning compensation for losses, which are left to general equitable principles. Nor is s 22(1) concerned with the matters to which the court will have regard in determining whether the actions of the trustee were prudent. Section 30B(a) of the *Trusts Act* provides that one matter which the court mayconsider is the nature and purpose of the trust. The effect of s 30B(a) is that the nature and purpose of the trust is considered for the purpose of determining whether the trustee acted prudently, and it therefore shapes the content of the trustee’s duty. If ASIC’s submission were correct, it could shape the content of the duty but it but it could not exclude the duty.

#### Contrary views

1. ASIC relied upon opinions expressed about the operation of s 22 of the *Trusts Act*. For instance, the QLRC concluded in its interim report in June 2013 that since the *Trusts Act* makes no provision for the duties imposed by s 22 of the *Trusts Act* to be excluded then “those duties apply whether or not a contrary intention is expressed in the trust instrument” (Queensland Law Reform Commission, *A Review of the Trusts Act 1973 (Qld): Interim Report* (WP No 71, June 2013) 5.17).
2. In its final report in December 2013, the QLRC explained the *power* and *duties* distinction in the existing s 22 and s 4(4) as follows (Queensland Law Reform Commission, *A Review of the Trusts Act 1973: Report* (Report No 71, December 2013) 61 [4.7]):

Further, although the current Act does not provide expressly that existing sections 22 and 24 apply despite a contrary intention in the trust instrument, there is no scope under the Act for a trust instrument to exclude the duties imposed by those sections or the effect of existing section 26. *In certain circumstances, existing section 4(4) enables* powers *that are conferred under the Act to be excluded by a trust instrument, but it does not make any similar provision for a trust instrument to exclude provisions of the Act that impose duties or that provide for other matters.* Accordingly, clauses 48, 49, 51 and 52 (which replace existing sections 22(1)(a) and (3), 24 and 26) have the same application as the provisions that they replace.

(Emphasis added.)

1. The QLRC also recognised in its final report the effect of a contrary intention in the trust instrument as follows (9-10):

***The effect of a contrary intention in the trust instrument***

1.10 Although clause 3 generally replaces existing section 4(1)–(4), it does not include a provision to the same effect as the main part of existing section 4(4).

1.11 Existing section 4(4) provides that, ‘unless otherwise provided’, the powers conferred by the Act on a trustee apply ‘if and so far only as a contrary intention is not expressed in the instrument (if any) creating the trust’.

1.12 The words ‘unless otherwise provided’ point to the application provisions at the beginning of each of the parts of the current Act that confer powers on trustees. In particular, existing section 31(1) states that, except where otherwise provided in Part 4 of the Act, the provisions of that part ‘shall apply whether or not a contrary intention is expressed in the instrument (if any) creating the trust’. To the extent that the provisions in Part 4 of the Act confer powers on trustees, this operates as an exception to the general position set out in existing section 4(4). In turn, it is subject to the particular exceptions that apply in some of the provisions of Part 4, which are expressed to apply subject to a contrary intention in the trust instrument.

1.13 The Commission considers that the better approach to indicating whether or not the provisions are subject to a contrary intention in the trust instrument is to rely on the general application provisions at the beginning of the various parts of the Draft Bill, and the limited exceptions to those provisions within the relevant part (if any). This allows for greater consistency and, in particular, removes any potential confusion about the relationship between existing sections 4(4) and 31(1).

(Footnotes omitted.)

1. Whilst I acknowledge the force in this opinion from an esteemed body, I do not accept the conclusion for the reasons discussed above, many of which do not appear to have been the subject of submission to the QLRC, concerning (i) textual and structural considerations; (ii) the background to the amendment which introduced s 22(1); and (iii) the anomalies that would otherwise be the case.
2. ASIC then argued that “even if, as a matter of legal principle, s 22 could be excluded, the provisions in the constitution would not achieve that exclusion”. It is necessary to turn to the MPF Constitution.

### Clause 12.8 of the MPF Constitution is effective to exclude s 22(1)

1. Apart from the submissions in relation to whether cl 12.8 of the MPF Constitution operates to exclude the equitable duty (which I have addressed above), ASIC submitted that cl 12.8 operates to exclude the duty under s 22(1) of the *Trusts Act* for an additional reason.
2. ASIC submitted that the prudent person duty in s 22(1)(a) was an *existing* duty in December 2001 when the MPF Constitution was executed. The current s 22 was inserted by s 5 of the *Trusts (Investments) Amendment Act 1999*. But cl 12.8(b) provides that the exclusion “specifically applies to any ‘Prudent Person Rule’ or the like which may be implied by any *future* enactment of legislation” (emphasis added). Hence, ASIC submitted, the duty had not become implied by a “future enactment of legislation”. In oral submissions, senior counsel for ASIC said that cl 12.8(b) would therefore apply only if “the *Trusts Act* is repealed and another Act comes into play” or possibly if s 22 were amended (ts 723).
3. There are two reasons why I do not accept this submission.
4. The first is that ASIC’s construction of cl 12.8(b) has an extremely uncommercial consequence in that an existing duty in s 22 is not within cl 12.8(a), but if the identical duty were re-enacted, perhaps within consolidating legislation, then it *would* fall within cl 12.8(a). Further, a future enactment of legislation might include the replacement of s 22 by an amendment which caused minor textual changes. On ASIC’s construction, this future enactment would bring s 22 within cl 12.8(a) but the earlier provision would not fall within the clause. ASIC could not provide any explanation for the commercial purpose of a clause which could operate in such a way. A commercial contract is to be construed so as to avoid it “making commercial nonsense or working commercial inconvenience”: *Electricity Generation Corporation v Woodside Energy Ltd* [2014] HCA 7; (2014) 251 CLR 640, 657 [35] (French CJ, Hayne, Crennan and Kiefel JJ). So too, a commercial trust is to be construed in the same way: *Byrnes v Kendle* [2011] HCA 26; (2011) 243 CLR 253, 286 [102] (Heydon and Crennan JJ).
5. The second reason, as I have explained above, is that as a matter of construction cl 12.8(b) plainly contemplates that a duty of care (including a “prudent person rule”) falls within the concept of cl 12.8(a) because cl 12.8(b) does not derogate “from the generality” of cl 12.8(a). In other words, even if cl 12.8(b) was intended to apply only to include future enactments of a prudent person rule, it demonstrates that the generality of cl 12.8(a) should include existing enactments of that rule.

## Was the duty in s 22(1) of the *Trusts Act* breached?

1. ASIC submitted that the issues in dispute in relation to the allegation of breach of the equitable duty are identical to the issues in relation to the allegation of breach of s 22(1)(a) of the *Trusts Act*, save only in respect of the issue as to whether the duty under s 22(1)(a) can be excluded. For the same reasons in relation to whether the equitable duty was breached, it is neither necessary nor appropriate to consider whether the duty in s 22(1) was breached.
2. However, an additional reason which it is not appropriate to attempt to consider whether s 22(1) was breached is that I do not necessarily accept ASIC’s submission that the issues in relation to breach of s 22(1)(a) are necessarily identical to breach of the equitable duty. The former require consideration of s 24 and s 30B of the *Trusts Act.* Section 24(1) of the *Trusts Act* provides:

**24 Matters to which trustee must have regard in exercising power of investment**

(1) Without limiting the matters a trustee may take into account when exercising a power of investment, a trustee must, so far as they are appropriate to the circumstances of the trust, have regard to the following matters—

(a) the purposes of the trust and the needs and circumstances of the beneficiaries;

(b) the desirability of diversifying trust investments;

(c) the nature of and risk associated with existing trust investments and other trust property;

(d) the need to maintain the real value of the capital or income of the trust;

(e) the risk of capital or income loss or depreciation;

(f) the potential for capital appreciation;

(g) the likely income return and the timing of income return;

(h) the length of the term of the proposed investment;

(i) the probable duration of the trust;

(j) the liquidity and marketability of the proposed investment during, and at the end of, the term of the proposed investment;

(k) the total value of the trust estate;

(l) the effect of the proposed investment for the tax liability of the trust;

(m) the likelihood of inflation affecting the value of the proposed investment or other trust property;

(n) the cost (including commissions, fees, charges and duties payable) of making the proposed investment;

(o) the results of a review of existing trust investments.

1. Section 30B of the *Trusts Act* provides:

**30B Court may take into account investment strategy etc. in action for breach of trust**

In a proceeding against a trustee for a breach of trust in relation to a duty under this part relating to the trustee’s power of investment, the court may, when considering the question of the trustee’s liability, take into account the following matters—

(a) the nature and purpose of the trust;

(b) whether the trustee had regard to the matters set out in section 24 so far as they are appropriate to the circumstances of the trust;

(c) whether the trust investments have been made under an investment strategy formulated in accordance with the duty of a trustee under this part;

(d) the extent the trustee acted on the independent and impartial advice of a person competent, or apparently competent, to give the advice.

1. No submissions of any party addressed these sections. Some of the factors in the sections were addressed incidentally, but far from all of them.

## The evidence of Mr Woolley

1. Although I do not consider it necessary or appropriate to reach a final conclusion on whether LMIM would have committed a breach of trust if the terms of the MPF Constitution had been different, it is necessary to explain why such an assessment would have necessarily proceeded without regard to any of the expert evidence from Mr Woolley.
2. Mr Woolley was called as an expert witness by ASIC. He has degrees in economics and practical experience of more than 31 years in the financial services industry, mostly as an investment manager. He purported to give evidence concerning the approach of a prudent trustee including in relation to the 7 August 2012 decision to approve the August 2012 Variation. Unfortunately, he had paid scant attention to the key documents. And when confronted by matters which were inconsistent with ASIC’s case, many of his answers were preposterous. He displayed the worst characteristics of partisanship and could not, in any respect, be described as an independent expert.
3. After considering Mr Woolley’s evidence, ASIC chose not to rely on his evidence in any relevant respect. As a model litigant, ASIC quite properly accepted that it could not reasonably submit that the Court should accept his evidence except where the evidence remained essentially unchallenged ([6], [220]). The matters upon which ASIC placed weak reliance were sections of Mr Woolley’s report where he asserted that an independent feasibility analysis of the anticipated future cash flows from the Maddison Estate development ought to have been obtained. However, my concerns with Mr Woolley’s evidence are so significant that I do not consider that it is possible to fillet even those areas of his evidence. The extent of my concerns about his credibility and about his reliability combine to give the effect that none of his evidence is capable of acceptance. Apart from issues of demeanour and the general conduct of Mr Woolley’s evidence including his evasiveness and inability or unwillingness to answer simple questions, the reasons why his evidence was neither credible nor reliable are as follows.
4. **First**, Mr Woolley did not properly consider many basic documents or issues which should have been necessary for him to form an opinion. One example was the RPS or core economics analysis that was referred to in an email with which he was provided (ts 628-629). He accepted in cross-examination that the report contained important information (ts 629) but said that he did not ask for it to be provided because he assumed that ASIC would have provided him with everything relevant (ts 631). Another example was that despite the importance of their roles and their prominence in many of the emails, Mr Woolley did not know who Mr Tickner and Mr McDonald were (ts 626), and said he “wouldn’t have a clue who LM Investment Management [LMIM] was” (ts 625). He also could not remember what issues Ernst & Young had identified as being problematic with the development (ts 624). He offered his opinion on the scope of the auditors’ obligations although he did not know what they had been asked to do (ts 637).
5. **Secondly**, Mr Woolley’s conclusions (pertaining, for example, to the risks presented to the MPF from the September 2011 variation and August 2012 Variation) were based upon some very basic misapprehensions about fundamental points. In relation to the August 2012 Variation, he said that between $240 million and $259 million of capital was at risk. He said that this was because $100 million would leave the MPF (ts 633). As I have explained, this assumption was incorrect. Only $16.5 million would leave the fund. After numerous questions, Mr Woolley finally conceded that he did not take into account that only around $16.5 million of capital would leave the fund, and that the difference between $16.5 million and $100 million was “significant” (ts 634).
6. Another example of a basic mistake made by Mr Woolley was that he did not appreciate that the joint venture arrangement for Maddison Estate was structured so that the profit from the development was passed through a special purpose vehicle as “interest” (ts 584). As I have explained, the loan agreement had an express provision to this effect. Mr Woolley read an investment memorandum which provided:

To simplify investor taxation requirements by ensuring that Fund returns are passed to investors as income and not capital gains, the property related (joint venture) assets of this Fund are held as commercial loans.

Mr Woolley said that he still didn’t realise that this was not an ordinary commercial loan. He thought it was “tax planning” (ts 584).

1. Another example is that Mr Woolley assessed the risk of capital loss on the incorrect premise that in September 2011 and August 2012 there was some value in the land which might be available to repay the Maddison Estate loan (ts 602). As he was inevitably required to accept, the existence of the Suncorp loan meant that, at least in September 2011, on the “as is” valuation of the Pimpama Land, there was no value which could have been realised by LMIM if the land were immediately sold (ts 606).
2. **Thirdly**, Mr Woolley’s report involved some large, and unsupported, leaps of logic. For instance, when assessing the advantages of an externally generated feasibility analysis he said that it would be “more likely… to result in… the trustee deciding to exit the investment in Maddison Estate development”. But he did not say what an independent feasibility report would have said (ts 87). In contrast, ASIC, quite properly, did not contend that an independent feasibility report would necessarily have been different in content from some of the internally produced feasibilities.
3. **Fourthly**, when Mr Woolley was taken to documents which caused difficulty for his conclusions, he took preposterous positions in relation to them. For instance, Mr Woolley was referred to the February 2011 investment memorandum upon which he relied in his report. He said that he would have seen from the information memorandum that the mortgage securities in which LMIM invested were in excess of $200 million, that there were 14 mortgages involved, and that the largest loan was more than $113 million (ts 571). But he maintained that the commercial loan, of more than half of the portfolio, involving $113 million, could be low risk. His response was that he would need to consider all 14 loans (ts 571):

in this case… you get a feel for the spread of risk. That’s what it is there for. Now, what if I said that largest loan happens to be to the Federal Police. I feel pretty comfortable with that loan because I know I’m going to get paid.

