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Dear Sirs

TRADING TRUSTS – OPPRESSION REMEDIES

The attached submission responds to the Commission's consultation paper dated June 2014 on trading trusts – oppression remedies.

The submission consists of responses to a number of the questions set out in the consultation paper. The responses focus on the questions set out on pages 68 and 69 of the consultation paper. Non-responses to particular questions are intentional (that is, we have no informed view on their subject matter).

The submission is made:

- on behalf of Mr Ari Bergman, known to the Committee; and
- this firm.

In some instances, our views (that is, of Mr Bergman on the one hand and of this firm on the other) diverge. The submission identifies the divergence. As Mr Bergman has been overseas, making it difficult for him to prepare a separate submission, he asked us to make this submission jointly (notwithstanding the divergence of responses on some questions).

In addition to the responses, we also attach an updated version of Mr Bergman's doctoral thesis entitled "Should statutory oppression remedies apply to unit trusts? A comparison of unitholder and shareholder rights" submitted by Mr Bergman to Monash University on 26 June 2014. (A previous draft was provided by Mr Bergman to the Commission, and has been cited in the Consultation Paper). While the responses set out in the submission are brief, the thesis contains more substantive discussion on the reasons for the positions outlined in the submission. Where relevant, the responses should be read in conjunction with the thesis.

Yours faithfully

[redacted]

JOHN HUTCHINGS
CHAIRMAN OF PARTNERS
CORNWALL STODART

SUBMISSION RESPONDING TO QUESTIONS IN CONSULTATION PAPER

1 IN YOUR VIEW, WHAT ROLES DO THE INTENTION OF THE SETTLOR AND THE LAW OF CONTRACT PLAY IN UNIT TRUSTS?

1.1 Essentially, a trust is a contractual obligation between the settlor and trustees in terms of how the trustees deal with the property of the trust.

1.2 The intention of the settlor is often considered by the Courts in determining how a particular trust deed is to be construed.

This is frequently based on a view that, since a trust is created by the settlor with property that had previously been his, the settlor's intentions about the operations of the trust and the conditions under which the trust property is dealt with should be determinative.

1.3 In our experience, the emphasis on the settlor's intention is largely misplaced:

- In any event, many unit trusts are created by declaration rather than by deed of settlement: i.e., there is no settlor.
- Most of deeds of settlement are created by settlors of convenience: the settlor is a professional acting for or family friend of the appointor and the settlement sum is nominal.

1.4 Beyond the relationship of settlor and trustee, there has been increasing support in legal academic and judicial circles for according a broader role to contract law in the context of trusts, most notably with respect to the relationship between the unitholder and the trustee, and to a lesser extent, between unitholders (in cases where there is no unitholders' agreement). The law is undeveloped and, therefore, the rights that may arise from those potential contractual relationships are difficult to determine.

2 HOW RELEVANT OR IMPORTANT IS THE CHARACTERISATION OF A BENEFICIARY OR UNITHOLDER'S INTEREST?

2.1 The interest of a beneficiary or a unitholder in a trust is fundamentally different in nature from a share in a company, which confers upon the holder no legal or equitable interest in the assets of the company but is a separate piece of property.

2.2 While beneficiaries may have an underlying equitable interest in the assets of the trust (in contrast to shareholders), the rights associated with those beneficial interests do not provide materially greater practical protection to beneficiaries in the context of oppressive conduct.

2.3 Accordingly, while the differences may need to be acknowledged for the purpose of legal analysis, the difference is unimportant from a fairness view point given that:

- the assets of a company are managed by those who control the company; and
- the assets of a trust are managed by the trustee or those who control the (corporate) trustee.

3 IS THERE ANOTHER, MORE APPROPRIATE DEFINITION OF 'TRADING TRUST'? COULD IT INCLUDE MANAGED INVESTMENT SCHEMES?

3.1 The terms "trading trust" and "investment trusts" are generally used to refer to trusts that carry on a specific type of activities.

3.2 The main characteristic of the trading trust is that the trust property is used in the conduct of business.

3.3 By contrast, the trustee of an investment trust holds assets (e.g. listed or unlisted equities, government/corporate bonds, real estate, shares in private companies) for a specific objective or objectives (e.g. growth, income, capital preservation).