1. In other words, knowing that the MPF’s loan balance with Maddison Estate was around $115 million at that time, Mr Woolley speculated, without any basis at all, that the $113 million loan referred to in the information memorandum might have been made to the Federal Police. He later said that he had no information from which he could assess whether the largest loan was to Maddison Estate. Only after he was pressed did he concede that it was obvious that this loan was the Maddison Estate loan (ts 572).
2. His position became even more bizarre when he later suggested that, despite his earlier remarks about spread of risk, a single loan of $113 million, which comprised more than half the fund, was not necessarily indicative of anything other than a low risk profile for the fund.
3. **Fifthly**, Mr Woolley’s evidence was constantly shifting to try to support the outcome of imprudence that he had expressed. For instance, Mr Woolley was asked about views he had expressed about the opinions that would have been held by an “ordinary investor” or “potential investor” reading one of the MPF information memoranda. After being asked different versions of the question five times, Mr Woolley said that he took that investor to be the “average person” (ts 574). This was despite him explaining earlier that he was aware that the fund was marketed through investment advisers and only open to “wholesale” or sophisticated investors who, in his words, “met the threshold of half a million or 2.5 million net assets as certified by your accountant every six months” (ts 567).

## The evidence of Mr Bristow

1. The other expert called by ASIC was Mr Bristow. He presented his evidence in a professional and proper manner. I do not reject his evidence generally. In a number of general respects it should be accepted. However, it is important to emphasise in this section that his evidence had significant limitations which is why I do not accept the criticisms he made of the feasibility reports prepared by the PAM team and why I would not have relied upon them in assessing whether a breach of trust had been committed.
2. Mr Bristow was a qualified, and experienced, valuer with expertise in computer modelling including the use of Excel and Estate Master. His report focused in some detail upon the limitations of Estate Master as a valuation tool.
3. In so far as Mr Bristow’s criticisms of LMIM’s approach to the feasibilities were based upon his analysis as a valuer, I do not accept that those criticisms are pertinent. Mr Bristow accepted in cross-examination that valuers prefer to avoid escalations (ts 520). In comparison, he explained:

The developer lives and breathes by creating new levels of value in the future. The valuer’s job is to analyse the recent past, make adjustments and apply it to the present. And for that reason, valuers and particularly lenders are very reluctant to crystal ball future performance.

1. ASIC rightly did not submit that in making a decision whether to approve the August 2012 Variation, LMIM should have conducted a valuation based on the recent past. LMIM was concerned with whether to lend in relation to a future development. It did not intend to sell the land “as is”.
2. However, I do accept, as Mr Bristow explained in his general evidence, that the Estate Master program was merely a tool which increased the speed at which it was possible to calculate a hypothetical development valuation. He explained that Estate Master calculates the profitability of a development from elements of: (i) land cost; (ii) building cost; and (iii) sale proceeds. However, a comprehensive feasibility requires more than just the inputting of these figures. He explained, and I accept, that a feasibility requires a deep understanding of the asset being valued, including *at the outset* in his words:
3. the physical asset (eg topography, access, flood, aspect, contamination, acid sulphate soils, and views);
4. the legal parameters (eg approvals, town planning, and access);
5. practical options given the above (eg house blocks, apartments, shopping centres, and leisure);
6. the approximate cost of completing possible schemes, typically construction, consultants, approvals, and infrastructure costs; and
7. the time scale involved covering establishment/approval stage, construction and selling period.
8. Mr Bristow also explained that a comprehensive feasibility would also require knowledge of:
9. the value of completed product for all options derived from analysed sales;
10. the demand for all the options from market data (thence resolving a likely time scale for the sale process);
11. the value of comparable land from comparable sales;
12. the cost and availability of finance; and
13. a target profit margin relevant to the risks.
14. Mr Bristow explained, and again I accept, that the value of the conclusions revealed by Estate Master will depend upon the accuracy and validity of the assumptions used (including escalation rates). As for escalation rates, as Mr Bristow explained, abnormally high escalation rates are unlikely to occur in an environment of low cost inflation. Conversely, it is far more likely that high price escalations will occur in periods of high cost inflation and in periods of high interest rates.
15. Although I accept Mr Bristow’s evidence on these general matters such as the operation of Estate Master and feasibilities, I do not accept his criticisms of the feasibilities produced by the PAM team. Mr Bristow’s criticisms were based on far too many assumptions, far too little actual knowledge of the process or the documents, and an absence of any attribution of the relevant feasibilities or their purpose. None of this is said as a criticism of Mr Bristow’s professional approach to his evidence. Mr Bristow frankly acknowledged the time constraints under which he worked in preparing his report and the limited number of documents upon which he had relied.
16. The limitations of Mr Bristow’s evidence on particular matters include the following. Mr Bristow was not aware of crucial facts such as the existence of the PAM team and its work in assessing costs and values (ts 517-518). He examined only the “models”, not the hundreds of documents that the PAM team would have considered (ts 521). He made statements in his report that the feasibility costs were not fully supported. But, by this, he meant only that they were not supported by the documents provided to him by ASIC. Of the hundreds of relevant documents that would have existed, ASIC had only provided him with 88 documents and he did not rely on 43 of them (ts 521-522). Mr Bristow also referred to, and relied upon, numerous different feasibility reports prepared by the PAM team using Estate Master. But those models were identified only by their electronic date of creation, their bar code and file name. There was some confusion about who provided the instructions or the data for the preparation of them. There was also no evidence about the purpose for which they were prepared; as Mr Drake submitted, the file names suggest that the models were prepared for various different purposes such as “Delfin”, “audit”, or “full recovery”.
17. Mr Bristow was also critical of the escalation rates used by LMIM in some of the 2012 models, but he did not consider potentially important matters such as the extent to which, if at all, the enhancements to the Maddison Estate development project (including the wave pool, the volleyball, and the swimming centre) would have increased the escalation rates (ts 520-521). Mr Bristow conceded that if an enhancement such as the wave pool could have permitted an extra 800 units around the pool area then this could have increased the value of the development (ts 536). Of course, the potential for these extra units had not been included in any feasibility but this issue emphasises the importance, which Mr Bristow accepted, of a deep understanding of the development before assumptions such as escalation rates could be made.
18. Ultimately, no doubt recognising these limitations, in ASIC’s closing submissions the only evidence of Mr Bristow relied upon which was critical of the feasibilities was the evidence concerning escalation rates. ASIC’s submissions concerning that evidence were confined to three paragraphs ([210]-[213]). The points made were that:
19. there was a bank of evidence set out in the Ernst & Young report showing a low inflation stable market with only one strong year of growth in 2007;
20. demand for lots and sales rates from competing estates was well documented at four to six sales per calendar month, which did not demonstrate that 16 sales per calendar month were consistently possible;
21. the 11 July 2012 and 17 July 2012 models chose to adopt a high price growth/low cost inflation assumption for the first five years with the assumption that whatever was built would be sold before the succeeding stage was built (without adopting a rate of sale). Mr Bristow stated that none of these assumptions were seemingly supported by research, with the consequence that seemingly zero risk was portrayed; and
22. the impact of the assumptions was to skew the results manifestly. Mr Bristow said that removing all escalations from the 17 July 2012 model results in a $3 million residual value indicating the project to not be feasible by a significant margin. The model was illusory, with all profit contingent on increases in value exceeding cost inflation by a factor of up to five.
23. As to each of these, and apart from Mr Bristow’s lack of a detailed knowledge of the Maddison Estate development:
24. the draft and final versions of the Ernst & Young report were not relied upon as evidence of the truth of its contents. It was relied upon only as a report about which the directors of LMIM should have been aware (ts 88, 285);
25. the point made about sales per calendar month relied upon by ASIC derives from paragraph [100] of Mr Bristow’s report. That paragraph continued, citing the source for the opinion about demand to be “amply demonstrated by draft Ernst & Young report which objectively summarised analysed data in this table”. Again, the Ernst & Young report was not relied upon for the truth of its contents (ts 88, 285); and
26. as to the final two points, the 11 July 2012 model (ie the 30 June 2012 reverse engineered feasibility) was not proved by ASIC to have formed the basis for the August 2012 Variation decision. To the extent that Mr Bristow was critical of the feasibility presented to WPIAS on 17 July 2012, the research considered by Mr Bristow was very limited and did not consider any of the research from the PAM team or perhaps other teams (as discussed above), nor did it take into account factors such as the enhancements or embellishments in 2012. Mr Bristow was also making his assessment with the benefit of hindsight, unlike the assessment made by WPIAS.

# The alleged breaches of Section 180(1) of the *Corporations Act*

## Legal principles concerning s 180(1) of the *Corporations Act*

1. Section 180(1) of the *Corporations Act* provides:

**180 Care and diligence - civil obligation only**

*Care and diligence - directors and other officers*

(1) A director or other officer of a corporation must exercise their powers and discharge their duties with the degree of care and diligence that a reasonable person would exercise if they:

(a) were a director or officer of a corporation in the corporation’s circumstances; and

(b) occupied the office held by, and had the same responsibilities within the corporation as, the director or officer.

*Business judgment rule*

(2) A director or other officer of a corporation who makes a business judgment is taken to meet the requirements of subsection (1), and their equivalent duties at common law and in equity, in respect of the judgment if they:

(a) make the judgment in good faith for a proper purpose; and

(b) do not have a material personal interest in the subject matter of the judgment; and

(c) inform themselves about the subject matter of the judgment to the extent they reasonably believe to be appropriate; and

(d) rationally believe that the judgment is in the best interests of the corporation.

The director’s or officer’s belief that the judgment is in the best interests of the corporation is a rational one unless the belief is one that no reasonable person in their position would hold.

(3) In this section:

***business judgment*** means any decision to take or not take action in respect of a matter relevant to the business operations of the corporation.

1. In *Australian Securities and Investments Commission v Cassimatis (No 8)* [2016] FCA 1023, I considered the principles concerning contravention of s 180(1) in detail. All counsel accepted the accuracy of the propositions at [486]-[487]. In those paragraphs I discussed the remarks of Ipp J in *Vrisakis v Australian Securities Commission* (1993) 9 WAR 395, 449-450 that the question whether a director has exercised a reasonable degree of care and diligence can only be answered by balancing the foreseeable risk of harm against the potential benefits that could reasonably have been expected to accrue to the company from the conduct in question. I explained that the reference to “balancing” by Ipp J should be understood as a reference to the well-known decision of Mason J in *Wyong Shire Council v Shirt* [1980] HCA 12; (1980) 146 CLR 40, 47-48:

[T]he tribunal of fact must first ask itself whether a reasonable man in the defendant’s position would have foreseen that his conduct involved a risk of injury to the plaintiff or to a class of persons including the plaintiff. If the answer be in the affirmative, it is then for the tribunal of fact to determine what a reasonable man would do by way of response to the risk. *The perception of the reasonable man’s response calls for a consideration of the magnitude of the risk and the degree of the probability of its occurrence, along with the expense, difficulty and inconvenience of taking alleviating action and any other conflicting responsibilities which the defendant may have. It is only when these matters are balanced out that the tribunal of fact can confidently assert what is the standard of response to be ascribed to the reasonable man placed in the defendant’s position.*

*The considerations to which I have referred indicate that a risk of injury which is remote in the sense that it is extremely unlikely to occur may nevertheless constitute a foreseeable risk. A risk which is not far-fetched or fanciful is real and therefore foreseeable. But, as we have seen, the existence of a foreseeable risk of injury does not in itself dispose of the question of breach of duty. The magnitude of the risk and its degree of probability remain to be considered with other relevant factors.*

(Emphasis added.)

1. As I explained in *Cassimatis*, this exercise is “forward looking” to what a reasonable person would have done, and the judgment of reasonableness is not amenable to exact calculation: quoting from *New South Wales v Fahy* [2007] HCA 20; (2007) 232 CLR 486, 491 [6] (Gleeson CJ), 505 [57] (Gummow and Hayne JJ).
2. The approach of Mason J in *Wyong Shire Council v Shirt* is well accepted. It has been iterated and reiterated by the High Court that, at the second stage of enquiry, the measure of the discharge of the duty is what a reasonable person would, in the circumstances, have done by way of response to a foreseeable risk: *Hackshaw v Shaw* [1984] HCA 84;(1984) 155 CLR 614, 662-663 (Deane J); *Australian Safeway Stores Pty Ltd v Zaluzna* [1987] HCA 7;(1987) 162 CLR 479, 488 (Mason, Wilson, Deane and Dawson JJ); and *Romeo v Conservation Commission of the Northern Territory* [1998] HCA 5; (1998) 192 CLR 431, 445 [21] (Brennan CJ).
3. However, senior counsel for ASIC submitted that it was not for ASIC to engage in a royal commission as to what could or could not have happened (ts 729). He maintained that ASIC did not need to prove what a prudent person shouldhave done in the circumstances. He submitted that it was enough to assert that a prudent person would *not* have approved the August 2012 Variation in the particular circumstances, adding that “it just comes back not so much to what somebody else [ie a reasonable director] would have done but what these people ought not to have done” (ts 731). That submission is contrary to considerable authority.
4. In *Romeo* the test was phrased by Toohey and Gummow JJ as follows (454 [50], quoting from *Nagle v Rottnest Island Authority* [1993] HCA 76;(1993) 177 CLR 423, 431 (Mason CJ, Deane, Dawson and Gaudron JJ)):

Whether there was a breach of the duty of care owed by the respondent to those who came onto the Reserve depended on “*the action that a reasonable person in the respondent’s situation would have taken* to guard against the foreseeable risk of injury which existed”.

(Emphasis added.)

1. In other words, in order to prove negligence it is necessary for an applicant to prove the action that *would have been taken* by a reasonable person. In *Graham Barclay Oysters Pty Ltd v Ryan* [2002] HCA 54; (2012) 211 CLR 540, 611-612 [192], Gummow and Hayne JJ said:

A duty of care that is formulated retrospectively as an obligation purely to avoid the particular act or omission said to have caused loss, or to avert the particular harm that in fact eventuated, is of its nature likely to obscure the proper inquiry as to breach. That inquiry involves identifying, with some precision, what a reasonable person in the position of the defendant would do by way of response to the reasonably foreseeable risk. As Isaacs A-CJ observed in 1924, “*[n]o conclusion of negligence can be arrived at until, first, the mind conceives affirmatively what should have been done”. The trial judge and the majority of the Full Court in the present case failed to identify with the necessary precision, by reference to considerations of the nature of those indicated in Wyong Shire Council, the reasonable response to the risk of harm that existed.* In so failing, their Honours fell into an error of law. There is no serious dispute as to the facts to which the law is to be applied. Thus, it is appropriate for this Court to resolve the matter. For the reasons that follow, the proper application of principle requires a conclusion different to that reached in the Federal Court.

(Emphasis added, footnotes omitted.)

1. There are many more authorities which emphasise this point in similar ways. In the High Court of Australia, these include *Vozza v Tooth & Co Limited* [1964] HCA 29; (1964) 112 CLR 316, 319 (Windeyer J); *Neill v NSW Fresh Food and Ice Pty Limited* [1963] HCA 4; (1963) 108 CLR 362, 364-365 (Dixon CJ), 369-370 (Taylor and Owen JJ); *Australian Iron & Steel Limited v Krstevski* [1973] HCA 42; (1973) 128 CLR 666, 668-670 (Barwick CJ and Menzies J); and *Nelson v John Lysaght (Australia) Limited* [1975] HCA 9; (1975) 132 CLR 201, 214-215 (Gibbs J).

## The process of drawing inferences and reaching conclusions

1. The parties made various submissions about techniques to draw inferences, including inferences against Mr Drake based on the fact that Mr Drake did not give or call evidence. It is necessary to explain why none of those matters affects my conclusions in this case.
2. First,ASIC relied on the operation of the rule in *Jones v Dunkel* [1959] HCA 8;(1959) 101 CLR 298. The rule does not generally apply to criminal proceedings. As Gaudron A-CJ, Gummow, Kirby and Hayne JJ said in *RPS v The Queen* [2000] HCA 3; (2000) 199 CLR 620, 633 [28], “not only is an accused person not bound to give evidence, it is for the prosecution to prove its case beyond reasonable doubt. The observations by the Court in *Jones v Dunkel* must not be applied in criminal cases without taking account of those considerations”. In *Mahmood v State of Western Australia* [2008] HCA 1; (2008) 232 CLR 397, 406 [27], Gleeson CJ, Gummow, Kirby, and Kiefel JJ said that where a witness for the defence was not called, “the question is not whether the jury may properly reach conclusions about issues of fact but whether, in the circumstances, they should entertain a reasonable doubt about the guilt of the accused”.
3. The jury question of whether an offence is proved beyond reasonable doubt is not an issue in civil penalty proceedings. But that does not mean that the rule in *Jones v Dunkel* applies automatically to civil penalty proceedings, which attract the same privilege as criminal proceedings: cf *Australian Securities and Investments Commission v Fortescue Metals Group Ltd (No 5)* (2009) 264 ALR 201, 221-224 [86]-[95] (Gilmour J). It is not necessary to decide the extent of its application. It suffices to proceed on the basis, assumed by the parties, that it does apply in these proceedings so conclusions of fact can more comfortably be drawn in the absence of Mr Drake as a witness. The reason I am content to proceed on this basis is because it does not alter any of the conclusions of fact which I reach.
4. Secondly, ASIC relied on *Weissensteiner v The Queen* [1993] HCA 65; (1993) 178 CLR 217, for the submission that it is easier for the tribunal of fact to draw inferences from circumstantial evidence against a party who must be able to give evidence on the topic of the circumstantial evidence but chooses not to do so. Again, there is no inference which I have drawn or failed to draw which I consider would be affected by Mr Drake’s failure to give evidence. Despite making substantial submissions about *Weissensteiner*, ASIC did not point to any particular inference which could be affected by this process of reasoning.
5. Thirdly, Mr Drake relied on *Briginshaw v Briginshaw* [1938] HCA 34; (1938) 60 CLR 336 to submit that the gravity of the allegations was such that the Court must obtain a high degree of satisfaction that a breach of trust arose and that the respondents contravened s 180(1) of the *Corporations Act*. Two points should be emphasised. The first is that it is well established that a reference to a “high degree of satisfaction” does not change the burden of proof which is the balance of probabilities. In broad terms the rule is really just that the more serious an allegation the more unlikely it might be that the conduct was committed by the respondent. The second point is that common law rules are not particularly helpful where statutory provisions such as s 140 of the *Evidence Act 1994* (Cth) apply. In reaching the conclusions which I do below, I take into account the nature of the cause of action, the nature of the subject matter of the proceeding and the gravity of the matters alleged (including that the proceedings are for civil penalties).

## Application of the legal principles

### Did Mr Drake “cause or permit” LMIM to approve the August 2012 Variation?

1. ASIC’s case against the remaining three respondent directors was that their acts which breached s 180(1) of the *Corporations Act* were “causing and/or permitting LMIM to approve the August 2012 Variation and agreeing to advance to Maddison Estate a further $100 million”. The conduct of Mr van der Hoven and Ms Mulder consisted of them voting in favour of the further loan variation at the 7 August 2012 meeting. Mr Drake also voted at the meeting, although his vote was not recorded in the minutes.
2. As I have explained, there is an obvious inference that Mr Drake spoke at the 7 August 2012 meeting in favour of the further loan variation and that Mr Drake voted for it at the 7 August 2012 meeting, although subsequently his vote was recorded in the minutes as having not been counted. As I explain below, these matters are sufficient to show that Mr Drake caused or permitted the August 2012 Variation.
3. However, in closing written submissions, ASIC sought to go further. ASIC submitted that Mr Drake had “influence over” Mr Fischer, Ms Mulder, and Mr van der Hoven. This was not pleaded, nor was it raised at any time prior to each of these persons giving evidence. The respondents did not have the opportunity to give evidence on the matter or to cross-examine Mr Fischer about it. It was not even put to Ms Mulder or Mr van der Hoven in cross-examination. It was too late for ASIC to raise this allegation in written closing submissions in reply.
4. In any event, I conclude that Mr Drake permitted LMIM to approve the August 2012 Variation. The issue concerning whether Mr Drake caused or permitted the variation is not a question of whether “but for” Mr Drake’s actions in speaking in favour and voting (although his vote was not subsequently counted), the variation would have been approved. If that were the test then no director who was in a majority of more than two could ever breach his or her duty under s 180(1) of the *Corporations Act* if other directors also voted in favour for independent reasons. It is enough if the act or omission is an exercise of powers or a discharge of duties by the director (or failure to do so). The inference which should be drawn in all the circumstances is that Mr Drake’s actions were a significant *contribution* to the decisionin the sense of the expression “causes or contributes”: see, for instance, the use of this expression in *Amaca Pty Ltd v Booth* [2011] HCA 53; (2011) 246 CLR 36, 62-63 [70] (Gummow, Hayne and Crennan JJ). Contribution is a different concept from causation where the latter is used in its best sense of a “but for” or necessary reason for an outcome. In the sense of contribution, Mr Drake exercised his powers to permit the August 2012 Variation.

### The August 2012 Variation approval had legal consequences

1. One of the most curious aspects of this case was the plea by ASIC concerning the date at which the August 2012 Variation took effect. ASIC pleaded the following at [123]-[124] of its statement of claim:

[123] On or about 1 July 2012 Trust Co as custodian for the MPF, entered into a deed of variation of the Loan Agreement with Maddison Estate (**July 2012 Deed of Variation**).

[124] The July 2012 Deed of Variation:

a. was executed by Trust Co at the direction of LMIM as trustee for the MPF, given in a letter from LMIM to Trust Co dated 29 October 2012;

b. was executed by the first respondent as director of Maddison Estate;

c. provided that the loan amount in the Loan Agreement was increased to $280 million;

d. provided for payment by Maddison Estate of a re-establishment fee of $9.8 million in consideration of the lender agreeing to the variation; and

e. was not considered or approved by the board of LMIM prior to execution.

1. At [151], ASIC then pleaded, as a circumstance of lack of care, diligence, and skill by LMIM and its directors, that “[t]he July 2012 Deed of Variation was entered into before the August 2012 Variation was approved”. The only reasonable construction of this plea was that there was a lack of care and diligence by the directors in allowing the deed to be entered into prior to their approval. A subsequent entry into a deed, say in October 2012, but dated at an earlier date, could hardly be evidence of lack of care in August 2012.
2. The curious consequence of this pleading is that if the 2012 deed of variation had entered into force *before* the August 2012 Variation decision, then that decision could have no legal consequences. No submission was made that the July 2012 deed of variation was entered into without authority. The effect, therefore, of the pleading was that Maddison Estate had binding legal rights for a loan as varied to $280 million *prior* to the August 2012 Variation decision.
3. Mr van der Hoven and Ms Mulder admitted these paragraphs in their defences. They also pleaded that, at all material times they had no knowledge of the July 2012 deed of variation.
4. Mr Drake (at [124] of his defence) did not admit “to the extent that it is impliedly alleged, that the July 2012 deed of variation included the handwritten date ‘1 July 2012’ at the time that [Mr Drake] executed it as a director of Maddison Estate”. He denied that the deed of variation was entered on 1 July 2012 “because of the letter referred to in subparagraph 124a of the Statement of Claim” ([123]).
5. In written closing submissions, Mr van der Hoven and Ms Mulder pointed out the obvious consequence which I have mentioned above. How, they submitted rhetorically, could there be a risk of legal action by unitholders arising from their August 2012 Variation decision when, without their knowledge, in the words of ASIC’s pleading, the deed “was entered into before the August 2012 Variation was approved”?
6. ASIC did not address this point in written closing submissions. In oral closing submissions, ASIC’s response was that its pleading could be construed to mean that the deed had been dated 1 July 2012 but only executed after 29 October 2012. This was said to be because of the plea at [124(a)] that the deed “was executed by Trust Co at the direction of LMIM as trustee for the MPF”. But that plea does not negate the pleas at [123] and [151] that the deed was entered into by the parties on 1 July 2012. It simply means that the deed was executed by a later direction after 29 October 2012.
7. I do not accept that any natural reading of ASIC’s pleading conveys that the deed was executed after 29 October 2012. However, in closing, ASIC made it plain that it wished to present its case on the basis that the deed had not been executed until October 2012. Although ASIC did not seek formally to amend its pleading, senior counsel for Ms Mulder and Mr van der Hoven did not suggest that they would have done anything differently if ASIC had properly pleaded a case that the deed was executed after 29 October 2012. Indeed, their case was that they knew nothing of this deed before August 2012. And senior counsel for Mr Drake accepted that the deed was post-dated.
8. For the reasons explained above, I conclude that the parties did not enter the deed prior to the MPF Credit Committee meeting on 7 August 2012. The approval by the MPF Credit Committee on that date, being a committee comprised of the directors of LMIM, had the practical, and foreseeable, consequence of entry into the deed of variation.