3.4 Both a "trading trust" and an "investment trust" can either be public or private and can include unit trusts, discretionary trusts or a mixture of two.

3.5 The Oppression Remedy under section 232 of the *Corporations Act* 2001 (Cth) (**CA**) does not distinguish between trading companies and investment companies.

3.6 Section 232 of the CA provides that:

"The Court may make an order under section 233 of the CA if:

(a) the conduct of a company's affairs; or

(b) an actual or proposed act or omission by or on behalf of a company; or

(c) a resolution, or a proposed resolution, of members or a class of members of a company.

Is either:

(d) contrary to the interests of the members as a whole; or

(e) oppressive to, unfairly prejudicial to, or unfairly discriminatory against, a member or members whether in that capacity or in any other capacity.

3.7 The term "affairs" is defined in section 53 of the CA to include, without limitation, the promotion, formation, membership, control, business, trading, transactions and dealings, property.

3.8 Section 232 of the CA does not currently apply to managed investment schemes.

3.9 It is submitted that the availability of the Oppression Remedies should not be based on the characteristics of the trust. Regard has to have been the conduct of the trust's affairs and the action taken or proposed to be taken by the trust in question (or more specifically, the trustee).

3.10 It is Mr Bergman's view that the availability of the Oppression Remedies should not be limited to unit trusts. He believes that it should apply to all trusts, including managed investment trusts, subject to the exceptions set out in paragraphs 3.11 and 3.12 below.

In our view, several difficulties confront applying Oppression Remedies to discretionary trusts, not least being that there are no individual beneficiaries, rather persons who have the right to be considered for benefit, which connotes a broad intent unstrained by notions of fairness.

3.11 The Oppression Remedies are not considered appropriate for superannuation trusts (and in particular, self-managed superannuation funds) as those trusts may be controlled by members and are highly regulated by the *Superannuation Industry (Supervision) Act* 1993 (Cth).

3.12 The Oppression Remedies may likewise be appropriate for charitable trusts which are also regulated differently.

4 ARE OPPRESSION REMEDIES APPROPRIATE FOR ALL TRADING TRUSTS?

4.1 In Mr Bergman's view, the Oppression Remedies should be available to all trading trusts, whether they are unit trusts, discretionary trusts or otherwise: to exclude discretionary trusts from the application of Oppression Remedies would result in a significant group of oppressed trust beneficiaries lacking access to effective remedies. Mr Bergman believes that there are circumstances where certain beneficiaries of discretionary trusts develop economic relationships (e.g. via loan accounts) with the trust that Mr Bergman suggests may give rise to legitimate expectations for those economic interests to be protected against oppressive conduct by the trustee. Further, there are circumstances where discretionary trusts form part of larger groups of entities in which oppression may occur, and remedying the rights of oppressed parties may require recognition of their rights as beneficiaries of discretionary trusts.

Mr Bergman suggests that, were Oppression Remedies to apply to discretionary trusts, it would be appropriate for the Legislature to set out the criteria that must be met in order to invoke the Oppression Remedies.

As indicated above, this firm does not consider that Oppression Remedies should be available for discretionary trusts.

4.2 We believe that the Oppression Remedies should be available to all non-trading trusts (other than the superannuation trusts and charitable trusts).

5 ARE THERE CIRCUMSTANCES IN WHICH AN OPPRESSION REMEDY WORKED TO PROTECT SHAREHOLDERS?

5.1 There are a number of cases where oppressive, unfair, prejudicial or unfairly discriminatory conduct has been found and the Courts have granted the Oppression Remedies to protect shareholders.

5.2 It is our experience that there are many more cases than those reported where oppressive conduct is alleged which are resolved by negotiation. In our opinion, the existence of those cases supports a conclusion that the Oppression Remedies have worked to protect shareholders.

6 HOW WELL HAS THE OPPRESSION REMEDY WORKED TO PROTECT SHAREHOLDERS

6.1 Refer response to 5.

7 IN YOUR VIEW, DOES THE EXISTING OPPRESSION REMEDY APPLY TO TRADING TRUSTS? IF NOT, SHOULD IT?

7.1 In our view, the existing Oppression Remedy does not apply to trusts – trading or otherwise. Nor does it apply to any other trusts.