### The consequences pleaded by ASIC were unlikely

#### The general reasons for unlikelihood of legal action by unitholders

1. The adverse consequence which was pleaded by ASIC in [161] of its statement of claim was that the decision to approve the August 2012 Variation exposed LMIM “to a foreseeable risk of harm, namely civil proceedings by the unitholders in the MPF” because the approval “caused LMIM to commit a breach of trust against MPF”. I am prepared to proceed on the basis that this consequence of civil proceedings was foreseeable in the sense of not being far-fetched or fanciful. But, although foreseeable, I consider that as at 7 August 2012 it was quite an unlikely consequence.
2. I have already explained the two reasons why LMIM did not commit a breach of trust against the MPF. These are each a sufficient reason to dismiss the s 180(1) claims against each director. However, even if my conclusion on each of these matters were not correct, these two reasons are at least very strongly arguable. These reasons, together with others, militate against a likelihood of civil proceedings by the unitholders.
3. The unitholders in the MPF were wholesale, or sophisticated, investors. It can reasonably be assumed that they would not have commenced an action against LMIM for breach of trust without legal advice. The likelihood of a risk of civil proceedings by the unitholders in the MPF would therefore need to consider the following legal obstacles:
4. whether the unitholders had any reasonable prospect of proving that there was a breach of trust. I have concluded that the equitable duty and the duty under s 22 of the *Trusts Act* were excluded. Although the latter at least might have been considered to be reasonably arguable there is no doubt that it would be a significant obstacle to the unitholders;
5. whether the unitholders had any reasonable prospect of proving that there was any loss *caused* by a breach of trust. There was no evidence from which this conclusion could be reached in this case. ASIC did not prove that there was any loss caused by its pleaded breach of trust, even if the breach occurred. Proof of such causation would require a careful consideration by the unitholders of whether a prudent trustee would have taken the same decision to approve the August 2012 Variation either at the same time or later in circumstances in which omissions pleaded by ASIC had been taken, for instance if an independent feasibility report had been obtained;
6. whether recovery of any loss that was caused would be excluded by cl 18(1)(a) of the MPF Constitution. I have concluded that there would be strong prospects to conclude that such recovery was excluded. This would be another significant obstacle to the unitholders;
7. whether, under cl 18(1)(a) of the MPF Constitution, any liability of LMIM would *in any event* be limited to Scheme Property. There is a strong argument that this would limit liability to the extent of loss of Scheme Property by any decision of LMIM. In relation to the August 2012 Variation decision, the maximum Scheme Property lost from the decision could be $16.5 million. And LMIM might be entitled to an indemnity from any remaining Scheme Property for its liability for that loss; and
8. the extent of any recovery if a causal loss could be proved from a breach of trust. As I explain in detail below, the total *capital* loss that could have been caused by the August 2012 Variation decision was around $16.5 million with a small prospect of proving that a loss of opportunity of investing money elsewhere was recoverable and not too remote. ASIC did not lead any evidence concerning how many investors had invested in the MPF, nor how much any of them had invested. It is possible that the number of investors might have meant that proportionate recovery for each individual investor would be very small.
9. Even more fundamentally, ASIC’s case that there was a likelihood of legal action by unitholders depended heavily upon the absence of an independent feasibility report as a crucial circumstance. But an investor who obtained legal advice would likely have realised that the concept of an “independent feasibility report” employed by ASIC was very elastic. At the very least, the elasticity of this concept would make a finding of liability based on this circumstance unlikely.
10. Further, and perhaps most fundamentally, a legally advised investor would appreciate that all of the circumstances of LMIM needed to be considered in assessing whether an action for breach of trust could succeed. Undoubtedly, LMIM could have taken greater care and employed greater prudence when assessing on 7 August 2012 whether to approve the proposal for a further advance. But the test for a prudent person is not one of perfection, nor is it whether more prudence could have been taken than was exercised. Whether the appropriate prudence was taken in the circumstances, including the terms of the trust, required consideration of all of the following matters which militate against liability:
11. the sophisticated investors who invested money on trust after 1 November 2011 did so pursuant to an information memorandum on that date. That memorandum, in similar terms to earlier memoranda, explained that: (i) 90.75% of the fund was invested in mortgage securities including second ranked mortgages; (ii) the mortgage securities in which LMIM invested were in excess of $248 million; (iii) the largest loan was more than $142 million; and (iv) nearly 5% of the funds mortgage securities were in arrears. The information memoranda also said that the MPF had entered related party transactions directly or through joint ventures to ensure that yield was delivered as income only for tax purposes and that “[f]or this reason, the majority of the Fund’s transactions in respect of the Fund’s assets would be classified as related party transactions”. The terms of the investment were such that any sophisticated investor would reasonably have formed the view that there was substantial risk involved in the investment;
12. the value of the loan was already $190 million but Suncorp had a first mortgage to cover its $22 million debt, so the failure to approve the loan could potentially result in the loss of the entire $190 million asset. Indeed, ASIC itself submitted that “[t]he security position was such that the only prospect of recovery of the advance was the successful completion and sale of the development”. As I have explained, the exit strategy of the MPF was not to complete the entire development but to be bought out during the process such as after completion of Stage 1. But, at a higher level of generality, ASIC’s submission is accurate that realistic prospects for recovery of the advance probably depended upon the additional finance being available;
13. as I have explained, the cost of the variation, in the sense of actual funds which would leave the MPF, was $16.5 million. It was not $100 million;
14. ASIC relied upon an allegation of imprudence against a background of five previous increases in the limit of the loan, which increased the limit from an original investment of $40 million to $180 million in a period of four years without construction having even been commenced on the project. But ASIC never proved that any of those limits was ever intended to cover the entire project or even to cover the development until the time when LMIM intended to exit the project. Even the later variations (September 2011 and August 2012) were only expressed, respectively, to provide funding to the end of March 2012 and then the end of Stage 1 of the development;
15. an important distinction between earlier variations and the variation in August 2012 was that by late 2011 the project had begun to move apace with a dynamic and efficient new manager, Mr Barnett and there was a general expectation that the Gold Coast market prices would improve (ts 476, 483);
16. another important distinction was that, as Mr Williams said, the embellishments that had been added to the Maddison Estate development since 2011 were unique, and the start and end values were comparable to similar properties (ts 469, 473). Mr Williams’ evidence was reliable in this respect as he had reasonably extensive experience with the Gold Coast property market and had conducted independent research on this point;
17. WPIAS had considered a feasibility study in a presentation on 17 July 2012 which resulted in a gross realisation value of $1 billion, albeit at a very high level, including the escalation rates, and had expressed a preliminary view that the feasibility was “conservative”;
18. although some of the net present values in feasibility calculations were less than the amount of the loan *when fully drawn down,* there was no attempt to compare net present value calculations (which involved a very large discount rate) with the value of the loan when *drawn down*. In relation to the comparison of amounts at the same time, the net present value in the 17 July 2012 feasibility which had been presented to WPIAS had been $169 million which *appeared to be* less than the value of the loan. But, putting aside a large difficulty to which I refer in the conclusion to these reasons, this must also be understood in light of: (i) recoverability of the $169 million being dependent upon completion of the project which would not occur without the August 2012 Variation; (ii) a large discount rate being used for the net present value calculation which was conservative (ts 465); and (iii) the erroneous assumption by the parties that the value of the loan on 17 July 2012 was around $201 million (see, for instance, ASIC’s closing submissions at [469]-[470]). The assumption about the value of the loan was based upon a misunderstanding of retrospective loan accounts which, for instance, included amounts such as $9.8 million which could not have been a debt that arose until after both the 7 August 2012 MPF Credit Committee meeting *and* the execution of the 2012 deed of variation; and
19. shortly before the 7 August 2012 meeting there had been strongly positive news and radio publicity which had described the development in glowing terms including as a billion dollar project, potentially generating excitement in the public about the development.

#### ASIC’s alleged defects in process, especially the lack of an independent feasibility study

1. There is another major reason why, on ASIC’s case, the risk of civil proceedings was not large. This is that most of ASIC’s submissions concerning imprudence were focused upon defects in the *process* of the decision-making taken by LMIM. For instance, one of the principal circumstances relied upon by ASIC was that “there was no reliable independent verification of those feasibility models or independent feasibility models commissioned”. Another was that there were said to be “significant shortcomings with the feasibility models prepared by the development team, including the assumptions of future revenue which were derived by using inputs selected specifically to deliver a valuation (of anticipated future cashflows discounted to net present value) that accorded with an *a priori* view of what the anticipated gross revenue would be”.
2. There are real difficulties with all of ASIC’s allegations of defects in process. As for the allegation of “significant shortcomings” essentially involving reverse engineering of feasibility reports, I am satisfied that the 30 June 2012 feasibility presented to the 11 July 2012 meeting was a reverse engineered report. But this 30 June 2012 feasibility report, which was prepared in order to show what was necessary to achieve full recovery of the loan, was substantially different from the 25 July 2012 feasibility report which was relied upon at the 7 August 2012 meeting.
3. In the course of these reasons I have also addressed other defects in process alleged by ASIC. One of those was the number of variations and the allegation that LMIM’s track record in forecasting the limit of the loan required was “abysmal”. I have explained why I do not accept that submission. Another was the draft and final Ernst & Young reports. I have explained the vociferous dispute about those reports and their tender being simply for the fact that they existed rather than for the truth of their contents or opinions.
4. ASIC’s most significant reason for alleging a defective process leading to a decision should not have been taken (and presumably one of the alternative decisions – deferral or refusal – should have been taken) was because an independent feasibility report had not been obtained. ASIC accepted that it had not excluded the possibility that if an independent feasibility report had been obtained the report might have provided a basis for the August 2012 Variation to be approved. On that basis, it might have been said by ASIC that the alleviating action that should have been taken was to defer the decision until an independent feasibility report was obtained or to refuse the loan variation because of the absence of an independent feasibility report. Although ASIC did not engage with the alternatives, there is a significant problem with any submission that an alternative should have been chosen due to the absence of an independent feasibility report. This is the lack of clarity concerning what ASIC meant by an independent feasibility report.
5. ASIC’s statement of claim alleged that in approving the August 2012 Variation, “LMIM did not obtain an independent feasibility analysis of the anticipated future cashflows from the development” ([150]). ASIC alleged at [152] that a trustee, exercising its powers of investment with the degree of care, diligence and skill of a prudent person engaged in the business of acting as a trustee or investing money, would have obtained an independent feasibility analysis of the anticipated future cash flows from the development. Although the statement of claim was not clear on the point of whether the absence of an independent feasibility report was alleged to be sufficient to establish a breach by itself, senior counsel for ASIC explained early in the trial that ASIC did not allege that the absence of an independent feasibility report was *by itself* sufficient to establish a breach of trust (ts 89-90). However, senior counsel later accepted that it was a “crucial” circumstance (ts 648).
6. During the trial, ASIC’s experts took different approaches to what was meant by an independent feasibility report.
7. When Mr Woolley was asked what he meant by an independent feasibility report, he said that “you could have feasibility studies done by independent groups perhaps using the same software [Estate Master] or other software” (ts 544-545). He then confirmed that by this he meant something a developer might prepare to determine a discounted cash flow from a development by reference to costs and expected revenue inputs. This apparently treats an independent expert report simply as a report from an independent developer, even if the inputs of cost and expected revenue were provided internally. Mr Woolley’s evidence was that a report is independent “to the extent that it is external, but one of the measures of independence is the degree of revenue that you get off a client” (ts 628). As I have explained, I do not place any weight on any of Mr Woolley’s evidence.
8. A different approach was taken by Mr Bristow. He assumed that an independent feasibility report would require independent verification of all inputs. In cross-examination, Mr Bristow gave evidence that if he were able to find someone who was able to perform the task of performing an independent feasibility report with all of the inputs obtained externally, it would take quite a long time for that person to marshal the consultants for those inputs (ts 532-533). Those consultants would include property valuers, quantity surveyors, engineers, town planners, ecologists, and (he said) the list goes on. He estimated that it would take a couple of months to get the information from those consultants, but this would depend on each of the consultants.
9. The process of preparing a feasibility with each aspect of the information prepared afresh would involve the “long time” to identify numerous relevant consultants as well as, at least, “a couple of months” (dependent upon the consultants) but potentially much longer. As Mr Bristow said in his report, it would also involve the person preparing the feasibility developing “a deep understanding of the asset” involving not merely the cost and revenue inputs from the consultants but also numerous matters including the time scale for the approval stage of the project, construction and selling period, the cost and availability of finance over the period, the target profit margin and others.
10. On the 10th day of trial, after the close of ASIC’s case, I asked ASIC’s counsel to explain precisely what ASIC meant by an independent feasibility report (ts 643). I repeated the question on the 11th day of trial (ts 648).
11. In written closing submissions, ASIC submitted at [56] that there was “nothing complicated about the concept of an independent feasibility”. ASIC submitted that it “is a valuation of the development based on anticipated future cashflows, discounted to the net present value, prepared by an advisor external to LMIM on behalf of the lender (and not the borrower) from the lender’s perspective”. ASIC submitted at [314] that “What was absent was a valuation of the development (albeit one based on the anticipated future cashflows discounted to the net present value) prepared by an adviser external to LMIM on behalf of the lender (and not the borrower) from the lender’s perspective”. ASIC submitted that the feasibility report was not independent because the staff who prepared the models (initially Ms Scott, then subsequently Mr King and Mr Barnett) were members of the PAM team in LMA and responsible for the development (on behalf of the borrower, Maddison Estate) under the LMA Development Management Agreement.
12. To a large extent this definition of an independent feasibility report relied upon ASIC’s expert, Mr Woolley, whose evidence ASIC properly abandoned reliance upon. Curiously, as I explain below, this definition is contrary to the evidence of Mr Bristow whose evidence ASIC *did* rely upon. However, putting the lack of an evidential foundation for ASIC’s notion of an “independent feasibility report” to one side, the definition raises considerable questions and its vagueness removes any real utility in it as a concept. What is meant by an adviser “external to LMIM”? What is meant by “the lender’s [LMIM’s] perspective”? To what extent must the adviser who is “external to LMIM” rely upon information which is external to LMIM?
13. The PAM team was employed by LMA and, in that formal sense, was external to LMIM. It was unclear whether ASIC alleged that the PAM team was “external to LMIM”. However, ASIC’s position in submissions became that the PAM team, even if external, was conflicted by its concern with the interests of the borrower, Maddison Estate.
14. Putting to one side whether this allegation had been pleaded or raised before closing submissions, ASIC is correct that the feasibility report prepared by the PAM team was prepared in its capacity as the development manager for the borrower. Ms Mulder accepted in cross-examination that the feasibilities prepared by the PAM team were prepared by it for LMA as the manager of the project under the Development Management Agreement (acting for the borrower, Maddison Estate) (ts 655). But although LMA was acting for Maddison Estate as borrower, LMIM and Maddison Estate did not stand in the usual opposed positions of borrower and lender. As I have explained, the interest rate for the loan was set at a rate to ensure that the profit from the development was paid to LMIM and that Maddison Estate made no profit from the development. ASIC did not explain how any real or potential conflict could arise between the interests of the lender (LMIM) and the interests of the borrower (Maddison Estate) in a scheme where the purpose of the borrower, as a special purpose vehicle, was not to make any profit. It remained unclear at the conclusion of ASIC’s submissions whether, in circumstances in which the PAM team’s interests were aligned with those of LMIM (as lender), ASIC would accept that the PAM team’s work would qualify as an independent feasibility.
15. It also remained unclear whether ASIC’s case required an independent feasibility report to be produced by a person external to LMIM (and acting from LMIM’s perspective) using only inputs provided from external parties. Prior to oral closing submissions, my associate emailed the parties with a list of questions to be addressed in oral closing submissions. One of those questions (question 4) included the following:

Were the consultants engaged by LMIM to provide information on council fees, consultants’ fees and construction costs estimates persons who were “independent”? Is it ASIC’s case that an independent feasibility report required a determination independent of LMIM of each and every input into the feasibility? If not, which inputs should be provided?

1. ASIC’s reply, initially in writing, was that it “does not posit, as part of its case, any precise formula as to what in the way of an independent feasibility might have gone to negate what was otherwise a failure to exercise due care”. ASIC said that an independent feasibility need not require a determination, independent of LMIM, of each and every input into the feasibility. ASIC submitted that too much focus on the various inputs was liable to distract from a recognition that the purpose of such a feasibility is to value the development by assessing the present value of the anticipated future cash flows.
2. This approach by ASIC may have been adopted to avoid the inevitable problem which would have arisen from a submission that an “independent feasibility report” required independent validation of all inputs. That problem would be that the process of identifying the various experts to provide independent inputs, obtaining those inputs, and developing the “deep understanding” necessary for an independent feasibility report would require deferring the 7 August 2012 decision for potentially a very lengthy time. As I explain later, that might have been assessed to have consequences which might have been worse than if LMIM had approved the loan.
3. Curiously, this approach by ASIC appeared to contradict the evidence of Mr Bristow who had said that “validation of *all* inputs is paramount, not the choice of marketing tool” (emphasis added). Mr Bristow continued, saying that “[a]s with any valuation exercise, the aim is always to reconcile the result with market data”.
4. Perhaps due to this contradiction, in ASIC’s written submissions it submitted that a feasibility report would only be “independent” if the validation of the revenue inputs and the reconciliation of the result with market data were undertaken by an advisor external to LMIM. In closing submissions, senior counsel for ASIC denied that this meant that all inputs should be externally validated (ts 791-794). Initially, senior counsel submitted that it was no part of ASIC’s case to say “This is precisely what you should have done.” However, given that ASIC had specifically pleaded and presented its case as involving a “crucial” factor of the absence of an independent feasibility report, it could hardly be sufficient for it to take the position that it was no part of its case to explain precisely the nature of an independent feasibility report. The following exchange then occurred at the very conclusion of the trial, in submissions in reply after I asked senior counsel for ASIC what it was that prevented a feasibility study from being an *independent* feasibility study if some inputs could be internally produced (ts 792-793):

MR DAVIS: Yes. So there’s some – obviously, there’s some external inputs. But in the end, this thing was put together in-house with no proper validation. Now, we don’t – we - - -

HIS HONOUR: … but what does “validation of the revenue inputs” mean?

…

MR DAVIS: Yes. The revenue inputs includes such things as the escalation rates, and the future value. Now, none of that is tested.

…

HIS HONOUR: Mr Bristow, the expert, is saying validation of all inputs is paramount.

MR DAVIS: Yes.

HIS HONOUR: But you’re not saying that?

MR DAVIS: We’re at least saying that the assessment of the escalation rates and the assessment of value should have been justified.

1. Ultimately, therefore, although only in closing oral submissions in reply, ASIC’s case became that the failure to obtain an independent feasibility report by LMIM was a failure to obtain verification of an internal feasibility report from an external adviser on behalf of LMIM, at least by reference to the chosen escalation rates and the assessments of future value, as discounted to net present value.
2. Unfortunately, even this approach invited more questions than it answered. I have already referred to the uncertainty concerning whether LMA could be categorised as an external adviser acting in the interests of LMIM, and whether this would be sufficient. In addition, if some, or even many, inputs for the calculation of future value are provided from external parties, then will this be sufficient for the assessment of future value to be independent? If not, then which factors in the assessment of future value would prevent the assessment of the feasibility from being independent? If the assessment of future value is independent then will it no longer be independent if an internal discount rate is used? And, if the exercise of providing an independent feasibility report is not to be an exercise in pure formalism, then how will the independent assessing party develop a “deep understanding” of the asset independently of LMIM?
3. Even putting all these points to one side, there is a large question of why, at least in relation to Ms Mulder and Mr van der Hoven, it was not reasonable for them to assume that WPIAS had considered the appropriate escalation rate. I consider that it was reasonable for them to assume this. Although the assessment that WPIAS could reasonably be assumed to have undertaken was not that of an audit of Maddison Estate, the evidence was that the consideration of an appropriate escalation rate involves speculation and is not scientific or precise. And WPIAS had a strong familiarity with the Maddison Estate development, reasonably extensive knowledge of the Gold Coast property market (ts 469) and had considered the loan to Maddison Estate in the course of the 2011 audit. The assumption by Ms Mulder and Mr van der Hoven that WPIAS would consider the escalation rates was a reasonable one, even though they would have been aware that WPIAS was not conducting a full audit of the Maddison Estate development and had not been informed that its conclusions would be relied upon in varying the limit to the loan.

#### Conclusion about ASIC’s alleged defects in process

1. In any event, even if an investor could prove such a case of defects in the process taken by LMIM before approving the August 2012 Variation, and establish imprudence by LMIM, these defects in process would not permit any financial recovery. The decision was an authorised one. A decision which is defective in the process it was reached might nevertheless have been made *in any event* even if the process had not been defective. Indeed, there are strong reasons to believe that the same decision might have been made even if the decision had been deferred to permit a more thorough process of review. As I have explained, the high level assessment by WPIAS, which included stress testing, concluded that the feasibility report was “conservative”. To the extent that an independent feasibility report might be obtained, and to the extent that such a concept is meaningful, many of the inputs in the feasibility report were independently obtained in any event, and variables such as escalation rates would require familiarity with the evolution of the development plan, which information could only realistically be provided by LMIM. This fact, coupled with the detail of the assessment conducted by WPIAS in the 2012 audit which resulted in the conclusion that the loan was not impaired, suggests a very real likelihood that an independent feasibility report (however defined) would have reached a similar conclusion to the 25 July 2012 feasibility report.

### The magnitude of harm

1. Even if it were assumed that there were any significant likelihood that sophisticated investors would bring legal action as a result of the approval of the August 2012 Variation, the magnitude of harm is, emphatically, *not* the prospect or chance of LMIM being liable for $100 million as ASIC submitted. As I have explained above, $100 million was not put at risk. To reiterate, part of the increase was simply to cover an amount which was *already* owed; and the vast majority of the increase would not involve any payment from the MPF but was concerned with capitalised interest and a loan re-establishment fee which would not otherwise be received. There would be only $16.5 million of outflows (of which $1.5 million in Suncorp interest would probably have accrued prior to Suncorp fully recovering its loan and redeeming the mortgage).
2. Hence, putting to one side the unlikelihood of any legal action, the magnitude of any harm is therefore the unlikely *prospect* that legal action would be successful and allow recovery of amounts in the region of $15 million to $16.5 million and legal costs. As we will see below, although ASIC resolutely declined to make any submissions concerning the burden of alleviating action, the only alleviating action might give rise to a far greater likelihood of harm and of a far greater magnitude.

### The burden of alleviating action

1. Although I do not consider that, as at 7 August 2012, there was a substantial likelihood of civil action by investors based on the matters raised in this trial by ASIC, I have proceeded on the basis that a civil proceeding was not far-fetched or fanciful and that there was some harm that might have resulted; that is, that there was a more than negligible, although unlikely, prospect of success.
2. A fundamental obstacle for ASIC’s case is the burden of alleviating precautions. What else could a reasonable director, with each respondent director’s responsibility and in LMIM’s circumstances, have done to avoid this risk of harm? This inevitable obstacle arises in part due to my rejection of Mr Woolley’s evidence.
3. As I have explained, ASIC’s case was that the respondent directors breached their duties because they caused or permitted LMIM to commit a breach of trust, and exposed LMIM to a foreseeable risk of harm, namely civil proceedings by unitholders in the MPF. The act which constituted this breach of trust and exposure to a foreseeable risk of harm was pleaded as “approving the August 2012 Variation and agreeing to advance to Maddison Estate a further $100 million” in all the pleaded circumstances. An essential question for the determination of whether s 180(1) of the *Corporations Act* has been contravened is what a reasonable person, with the position and responsibility of each respondent, in LMIM’s circumstances would have done if he or she had acted with due care and diligence. There were only three possibilities in relation to the August 2012 Variation decision. The person could: (i) refuse the loan variation; (ii) defer the decision of whether to make a loan variation on the same or different terms; or (iii) approve the loan variation.
4. On numerous occasions, ASIC answered this question simply by saying a reasonable director “would not have approved” the loan. By definition, ASIC’s case must have been that a reasonable director would have either refused the loan variation or deferred the decision. However, there may have been powerful reasons why a reasonable director with the responsibilities of each respondent would not have taken either of those courses of action in the circumstances. This was a fundamental problem with ASIC’s case.
5. As for whether a reasonable director would have deferred the decision, how long would a reasonable director expect would be required for deferral of the decision? What steps would need to be taken before a concluded view could be reached? Would an alternative proposal have been more attractive? Would a reasonable director have assessed that deferring the decision would cause Suncorp to foreclose? If so, would a reasonable director have considered that deferral, causing foreclosure by Suncorp as the first mortgagee, would cause the loan, with a value of approximately $191 million, to be entirely irrecoverable?
6. As for whether a reasonable director would simply have refused the loan variation, would a reasonable director have considered that this would necessarily bring the project to an end? Would a reasonable director have considered that refusal would cause Suncorp to foreclose and sell the land? If so, would a reasonable director have considered that foreclosure by Suncorp as the first mortgagee would cause the loan, with a value of approximately $191 million, to be entirely irrecoverable?
7. As I explain below, ASIC bore the onus of proof on these matters. These gaps in ASIC’s case, by themselves, are therefore a sufficient basis to dismiss the action for breach of s 180(1) of the *Corporations Act*. However, in deference to the detailed submissions by the parties, I explain below why I would dismiss the claims of contraventions of s 180(1) in any event.

#### ASIC did not discharge its onus of proof on this issue

1. In written submissions following oral closing addresses, ASIC changed tack. ASIC accepted that it bore the ultimate burden of proving that the risk could have been avoided by some reasonably practicable alternative but submitted that “it is not incumbent upon ASIC to plead or prove every possible permutation involved in that alternative”. It is unclear what this submission means. There were only two alternatives to the decision to approve the August 2012 Variation. One alternative was to defer the decision. The other alternative was to refuse the loan variation. ASIC did not lead anysubstantial evidence or make any submissions about the consequences of adopting those alternatives. The submission that ASIC was not required to prove “every possible permutation” must, therefore, have been a submission that ASIC had no onus to show that these alternatives were reasonably practicable. The failure of ASIC to lead any substantial evidence or make any submissions directed to what alternative a reasonable person would have taken is fatal to ASIC’s case if it bears that onus of proof. For the reasons below, that onus was borne by ASIC.
2. ASIC’s submission that it was not required to establish what a reasonable person would have done or the consequences of that alternative decision requires careful consideration of the authority to which the parties referred in detail: the decision of the High Court in *Swain v Waverley Municipal Council* [2005] HCA 4; (2005) 220 CLR 517.
3. In *Swain,* Mr Swain brought a claim against the Waverley Municipal Council for negligence. He alleged that he had entered the water on a calm day between the flags at Bondi Beach. He said that he had attempted to dive through a wave when he hit a hidden sandbar. He suffered spinal injury and was rendered a quadriplegic. The main issue of contest before the trial judge and jury was whether he was swimming between the flags. In the closing address for the Council, the jury were invited to consider whether the flags could have been placed elsewhere. But no witness had given evidence on that point. The jury found the Council liable. The New South Wales Court of Appeal overturned the verdict. A majority of the Court of Appeal held that (i) it was normal, if not inevitable, that there would be a sandbar in the swimming area between the flags, and (ii) moving the flags would not have protected Mr Swain from a sandbar and a channel.
4. The Council argued that it was for Mr Swain to prove that the risk of injury from diving was preventable but that Mr Swain had adduced no evidence on the point. A majority of the court (Gleeson CJ, Gummow and Kirby JJ; McHugh and Heydon JJ dissenting) held that it was reasonably open to the jury to make a finding of negligence. As Gummow J explained, the issue before the High Court was narrow: it was whether the Court of Appeal applied settled principle in setting aside the jury’s verdict (556 [110]).
5. In the majority, Gleeson CJ observed that there was an absence of any evidence that moving the flags would have made a difference, and that the jurors might reasonably have thought that “it was up to the [Council], rather than [Mr Swain], to tell them what difficulty there would have been about moving the flags” (525 [17]).
6. Also in the majority, Gummow J held that “[w]hile the plaintiff bears the ultimate burden of proving that his or her injuries could have been avoided by some reasonably practicable alternative course of conduct available to the defendant, in some cases, the evidentiary burden which has come to rest upon the defendant may prove decisive of the outcome” (566 [153]). He relied upon the remarks of Gibbs J in *Nelson v John Lysaght* (214-215), concerning a circumstance where a defendant had adopted a new installation and must have had full knowledge of the nature, cost, and practical consequences. Gibbs J said that in these circumstances, if the defendant gave no evidence, and the defendant’s counsel asked no questions, the jury could infer that the new installation’s advantages were not outweighed by disadvantages. Applying this to *Swain,* Gummow J concluded that the Council carried at least an evidentiary onus of showing that there was no reasonably practicable alternative course (567 [155]). The failure of the Council to lead evidence or ask questions about the placement of the flags permitted the jury to infer that the Council could have moved the flags.
7. Also in the majority, Kirby J held that (586 [225]):

the Council, which called Mr Nightingale to give evidence, failed to ask him why, on the day of the appellant's injury, the flags had not been shifted. By inference, he could have answered that question. It is true, that the appellant, as the plaintiff in the action, bore the legal onus throughout the trial of adducing evidence sufficient to discharge his burden of proof. However, in the context of the trial, it was unreasonable to expect the appellant, on the blind, to have asked Mr Nightingale such a question. It was for the jury to draw inferences from the facts proved at the trial. Inferences (representing something more than mere conjecture) may be drawn by a jury from the omission of a party with the interest to do so to ask such an obvious question. The Council had the interest to ask the question.

(Footnotes omitted.)

1. There were dissents from McHugh and Heydon JJ. McHugh J held that there was no evidence from which the jury could have concluded that there was a reasonably practicable means of avoiding that risk. As McHugh J explained, Mr Swain had failed to tender any evidence that relocating the flags would not only have eliminated the risk of *his* injury but would also not have exposed himself or other swimmers to similar or other risks (526 [22]). McHugh J said that (534 [40], 535-356 [44]):

The plaintiff bears the legal and evidentiary burden of establishing a prima facie case of negligence. *To prove negligence, the plaintiff must be able to point to a reasonably practicable precaution or alternative course of conduct that could have avoided, or reduced the consequences of, the injury to the plaintiff.* The plaintiff does not establish a prima facie case simply by asserting that there “must be” a practicable alternative, and that it is for the defendant to provide evidence that no such alternative exists. The plaintiff does not prove a case of negligence, for example, by proving the existence of the risk and then alleging that the defendant took no precautions to protect the plaintiff against that risk.

…

In some cases, common knowledge or common sense is all that is required to prove a reasonably practicable alternative. In other words, the plaintiff may be able to discharge the evidentiary onus of establishing a practicable alternative without the benefit of technical or expert evidence. In *Maloney v Commissioner for Railways*, Barwick CJ said that evidence of the practicability of the proposed alternative course or safeguard “is essential except to the extent [that it is] within the common knowledge of the ordinary man.” Similarly, in *Tressider v Austral Stevedoring and Lighterage Co Pty Ltd*, the New South Wales Court of Appeal said that in some cases:

“[N]o more than common knowledge or common sense is necessary to enable a judge or jury to perceive the existence of a real risk of injury and to permit the tribunal of fact to say what reasonable and appropriate precautions might appropriately be taken to avoid it.”