7.2 The existing Oppression Remedy may only be invoked by a member of a company[1]. Under the current law, a beneficiary does not have standing to apply for the existing Oppression Remedy if the beneficiary is not a member of the corporate trustee of the trust, or if the trustee is not a company.

7.3 It is Mr Bergman's view that the existing Oppression Remedy should also apply to trusts (other than superannuation trusts and charitable trusts). We believe that it should also not apply to discretionary trusts.

8 DO YOU AGREE WITH THE REASONING IN *KIZQUARI?*

8.1 The decision in *Kizquari* provided the foundation for the line of cases upholding the proposition that the courts should reject the application of the oppression remedies to unitholders in trusts. Young J commented that, because the oppressive conduct had no impact on the value of the shares, the oppression remedies had no application. However, oppressive conduct may have a significant impact on the value of the units - a point that Young J held was of no relevance in considering the relief that could be provided to the shareholder/unitholder under the subsisting oppression remedies. While Young J in *Kizquari* emphasised that the trust law remedy of ordering repayment of the excessive salaries to the trust could provide the aggrieved unitholders with partial relief, the fact remains that they were unable to achieve their desired remedy (compulsory buyout of their units).

8.2 We agree with the reasoning in Kizquari i.e., that the subsisting Oppression Remedies cannot apply to trusts.

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[1] Section 231 of the CA.

9 JUSTICE YOUNG IN *KIZQUARI* TREATS THE VALUES OF SHARES AND THE VALUE OF UNITS AS ENTIRELY SEPARATE MATTERS. DO YOU AGREE WITH THIS APPROACH?

9.1 The values should be separated as they consist of different "assets". It is Mr Bergman's view that Young J's approach is correct.

9.2 We believe that, except insofar as they provide a means of control of the trustee, the shares in the corporate trustee are a non-sequitur: in our opinion, the distinctions are not readily perceived by the consumers of legal services and reflect adversely on the judicial process in terms of perception.

10 WHICH APPROACH TO SECTION 232 DO YOU CONSIDER PREFERABLE, ACTING JUSTICE WINDEYER'S OR JUSTICE DAVIES'?

10.1 Windeyer J's view in Trust Company Ltd v Noosa Venture 1 Ply Ltd2 (Noosa Ventures) is preferred. She held that the argument that section 232 of the CA refers to 'the conduct of the company's affairs' as defined in section 53 of the CA to include the affairs of the company as trustee in dealing with beneficiaries rights is persuasive.

10.2 It is submitted that some difficulty arises from Davies J's conclusion that the phrase in section 232 of the CA, 'a member or members whether in that capacity or any other capacity,' empowered the Court to provide relief to a shareholder in the capacity of unitholder of a Unit Trust. While the phrase 'or any other capacity' may contain some ambiguity, it appears to have been directed to providing relief under section 233 to a shareholder who holds shares as trustee, or alternatively, where a shareholder is also a director, employee, or has some other direct relationship that is affected by the oppressive conduct. It does not seem to be directed to remedying issues unrelated to the shareholder's shareholding, such as units (or other assets/rights that the shareholder may hold). Whilst there has been limited discussion as to whether the oppression remedies can compensate interests beyond the shareholding, the courts seem hesitant to deploy them in that way. In Starr3, Justice Young noted the reluctance of the courts to utilise oppression remedies to assist franchisees in enforcing their franchise contracts with a corporate franchisor. Indeed, Young J's approach in both in Kizquari and Starr has been that non-shareholder rights are to be enforced outside the oppression remedies. There does not appear to be case law to support Davies J's assertion that the wording 'in any other capacity' is intended to open up oppression remedies.

11 DO YOU AGREE WITH JUSTICE DAVIES' INTERPRETATION OF THE PURPOSIVE APPROACH?

11.1 We agree with Justice Davies' interpretation of the purposive approach, but do not agree with the law.

12 DO YOU AGREE WITH JUSTICE DAVIES' INTERPRETATION OF SECTION 53?

12.1 No. Refer to paragraph 10 above.

13 DO YOU AGREE WITH JUSTICE FERGUSON'S APPROACH OF TREATING THE WHOLE GROUP AS ONE ENTITY?

13.1 We agree that Justice Ferguson's purposive approach should be adopted (i.e., by changes to the law) but as the law currently stands, we do not believe that the law currently provides for trusts to be grouped with companies in the provision of Oppression Remedies to oppressed unitholders.