(Emphasis added.) (Footnotes omitted.)

1. Heydon J agreed with McHugh J that there was no evidence from which it could be concluded that there was a reasonably practicable means of avoiding the risk of the injury (589 [236]).
2. The effect of the decision in *Swain* is that at least four justices (McHugh, Gummow, Kirby, and Heydon JJ) reiterated the long standing position that it is the applicant who generally bears the onus of proof to show the existence of a reasonably practicable alternative. However, in the particular circumstances of the case, where the Council had full knowledge of the nature, cost, and practical consequences of the alternatives, a majority held that the Council nevertheless was liable either because it had an evidentiary onus to lead evidence, or because inferences were drawn from its failure to lead that evidence.
3. Four months after *Swain,* the High Court delivered reasons for decision in *Roman Catholic Church Trustees for the Diocese of Canberra and Goulburn v Hadba* [2005] HCA 31; (2005) 221 CLR 161. In that case, an eight year old girl, Miss Hadba, was pulled off a flying fox in the school playground. The girl was seriously injured. The children who pulled Miss Hadba off the flying fox was acting in breach of the school’s “hands off” policy. The school had taken numerous precautions against an event like this occurring. Miss Hadba did not prove that there was a practical alternative for the school to have taken which was free from the risk which eventuated. A majority of the High Court held that the school should not have been held liable. At 167 [13], Gleeson CJ, Hayne, Callinan and Heydon JJ said:

it was open to [Miss Hadba] to establish a breach of the [school’s] duty of care. But, if she were to do this, *it was incumbent on her to demonstrate that there was some system of supervision which was an alternative to that which the school was using at the time of the accident, which was free of the risk of which the plaintiff complains and which was available – not in a general or theoretical way, but in a practical sense.*

(Emphasis added.)

1. Like *Hadba,* this case is not one in which the respondent directors bore any evidentiary or substantive onus to prove what alternative courses they might have taken. Indeed, their case was that there was no reasonable alternative. Nor is this a case in which an inference should be drawn against the respondents for their failure to lead evidence about the consequences of a decision by a prudent trustee in LMIM’s position (i) refusing the August 2012 Variation application, or (ii) deferring the August 2012 Variation decision. None of these matters was uniquely in the respondents’ knowledge. Each of these matters would probably have required expert evidence on matters such as (i) the consequences of refusing the application, or (ii) in relation to deferral, the reason why deferral should have been sought, what any alternative deferred proposal might have been, and, if the reason for deferral was to obtain an independent feasibility report, the time it would have taken to obtain that report and the cost of it and the consequences in the meantime. In the language of the joint judgment in *Hadba,* it was incumbent upon ASIC to demonstrate that there was an alternative decision which was free of the risk of which ASIC complains. The failure of ASIC to examine any alternatives is fatal to its case.

#### The burden of alleviating action and lack of clarity about an “independent feasibility report”

1. In any event, and even if the onus of proof were borne by the respondents, on the evidence before the Court I am satisfied that the burden or cost of alternative or alleviating measures was greater than the cost of the decision which was taken. In the circumstances of LMIM that existed at 7 August 2012, therefore, the choice made by the respondents, in their positions of responsibility, was a reasonable one even if the process by which the decision was taken was not perfect. This conclusion says nothing about the conduct of the respondents or LMIM in the decisions that they took prior to 7 August 2012. There was no allegation of breach of duty in relation to any of those earlier decisions and it is not necessary to address any of them.
2. To reiterate, on 7 August 2012 there were two possible alternative “alleviating” courses that could have been taken: the decision could have been deferred for consideration of the same proposal or a proposal with different terms, or the 2012 Loan Variation could have been refused.
3. As for the first consequence, deferral, the core of ASIC’s case was that a reason why deferral was reasonable was because of the lack of an “independent feasibility report” (whatever that may have been). The feasibility report which was considered at the 7 August 2012 MPF Credit Committee meeting involved many, many pages in 10 point font. Depending on the extent to which this report needed to be independently prepared, the time period could easily have taken months. ASIC did not lead any evidence, nor make any submissions, about the time period that would have been required or the consequences of a lengthy delay. Even without evidence, an inference which might be drawn is that any substantial deferral of the decision would bring the development to an end. Suncorp would foreclose and sell the land. There would be a real prospect that the MPF would recover little or nothing.
4. Another matter which ASIC did not address is the speculative nature of key aspects of feasibility reports, whether independent or not, such as escalation rates and discount rates. What purpose would be served by deferring a decision, potentially for a substantial period simply to have an independent speculation rather than speculation by the directors? Mr Williams, the independent auditor from WPIAS who was the most reliable of the experts called even though he was not called as an expert, said that before any sales of a development actually begin, any feasibility is “very much only an estimate”. He said, and again I accept, that a “much more accurate indication of the value of a development could be ascertained once the project entered into the presale stage”.
5. In summary then, the consequences of deferral would be a potentially lengthy period (depending on what was required for an “independent feasibility report”) in order for an independent company to familiarise itself with the development, confirm many figures which had been obtained independently anyway, and to provide estimates such as escalation rates and discount rates which would, in any event, involve uncertainty and speculation.
6. On the other hand, on the evidence before the Court, there would have been a very real prospect that Suncorp would foreclose and sell the land to recover its loan if there were a significant period of default. The loan from LMIM already exceeded the limit by $10 million. A deferral of a decision to further extend the limit would not have permitted any repayments to Suncorp. Suncorp had received a negative report from Ernst & Young. Suncorp wanted to exit the market from property development. It had been trying to recover this loan since mid-2010. It had a preliminary valuation of between $35 million to $40 million which would allow it to recover its loan. Mr Kop from Suncorp had told Mr Tickner prior to May 2012 that Suncorp would not fund any construction at the Maddison Estate site, so if LMIM was unable to refinance the Maddison Estate loan or unable to fund any proposed development then the Maddison Estate development would not proceed (ts 200).
7. On the evidence before the Court there was a very significant prospect that the deferral of the decision for any substantial period of time would cause the loss of most or all of the $191 million asset for the investors. There would be a real prospect of civil action by investors if *that* decision were taken on 7 August 2012. And the magnitude of the claim by investors based on *that* decision would plainly be far greater than $16.5 million.
8. The other alternative course for the respondents to have taken on 7 August 2012 was for them to cause LMIM to refuse the loan variation for the further advance. That would have been extremely likely to bring the development to an end. Again, the end of the development would have lost most or all of the $191 million value of the investment. And, again, there would have been a real prospect of civil action by investors if a refusaldecision were taken on 7 August 2012, with the magnitude of the claim by investors far greater than $16.5 million.
9. In summary, on the limited evidence before the Court, and the limited extent to which the consequences of the alternatives were explored, the consequences of the two alternatives which were open to the respondent directors at the 7 August 2012 meeting of the MPF Credit Committee were likely to be more deleterious for LMIM, as assessed at that date without hindsight. That is another reason why ASIC’s case based on s 180(1) of the *Corporations Act* must fail.

## ASIC’s submission that Mr van der Hoven and Ms Mulder admitted impropriety

1. In closing submissions, ASIC submitted that “each of [Ms] Mulder and [Mr] van der Hoven admitted that it would have been improper to vote in favour of the August 2012 variation unless there was independent verification of the feasibility.” ASIC submitted that this was “effectively an admission of ASIC’s case”. This submission cannot be accepted for two independent reasons.
2. First, a finding of breach of s 180 of the *Corporations Act* is a question of law. The remarks by each of Ms Mulder and Mr van der Hoven about the propriety of an independent auditor were not an attempt to express any conclusion on this question of law. To do so they would have needed to undertake a legal assessment of each of the integers discussed above. And even if they had done so, that legal assessment is not one that can be made by a witness. Of course, the allegation of breach of s 180(1) could have been formally admitted in pleadings (which it was not).
3. Secondly, ASIC’s submission misconstrued the evidence of Ms Mulder and Mr van der Hoven. One reason why ASIC’s submission involved a misconstruction of their evidence was because Ms Mulder and Mr van der Hoven were plainly not accepting or adopting ASIC’s definition of an “independent feasibility report”. It was a curious submission that they were. They had denied ASIC’s case on this point in their pleading. And as I have explained, it was not even clear what ASIC meant by an independent feasibility report.
4. In the passages in cross-examination relied upon by ASIC, Ms Mulder (ts 657-658, 665, 673) and Mr van der Hoven (ts 680, 683) both said that they had not intended to approve the application to vary the loan unless WPIAS looked at the feasibility and was comfortable with it. Ms Mulder said that “the auditor would be testing certain aspects of the feasibility” and that she wanted confirmation from WPIAS “looking at it and being comfortable with it and having audited the fund previously” (ts 657). She confirmed that she expected that the auditor would “look at” the model drivers, assumptions, escalation, and pricing. Plainly, the confirmation she was describing was no more than what she had understood to have occurred. In other words, Ms Mulder said that she would not have subjectively approved the loan variation unless WPIAS had reviewed and approved the assumptions. It did that on 17 July 2012. She said that she was relying on “*that* check by the auditor” (ts 658). She later reiterated that although she did not have a recollection of all matters that were discussed at the meeting she “was comfortable with what had been discussed in relation to the feasibility” (ts 667). She said this was after WPIAS looked “at the escalation rates and sales pricing in that feasibility presented to them” (ts 673). Similarly, Mr van der Hoven accepted that he would not approve the feasibility unless WPIAS “looked at the feasibility and expressed their comfort with it” (ts 680). That was exactly what WPIAS did. Although Mr van der Hoven was not present at the 17 July 2012 meeting with WPIAS, as Mr van der Hoven explained he understood that WPIAS was “asked for the auditor’s opinion on the veracity of the assumptions made in the feasibility and specifically the escalation rates” (ts 685).
5. ASIC also submitted that I should reject Mr van der Hoven’s and Ms Mulder’s evidence about their subjective belief of the purpose of WPIAS’ engagement. ASIC submitted that the vague detail and the lack of recollection that each had concerning crucial meetings stood in stark contrast to their recollection concerning matters related to the audit to be performed by WPIAS. For instance, ASIC submitted that Mr van der Hoven could not have had a clear recollection of discussing with Mr Fischer and Ms Mulder the need for the auditors to look at the feasibility model for Maddison Estate before he would approve the loan. I do not accept that submission. As I have explained, I was satisfied that both Mr van der Hoven and Ms Mulder were honest witnesses whose evidence was reliable, to the extent of their recollection. Even more fundamentally, the issue concerning escalation rates had been the subject of very heated debate. It is unsurprising that this matter generally, and the need for confirmation from an independent auditor, was one of the key matters recalled by each of Mr van der Hoven and Ms Mulder.
6. ASIC submitted that an answer given by Ms Mulder in re-examination demonstrates that her evidence was contrived. In re-examination, Ms Mulder had been asked what she meant by “an auditor signing off”. She replied that she meant that she understood it to be “an independent verification of the management decision we were making” (ts 676). Senior counsel then asked her “an independent decision about what?” After an objection by senior counsel for ASIC was dismissed she replied “[t]he aspects of that feasibility that were the subject of dissension in various meetings such as the escalation rates and the sales pricing” (ts 677).
7. I do not accept that Ms Mulder’s answer was contrived. Throughout her evidence she strove to give honest answers to the best of her recollection and sought genuinely, and politely, to assist the Court and each counsel who examined or cross-examined her. As for Ms Mulder’s allegedly contrived answer, her initial answer to what she meant by an auditor “signing off” was unclear. It was a shorthand answer given at the conclusion of a substantial cross-examination and re-examination. What did she mean by the “management decision” which was being verified? Was it just confirmation that the result was reasonable? Was it confirmation that all of the inputs were reasonable? Was it confirmation that the assumptions were reasonable? Her further answer clarified this in terms which, even apart from her demeanour which assists my conclusion, were wholly consistent with her earlier evidence and, in the circumstances of the case, entirely reliable.

# ALLEGED BREACHES OF SECTIONS 181(1) AND 182(1) OF THE *CORPORATIONS ACT* BY MR DRAKE

## The terms of s 181(1) and s 182(1) of the *Corporations Act*

1. Section 181(1) of the *Corporations Act* provides as follows:

*Good faith - directors and other officers*

(1) A director or other officer of a corporation must exercise their powers and discharge their duties:

(a) in good faith in the best interests of the corporation; and

(b) for a proper purpose.

1. A person who is involved in a contravention of subsection (1) contravenes this subsection.
2. Section 182(1) of the *Corporations Act* provides:

*Use of position - directors, other officers and employees*

(1) A director, secretary, other officer or employee of a corporation must not improperly use their position to:

(a) gain an advantage for themselves or someone else; or

(b) cause detriment to the corporation.

(2) A person who is involved in a contravention of subsection (1) contravenes this subsection.

## The two core aspects of ASIC’s s 181 and s 182 claims

1. The issues in dispute in relation to both s 181(1)(b) and s 182(1)(a) concerned ASIC’s plea that Mr Drake caused or permitted LMIM to approve the August 2012 Variation:
2. in a manner which caused LMIM to commit a breach of trust against MPF; and
3. not in the best interests of the company but for an improper purpose.
4. The pleaded improper purpose was that Mr Drake approved the August 2012 Variation “for the purpose of maximising the cashflow available to LMA as trustee for the [LMA] Trust to fund the loans to [himself]”.
5. Neither of the elements (1) or (2) of ASIC’s claim is established.
6. I have already explained why (1) was not established, that is why no breach of trust was committed by LMIM. The section which follows explains why ASIC did not prove that Mr Drake exercised his powers *for* an improper purpose or used his position *to* gain the pleaded advantage. The words “for” and “to” require a causal or connecting link.

## Legal principles concerning improper purpose

1. The concept of “impropriety” was considered in *Doyle v Australian Securities and* *Investments Commission* [2005] HCA 78; (2005) 227 CLR 18, 28 [35] where the Court held that impropriety on the part of a director would arise where there was:

a breach of the standards of conduct that would be expected of a person in his position by reasonable persons with knowledge of the duties, powers and authority of his position as director, and the circumstances of the case, including the commercial context. Such standards, expressed according to objective criteria, are ultimately stated, as necessary, by the courts.

(Footnotes omitted.)

1. In *Permanent Building Society (in liq) v Wheeler*,Ipp J (with whom Malcolm CJ and Seaman J agreed) said that the principles applicable to determining whether directors have acted for an improper purpose and in abuse of their powers were well settled. Those principles were common ground in this case. As Ipp J explained (218):

(a) Fiduciary powers and duties of directors may be exercised only for the purpose for which they were conferred and not for any collateral, or improper purpose.

(b) It must be shown that the substantial purpose of directors was improper or collateral to their duties as directors of the company. The issue is not whether business decisions were good or bad; it is whether the directors have acted in breach of their fiduciary duties.

(c) Honest or altruistic behaviour by directors will not prevent a finding of improper conduct on their part if that conduct was carried out for an improper or collateral purpose. Whether acts were performed in good faith and in the interests of the company is to be objectively determined, although statements by directors about their subjective intentions or beliefs will be relevant to that inquiry.

(d) The court must determine whether but for the improper or collateral purpose the directors would have performed the act impugned.

1. Although these principles were not in dispute, (b) and (d) may be controversial in the context of the *Corporations Act*. I proceed only on the basis of these two principles because they were common ground and, in the case of (d), because ASIC accepted the higher burden for its case and made a conscious decision to run its case in that way.
2. As to (b), the question of whether improper purpose is objective or subjective, or a combination of the two, is not wholly settled. As Black J observed in *In the matter of Colorado Products Pty Ltd (in prov liq)* [2014] NSWSC 789 [421], the bulk of authority favours the objective approach. In addition to *Permanent Building Society (in liq) v Wheeler*, cases which might support this approach include *Australian Securities and Investments Commission v Adler* [2002] NSWSC 171; (2002) 168 FLR 253 [738]-[740] (Santow J); *Parker v Tucker* [2010] FCA 263; (2010) 77 ACSR 525, 543 [73] (Gordon J), and *Westpac Banking Corporation v Bell Group Ltd (in liq) (No 3)* [2012] WASCA 157; (2012) 44 WAR 1, 170 [933] (Lee AJA), 353 [1988], 362 [2027], 371 [2073] (Drummond AJA). However, in *Bell Group,* Carr AJA held at 566-567 [2923] that the test whether directors had acted for an improper purpose was primarily subjective. It is unnecessary to resolve this issue.
3. As to (d), initially none of the submissions by ASIC and Mr Drake addressed the test of for causation. In written submissions, ASIC initially assumed that the question of purpose was binary: it was assumed that Mr Drake could only have one substantial purpose and that purpose was either in the best interests of the company or it was an improper purpose. Hence, ASIC submitted that it was necessary to examine *the* substantial purpose for which Mr Drake approved the loan increase, and to reach a conclusion whether that purpose was proper. I do not accept that such a strict approach is required. The substantial (improper) purpose might be one of a number of purposes. Proceeding in this way does not create any unfairness to the Mr Drake. His cases would not have been conducted any differently whether the issue was whether his purpose was *the* substantive purpose or *a* substantive purpose.
4. ASIC also assumed that s 181(1) or s 182(1) require proof that a transaction involving an improper purpose would not have occurred but for the improper purpose. In contrast, in *Eclairs Group Ltd and Glengary Overseas Ltd v JKX Oil & Gas plc* [2015] UKSC 71 [21] Lord Sumption said (Lord Hodge agreeing):

The statutory duty of the directors is to exercise their powers “only” for the purposes for which they are conferred. That duty is broken if they allow themselves to be influenced by *any* improper purpose. If equity nevertheless allows the decision to stand in some cases, it is not because it condones a minor improper purpose where it would condemn a major one. It is because the law distinguishes between some consequences of a breach of duty and others. The only rational basis for such a distinction is that some improprieties may not have resulted in an injustice to the interests which equity seeks to protect. Here, we are necessarily in the realm of causation.

1. Lord Sumption’s approach recognises a mere *influence* as sufficient for a breach of duty. This conclusionrests upon the fact that people are often motivated to act by a number of purposes. They need not be motivated by any single factor, or even any single substantial purpose. The recognition of a mere influence as a breach of duty means that the “but for” test (would the respondent have entered the transaction but for the improper purpose) does not apply to the question of whether a breach has occurred. But the “but for” test would still apply in relation to whether the *consequences* of the breach of duty are that a transaction should be set aside or compensation paid. It is established in Australia that the transaction will not be set aside unless “but for” the breach of duty the transaction would not have occurred or the power would not have been exercised: *Whitehouse v Carlton Hotel Pty Ltd* [1987] HCA 11; (1987) 162 CLR 285, 294.
2. I have doubt whether the “but for” test applies at the stage when it is determined whether a breach of duty occurs. However, all parties assumed that it did and the case was conducted in that way. As I explain below, I accept the submission by senior counsel for ASIC that in this case “different tests of causation are probably unlikely to make much practical difference”.

## The purpose of the re-establishment fee or the August 2012 Variation

### ASIC’s case

1. The August 2012 Variation was the sixth variation to the original loan agreement. But the August 2012 Variation was the first time that a re-establishment fee was charged by LMIM to Maddison Estate.
2. This curiosity of this first occasion for the re-establishment fee may have been the reason why ASIC pleaded that the inference for the charging of this re-establishment fee was the improper purpose of procuring funds for Mr Drake to draw from LMA.
3. Further suspicion as to Mr Drake’s conduct arises from Mr Fischer’s evidence, which I accept, concerning a presentation Mr Fischer gave on 20 June 2012. On that day, Mr Fischer gave a presentation to the LMIM directors which included an overview of the LM Group’s profit forecast. That profit was $8.4 million for the next financial year. Mr Fischer said that he “noted” that the profit included $9 million from the re-establishment fee. All three respondents were at this meeting and the obvious conclusion that they would have drawn, whether correct as a matter of accounting or not, was that without the re-establishment fee there would be a loss suffered by the LM Group for the 2012 financial year.
4. ASIC submitted that the need for the re-establishment fee to make a profit “directly links the decision to approve the August 2012 Variation with the profit forecast for the LM Group for the financial year, and therefore the prospect of whether performance bonuses would be paid for that financial year to the directors”.
5. Several points must be made about this submission. First, there was no evidence that Mr Drake was paid, or entitled to, any bonuses. Secondly, to the extent that it is relevant, I do not consider that Ms Mulder or Mr van der Hoven were contemplating their bonuses when they approved the August 2012 Variation (although ASIC did not cross-examine them on the basis that they have subjectively considered this). The bonuses were paid on a monthly, not an annual basis (ts 693). Ms Mulder had even mistakenly (but honestly) been under the impression, which continued until cross-examination, that the loan was carried in the accounts at the discounted net present value (ts 675). Thirdly, to the extent that this submission by ASIC raises an objective question of whether a profit would have occurred without the re-establishment fee, this invites consideration of whether Mr Fischer’s statement in the 20 June 2012 presentation was correct. As it turned out, the financial report presented on 13 July 2012 forecast a net profit of $10,207,000 and the re-establishment fee became $9.8 million. So it might have been expected on 7 August 2012 that there would have been a small profit made even without the re-establishment fee (although compare the 20 July 2012 minutes which forecast a group profit of $8.4 million).
6. Perhaps the most fundamental difficulty with an inference that the purpose of imposing the re-establishment fee was to increase funds to LMA was that the $9.8 million re-establishment fee involved no movement of funds from Maddison Estate to the MPF. The re-establishment fee would not, and did not, result in any actual movement of funds to LMIM and the MPF because the loan was simply increased by the amount of the fee. In other words, the practical effect of the re-establishment fee was to increase the amount of the loan by $9.8 million rather than to provide any additional available funds. Hence, as Mr Fischer explained, there was no cash to use from that $9.8 million to fund Mr Drake’s lifestyle (ts 324).
7. Since it was not possible to infer that the purpose of the re-establishment fee was *directly* to increase funds to LMA, ASIC’s case instead alleged that the improper purpose of the re-establishment fee, or the August 2012 Variation generally, was to fund Mr Drake’s lifestyle in an *indirect* way as follows (ts 326, 743-744, 771-772, 775-776; submissions [399]):
8. LMA funded Mr Drake’s lifestyle;
9. LMA’s primary source of funding was LMIM’s management fees;
10. LMA’s management fees could be drawn subject to a limit of 10% of the balance of the total assets of the MPF; and
11. increases in the MPF loan balance increased the total assets of MPF and hence increased the upper limit of the management fees which were payable.
12. As I explain below, I accept each of these points. But the inference which ASIC seeks does not flow from them because any funding of Mr Drake’s lifestyle could not reasonably have been expected to be affected by the upper limit of the management fees which were payable.

### The use by Mr Drake of LMA’s funds

1. Mr Drake relied on LMA’s funds to maintain his lifestyle. He was not paid an income from LMA but he drew funds from LMA (as trustee) which he spent on his lifestyle. Those drawings were recorded as a loan to Mr Drake in the financial reports of LMA, rather than as an expense. There was no issue at this trial concerning the legality of these drawings or the manner of their accounting as a “loan”.
2. Mr Fischer monitored Mr Drake’s drawings and expenditure. He said that Mr Drake spent between $5 million and $6 million per year on matters such as his home mortgage, personal expenses, travel, personal staff, and his divorce settlement. One documentary exhibit showed a weekly payment of $50,000 to Mr Drake’s former wife and $21,293 for Mr Drake’s household in the UK. In 2012, Mr Drake also drew money from LMA to make interest payments on a loan he had taken from the MPF (with a $17 million balance in 2012) for his LMIM business expenses. Prior to 2009, the interest on that loan had been paid, but after the global financial crisis and until 2012, Mr Drake had been capitalising the interest. Mr Drake admitted that the yearly balances for his LMA “loan” were as follows:
3. $3,925,901.26 as at 30 June 2009;
4. $9,815,559.82 as at 30 June 2010;
5. $12,157,570.58 as at 30 June 2011; and
6. $22,490,723.44 as at 30 June 2012.

### The source of LMA’s funds

1. Prior to 2009, the LM Group had received revenue from management fees from the LM First Mortgage Income Fund (**FMIF**, a managed investment scheme for which LMIM was the responsible entity) and other funds. In March 2009, after LMIM suspended redemptions to the FMIF, the revenue source for the LM Group increasingly became the MPF. Mr Fischer said in a report on 14 June 2012 that there was a backlog of cash payments for the LM Group of more than $2.5 million and that this was “at a critical point and must be repaid”.
2. The increased reliance on management fees from the MPF can be seen in a chart produced by ASIC:

|  |  |  |
| --- | --- | --- |
| **Financial year ending** | **Management fees from MPF to LMIM (or direct to LMA)** | **Management fees from FMIF to LMIM (or direct to LMA)** |
| 30 June 2010 | $2,740,000 | $12,000,000 |
| 30 June 2011 | $3,270,787 | $10,997,188 |
| 30 June 2012 | $26,953,511 | $5,180,443 |

1. There is one respect in which this chart is not entirely accurate. The amount on 30 June 2012 of $26,953,511 million was described in the MPF audited balance sheet as management fees paid *or prepaid*. Note 12 to the 2012 audited financial statements disclosed that on 30 June 2012, $15,585,329 million (the change in prepayments from 2011) of the $26,953,511 million management fees had been prepayments. Note 12 also disclosed that management fees *expensed* to the MPF for the year ended 30 June 2012 had been $11,368,182 million. This was said in Note 12 to represent 3.1% of the average net assets of the MPF.

### The calculation of management fees and the inference that ASIC alleged should be drawn

1. Senior counsel for Mr Drake put to Mr Fischer in cross-examination that the idea to charge a re-establishment fee was Mr Fischer’s. Mr Fischer denied this, saying that Mr Drake had told him to include the re-establishment fee. I accept Mr Fischer’s evidence on this point. I also accept his evidence that prior to the meeting on 7 August 2012, Mr Drake had asked Mr Fischer to look at a re-establishment fee of 4% (ts 308).
2. The submission by ASIC was that an inference should be drawn that Mr Drake’s purpose in asking Mr Fischer to include a re-establishment fee was to increase the book value of the MPF’s assets, so that larger management fees could be drawn by LMA in order to fund his lifestyle. Even taking into account Mr Drake’s failure to give evidence (which I have addressed above), there are five obstacles to this inference, each of which by itself would be sufficient to prevent the inference from being drawn.
3. **First**, an increase in the assets of the MPF would not have any real practical effect on the limit of the funds which Mr Drake was able to draw from LMA (I reiterate that I say nothing about whether it was lawful for him to draw those funds from LMA, or for them to be treated as “loans”; the only issue was whether the re-establishment fee was for the improper purpose of increasing the funds to LMA to permit more drawing).
4. As Mr Fischer explained, LMIM was entitled to take a management fee of up to 10% per annum of the net value of the MPF (ts 326). The entitlement of LMIM to management fees came from cl 17.3 of the MPF Constitution. From June 2007 until at least October 2012, that clause provided:

The Manager [LMIM] is entitled to be paid a management fee from the Scheme Property up to 10% per annum of the Net Fund Value in relation to the performance of its duties as detailed in this Constitution and the Law. This fee is to be calculated monthly and paid at such times as the Manager determines.