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[2] (2010) 80 ACSR 485.

[3] Starr (1991) 6 ACSR 63.

14 EVEN UNDER THE MORE LIBERAL APPROACH ADOPTED IN *VIGLIARONI* AND *DRAPAC*, IN ORDER TO CLAIM AN OPPRESSION REMEDY, THE PLAINTIFF NEEDS TO BE BOTH A MEMBER/SHAREHOLDER AND A BENEFICIARY. IS THIS APPROPRIATE AND DESIRABLE?

14.1 In our view, it is not desirable that a plaintiff seeking relief from oppressive conduct should have to be both a member and beneficiary. We believe that the law should be extended to unitholders and other beneficiaries who are not shareholders.

15 DO YOU AGREE WITH JUSTICE FERGUSON'S USE OF THE 'QUASI-PARTNERSHIP' DOCTRINE AS SET OUT IN *EBRAHIMI*?

15.1 Ferguson J's reference to *Ebrahimi* sought to lend weight to the application of oppression remedies to cases of oppression generally (irrespective of structure) so that a just and equitable result could be achieved for an oppressed party. While Ferguson J largely followed the thinking of Davies J in *Vigliaroni,* her Honour supported it by introducing the 'quasi-partnership' concept. Ferguson J asserted that the 'quasi-partnership' principle could be used as a bridge to support statutory relief under the CA oppression remedies, especially when applied to a buyout. *Koko Black* excluded buyouts as a remedy under *Ebrahimi.*

15.2 In our view, the use of the "Quasi-Partnership" Doctrine to provide for a court ordered buy out of units is unconvincing.

16 ARE THERE ANY CIRCUMSTANCES IN WHICH TERMINATION UNDER THE TRUST DEED COULD PROVIDE A SATISFACTORY REMEDY TO MINORITY BENEFICIARIES?

16.1 Yes, although such a remedy will only be effective in a limited number of circumstances (i.e., where there is no negative impact on the value of the trust assets that the oppressed minority beneficiary receives as a result of the termination).

17 CAN THE DOCTRINE OF ESTOPPEL ASSIST A UNITHOLDER IN REDEEMING THEIR INTEREST ON MORE FAVOURABLE TERMS THAN PROVIDED FOR IN THE TRUST DEED?

17.1 Yes, estoppel based on *Koko Black* may assist, but the facts that give rise to estoppel do not commonly apply to cases involving oppression of beneficiaries.

18 CAN RELIEF UNDER THE *TRUSTEE ACT 1958* (VIC) PROVIDE AN EFFECTIVE ALTERNATIVE REMEDY FOR OPPRESSION OF MINORITY BENEFICIARIES?

18.1 In our view, the *Trustee Act 1958 (Vic)* does not provide an effective alternative remedy for oppression of minority beneficiaries.

18.2 The *Trustee Act 1958 (Vic)* only governs the conduct of trustees and not the conduct of a majority of beneficiaries or the conduct of those who control the (corporate) trustee.

19 COULD SEEKING AN ORDER UNDER THE INHERENT JURISDICTION OF THE COURT PROVIDE AN ALTERNATIVE REMEDY FOR MINORITY BENEFICIARIES?

19.1 There are authorities to suggest there is no inherent jurisdiction in the Court to provide an alternative remedy for minority beneficiaries. Hence the scope for minority beneficiaries to receive an alternative remedy is, at best, uncertain under the current law.

20 IN YOUR VIEW, CAN THE 'QUASI-PARTNERSHIP' APPROACH ADOPTED IN *EBRAHIMI* APPLY TO TRADING TRUSTS? IF SO, CAN A BENEFICIARY OBTAIN A REMEDY OTHER THAN THE WINDING UP OF THE TRUST?

20.1 Some cases in the UK suggest that it can apply to trading trusts.

20.2 It is difficult to see how a successful invocation of the quasi-partnership approach can result in any remedy other than termination under the trust deed.

21 ARE THERE CIRCUMSTANCES IN WHICH THE DOCTRINE OF FRAUD ON POWER COULD PROVIDE A USEFUL REMEDY TO MINORITY BENEFICIARIES?