1. The management fee paid to LMIM would accrue to LMA because the LMA Service Agreement between LMIM and LMA (as trustee for LMA Trust) provided in cl 5 for service fees to be paid according to Sch 1 of the MPF Constitution. Section 8 of Sch 1 provided that the service fees included “all management fees on behalf of [LMIM] earned in [LMIM’s] capacity as manager of all of its managed investment schemes”.
2. If Mr Drake wished to ensure that LMA had sufficient funds to allow him to maintain his lifestyle then he could simply have increased the LMIM management fee (and therefore the management fee which would accrue to LMA under the LMA Service Agreement). He did not need to increase the assets of the MPF to do this because the management fees paid to LMIM were significantly less than 10%. As I have explained, the 30 June 2012 audited financial statements for the MPF described the management fees paid to LMA as 3.1% of average net assets.
3. Hence, a simple way for LMA’s cash assets to increase would have been for LMIM to charge higher management fees, which would then be paid to LMA. It was not necessary to increase the assets of the MPF, or to charge a re-establishment fee, in order to charge these higher fees.
4. **Secondly**, although a large part of LMA’s staff were devoted to MPF business (ts 325), Mr Fischer explained that the management fees paid to LMA remained too low. Mr Fischer regularly had conversations with Mr Drake to the effect that the management fees were too low and Mr Fischer would ask Mr Drake why more management fees were not taken from the MPF (ts 326).
5. Once again, not only would there have been little obstacle to increase LMA’s cash assets by LMIM charging higher management fees, but Mr Drake was under pressure to take this course. An example is the minutes of the 4 June 2012 meeting which described how Mr Fischer had emphasised to directors (including Mr Drake) the importance of declaring a fee to which LMIM was entitled of up to 10% of the funds under management.
6. If Mr Drake had wanted to increase LMA’s funds in order to increase his “loan” to fund his lifestyle then the simplest step to take would have been to agree to the course of charging higher management fees.
7. **Thirdly**, during 2012 Mr Fischer had been putting pressure on Mr Drake to *reduce* his expenses from LMA which had been used to fund Mr Drake’s lifestyle. So, to the extent that Mr Drake was contemplating any further amount which he could “borrow” from LMA, he must have been aware that it was being watched closely and that there would be resistance to any more borrowing.
8. Mr Fischer closely monitored Mr Drake’s “loans” from LMA. He described the amount of those loans and, from his recollection, the use to which the money was put in considerable detail. He explained how if a payment to Mrs Drake from the divorce settlement was missed, he would often receive a phone call from Mrs Drake, or from her lawyer. Mr Fischer also said, and I accept, that in 2012 he had told Mr Drake on several occasions that he (Mr Fischer) was concerned about the amount of money Mr Drake was drawing from the business. Mr Fischer had also mentioned this to other directors of LMIM. I have little doubt that Mr Drake was under considerable pressure to reduce his drawings from LMA.
9. In around June or July 2012, Mr Drake’s accountant and Mr Fischer both separately declined to support Mr Drake’s request for an equity payment from a bank to pay out $5 million to Mr Drake’s ex-wife. Mr Drake’s accountant and Mr Fischer also refused Mr Drake’s request to borrow against the business in order to buy the property next door to his home, so that he could build a tennis court.
10. After Mr Fischer put pressure on Mr Drake to reduce his LMA drawings (or “loan”), Mr Drake agreed to do so, although he did not ultimately do so. The reasons for the large increase in LMA drawings or “loan” were not explored in any of the parties’ submissions. It seems from one LMA accounting record that at least part of the increase in 2012 ($1,207,277) was due to Mr Drake using these “drawings” to repay his loan from the MPF for LMIM business expenses. Another difference in the 2012 financial year which contributed to the larger amount of “drawings” was a payment on the last day of the financial year from LMA of more than $2.4 million for “Loan Reduction … Maddison Estate …” which may have been a repayment of part of the capital for Mr Drake’s loan from the MPF for his LMIM business expenses. However, other matters were plainly Mr Drake’s personal expenses. For instance, more than $4 million was transferred to his ex-wife.
11. In any event, the increased pressure from Mr Fischer militates against an inference that, at least by August 2012, Mr Drake would have sought to increase the assets of the MPF so that he could raise the ceiling for the LMA’s fees (which had not come close to reaching the ceiling) in order to maintain or increase his expenditure from an increased “loan” or drawings from LMA.
12. **Fourthly**, Mr Drake was a party to efforts to *reduce* the MPF’s assets by reducing prepaid management fees (which were recorded as an asset) and expensing those fees. Going into the 2013 financial year, those efforts had proved fruitful (ts 326). As Note 12 to the audited financial statements, observed, “as at the date of this report [December 2012] the balance had reduced to $17.7 million [from $26.9 million]”. It would be a curious scheme by Mr Drake to attempt to inflate the assets of the MPF in order to increase the limit for management fees and yet, at the same time, to pay down prepayments dramatically, causing an equivalent decrease in the assets of the MPF which prevented him from increasing the limit by which he could charge higher management fees.
13. **Fifthly**, there are a number of competing inferences. As for the decision to approve the 2012 Loan Variation itself, the obvious inference was that this decision was one which was made to preserve the project against the potentially disastrous alternatives of refusing the variation or deferring it. There is no need to draw an inference, against the four matters above, that the 2012 Loan Variation was somehow motivated by an improper purpose of increasing the assets of the MPF in order to allow an increased limit for management fees that could be paid to LMA.
14. As to the re-establishment fee, one competing inference is that the re-establishment fee was included because that is the fee which should be charged for a development loan of this nature. Mr Fischer accepted that for a development loan of this kind there were typically re-establishment fees of between 2% and 3% (ts 324). It is true that none of the other increases in the loan had charged a re-establishment fee. But none of the other increases had been for $100 million.
15. Another competing inference is that the re-establishment fee was used so that management fees which had been prepaid could be expensed (instead of treated as a prepayment, and hence an asset) so that the total net assets would remain unchanged. I emphasise that at no stage in this case did ASIC plead or submit that Mr Drake had prepaid the large amount of management fees in 2012 ($15,585,329) as part of any improper scheme or for any illegitimate purpose concerning an artificial increase in the assets of the MPF. The massive increase in prepayments in 2012 is, to say the least, extremely curious and there was evidence from Mr Fischer that he and Ms Darcy were not happy with the increase (ts 389). But it was not part of ASIC’s case that the prepayments were for any improper purpose and no attention was directed to the purpose for this prepayment in 2012 other than the submission that the purpose was for LMA to obtain cash to run its business.
16. The competing inference of using the re-establishment fee as a means of offsetting the increased prepayments might be inferred from the following.
17. The evidence was that management fees could be paid as an expense or as a prepayment. The difference for accounting purposes was that recording the management fees as a prepayment meant that they were an asset on MPF’s balance sheet. But recording them as an expense meant that they reduced the MPF’s net profit. The difficulty with recording the fees as “pre-paid” is that they could not be recorded in this way forever, especially as LMA was continually performing work and earning fees. But a reduction in the amount of prepayments (and corresponding increase in expense) would have the effect of decreasing the MPA’s assets (as the prepayment is an asset) and decreasing its net profit (due to the increased expense). As Mr Fischer observed, a consequence of reducing assets on the balance sheet could be a reduction in the unit price of the fund which was one dollar. Mr Fischer often heard Mr Drake say that he did not want to affect the unit price of the funds.
18. If assets (and the unit price) of the MPF were to be maintained then the MPF needed a scheme to maintain the asset value. This scheme would need to address a fall in assets which resulted from the recording a pre-payment as having become an expense. Mr Fischer accepted in cross-examination that a result of charging the re-establishment fee was that in the process the assets of the MPF were not depleted despite the reduction in prepayments and, consequently, the unit price of the MPF was unaffected (ts 324). By December 2012, the MPF had reduced prepayments by around $9.2 million. The loan re-establishment fee of $9.8 million ensured that the total assets of the MPF were unaffected by this reduction in the prepayment asset.

## Conclusion on improper purpose

1. For the reasons above, I do not accept that the pleaded improper purpose was, either objectively or subjectively, a motivating factor for Mr Drake voting to approve the August 2012 Variation.
2. Nor do I accept that, even if it was a subjective purpose in Mr Drake’s mind, it was a purpose but for which Mr Drake would not have approved the August 2012 Variation. Initially, in oral closing submissions, senior counsel for ASIC conceded that ASIC could not establish that but for the alleged improper purpose Mr Drake would not have approved the August 2012 Variation. Although that concession was later retracted, it was properly made for the reasons I have explained above.

# Conclusion

1. ASIC’s claims against each of the remaining three respondent directors of breach of s 180(1) of the *Corporations Act* must be dismissed. In broad terms the claims must be dismissed for each of the following reasons:
2. ASIC ran its case on the basis that a breach of trust was a precondition to establishing liability, but the duty of care upon which that breach was based had been excluded by the MPF Constitution;
3. ASIC’s pleaded case, properly construed, required an actionable breach of trust as a precondition to establishing liability, but ASIC failed to prove that any breach caused any losses to be suffered;
4. ASIC’s pleaded case was that the act which constituted the breach of s 180(1) was the decision by the respondents to approve the August 2012 Variation on 7 August 2012, but ASIC’s case omitted to assess alternative choices to a prudent trustee on 7 August 2012 (either to defer the decision or refuse the loan variation). A breach of s 180(1) in the circumstances of this case required ASIC to prove that a prudent trustee would have chosen one of those alternatives; and
5. to the extent to which there was information before the Court to assess the alternative choices, ASIC failed to prove that a reasonable director of a company in LMIM’s circumstances, with the responsibilities of each respondent, would have refused to approve the August 2012 Variation.
6. Much of the difficulty and gaps in ASIC’s case were caused by what can only be described as the implosion of its expert witness, Mr Woolley. For instance, as to (3), even Mr Woolley who generally would not concede even the clearest points, accepted that deciding whether something is a prudent decision to approve involves an identification of the alternatives and an assessment of the alternatives (ts 604). But Mr Woolley singularly failed to do so and ASIC’s case followed suit.
7. I reiterate that ASIC’s case for contravention of s 180(1) against each of Mr Drake, Ms Mulder, and Mr van der Hoven was concerned only with an alleged breach of duty arising from LMIM’s decision on 7 August 2012. By the conclusion of trial, no claim was made that any earlier decision or any earlier conduct was itself a breach of duty. The assessment of breach as at 7 August 2012 is based on all the circumstances in which LMIM found itself: with $190 million of investors’ money protected by a second mortgage over a development where the first mortgage holder was anxious to exit, the loan was overdrawn, and, on one view, the only realistic prospect for the investors recovering some or all of their money was to complete Stage 1 of the development and move towards the exit plan.
8. In light of the conclusion I have reached, it is unnecessary to deal with the pleas by each of the respondents for relief from liability based on s 1317S and s 1318(1) of the *Corporations Act*. Whether such relief would be given would depend upon the nature of the breach which had been found and the circumstances of that breach. For instance, the submissions by Ms Mulder and Mr van der Hoven on this point speculated upon different possible findings about the nature of a breach which might be established and what findings might be made about an independent feasibility analysis. It would be inappropriate to attempt to catalogue all possible adverse findings in order only to address a hypothetical relief against liability. However, for completeness, and in circumstances in which both Ms Mulder and Mr van der Hoven gave evidence, I record my conclusion that both were honest and reliable witnesses and that I accept from their evidence, and in all the circumstances, that the decision that each took on 7 August 2012 was taken honestly, in good faith for a proper purpose, and which decision they rationally believed to be in the best interests of the corporation. There would be strong grounds to conclude that each ought fairly be excused depending upon the nature of the liability which was found.
9. Each of the matters in the penultimate sentence in the paragraph above could also be a strong basis for concluding that the business judgment rule, contained in s 180(2) of the *Corporations Act*, applied subject to the issues of (i) whether the respondents informed themselves about the subject matter of the judgment to the extent they *reasonably* believed to be appropriate, and (ii) whether the respondents had a material personal interest in the subject matter of the judgment. It is unnecessary to reach any conclusions on these issues but it suffices to say that there would have been real obstacles in the path of the respondents establishing that the 7 August 2012 business judgment, which caused the re-establishment fee to be payable and which affected Mr van der Hoven and Ms Mulder’s bonus entitlements, was one in which they did not have a material personal interest in the subject matter of the judgment.
10. The claims against Mr Drake for contravention of s 181(1)(b) and s 182(1)(a) of the *Corporations Act* also fail for the following reasons:
11. LMIM did not commit a breach of trust for the two independent reasons described above; and
12. ASIC failed to prove that Mr Drake acted for the pleaded improper purpose.
13. Finally, it is necessary to make one observation about an assumption which underpinned the way this case was run. I alluded to this point earlier when discussing Ms Blank’s report. This observation is not said critically of the conduct of a lengthy and detailed case by skilled counsel and solicitors. The assumption was made by the parties generally although, most clearly by ASIC because some submissions by the respondents can be read as doubting the assumption. It was that the Maddison Estate loan should be treated as a loan for the purposes of assessing matters such as its net present value, recoverability and so on. However, one of the surrounding circumstances relied upon by ASIC (and which I have taken into account) was that Maddison Estate was a special purpose vehicle “set up for the purpose of allowing the MPF to mimic [although not precisely] a *de facto* equity position in the development while carrying the amount of the loan in the assets of the fund as an amount receivable and referring to the investment in various information memoranda as a commercial loan”. There is a tension between this stance and ASIC’s assumption that the loan should be treated as a loan for the purposes of matters such as its net present value and recoverability. If the loan were properly to be characterised as an equity position then it might be strongly arguable that assessments of the value of the “loan” for the purposes of “recoverability” should not include the “capitalised interest” of potentially around $100 million at the time of the August 2012 Variation decision. The “recoverability” of an equity position would be recoverability of the capital contribution, not recoverability of speculative profits. The amount of “capitalised interest” might, on an equity participation view, be properly characterised as profits at the conclusion of the development with the treatment of it as capitalised interest income to be, as described in the information memoranda, “only for taxation purposes”. But these issues were not explored. They were not the subject of any detailed expert evidence. I have put them to one side in these reasons and treated the loan in the way that it was treated in the evidence, albeit taking into account its terms as a loan to a special purpose vehicle which was designed not to profit from the development.
14. I will hear from the parties concerning costs but prima facie the appropriate order should be that ASIC pay the costs of the first, second and third respondents, to be taxed if not agreed.

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| I certify that the preceding five hundred and forty-three (543) numbered paragraphs are a true copy of the Reasons for Judgment herein of the Honourable Justice Edelman. |

Associate:

Dated: 23 December 2016

SCHEDULE OF PARTIES

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|  | QUD 596 of 2014 |
| Respondents |  |
| Second Respondent | FRANCENE MAREE MULDER |
| Third Respondent | EGHARD VAN DER HOVEN |
| Fourth Respondent | SIMON JEREMY TICKNER |
| Fifth Respondent | LISA MAREE DARCY |