21.1 Fraud on the power is a breach of trust for which aggrieved unitholders/beneficiaries are able to seek remedies that commonly include declarations, injunctions, rescission or restitution. Within the context of oppressive conduct in trusts, such remedies are, therefore, of potential value in assisting oppressed unitholders/beneficiaries. However, the traditional doctrine of fraud on the power (in a Unit Trust context) will generally only provide relief to a unitholder against the trustee rather than against fellow unitholders.

21.2 Most claims of oppression relate to circumstances where the alleged infringer has acted in accordance with the terms of the empowering document but in a manner that is oppressive to the aggrieved party. In such circumstances, the doctrine is generally inapplicable.

22 IS LEGISLATIVE REFORM TO PROVIDE OPPRESSION REMEDIES TO MINORITY BENEFICIARIES IN VICTORIA JUSTIFIED?

22.1 We would prefer that comprehensive oppression remedies be incorporated into national legislation (constitutional restrictions permitting). It is submitted that, in the context of oppression, the CA, rather than the Trustee Acts, is the primary legislative instrument by which unitholders should have access to relief. The law of oppression has developed substantially within the general corporate law context and, as Hely J argued in *Cachia*, the doctrine of fraud on the minority, which was the precursor to oppression remedies in corporate law, was viewed as an exclusively corporate law doctrine. Given the substantive development of oppression remedies under the CA, it would seem appropriate to provide protection to oppressed unitholders/beneficiaries primarily through that legislation.

22.2 The federal legislature have historically been reluctant to regulate trusts under the CA and there is no certainty that it will be persuaded to change that attitude. Failing action by the Commonwealth, consideration should be given to amendments to the Trustee Acts to include relief against oppression as an alternative. Amendments to the *Trustee Act 1958 (Vic)* would afford protection in those oppression cases where there is no corporate trustee.

22.3 It reflects adversely on the law and the judicial process that, from time to time, unitholders/beneficiaries who have been oppressed are found not to have any remedy.

22.4 It is therefore timely for the legislature to take action to address the deficiencies and to provide lucidity, certainty and trust in the law.

23 COULD NEW REMEDIES UNDER THE TRUSTEE ACT COEXIST WITH THOSE UNDER THE CORPORATIONS ACT?

23.1 Refer to paragraph 22 above.

24 SHOULD THE *TRUSTEE ACT 1958* (VIC) BE AMENDED TO PROVIDE OPPRESSION REMEDIES FOR MINORITY BENEFICIARIES?

24.1 Yes, although it is our preference to extend the operation of the Oppression Remedies currently available for companies in the CA - see paragraph 22 above.

25 IF SO, TO WHAT EXTENT SHOULD THE PROVISIONS REFLECT THOSE IN PART 2.1F OF THE CORPORATIONS ACT?

25.1 There are significant advantages in, so far so possible, adapting the provisions of Part 2.1F of the CA: i.e., the courts have already applied and interpreted their provisions.

26 SHOULD THE ORDERS AVAILABLE TO THE COURT BE SPECIFIED, OR LEFT TO WHAT THE COURT 'CONSIDERS APPROPRIATE' AS IN SECTION 233 OF THE CORPORATIONS ACT?

26.1 In our opinion, section 233 of the CA works well. For that reason, we favour leaving it to the Court to make any order it considers appropriate to the circumstances of individual cases.

27 SECTION 233 OF THE CORPORATIONS ACT PROVIDES A NON-EXHAUSTIVE LIST OF EXAMPLES OF THE TYPES OF ORDER AVAILABLE. SHOULD A SIMILAR LIST BE INCLUDED IN ANY AMENDMENT TO THE TRUSTEE ACT?

27.1 Yes, a similar list should be included. Refer to paragraph 26 above.

28 WHAT EFFECT SHOULD THE TRUST DEED HAVE ON THE AVAILABILITY OF ANY OPPRESSION REMEDIES INCLUDED IN THE TRUSTEE ACT? SHOULD IT BE POSSIBLE TO EXCLUDE THEIR OPERATION BY EXPRESS PROVISIONS IN THE TRUST DEED?

28.1 In Mr Bergman's view, the Oppression Remedies should not be capable of being excluded by express provisions in the trust deed: otherwise it would defeat the purpose of the remedies, which is to provide the minority beneficiaries with protection against commercially unfair practices on the part of the trustee or those who control the trustee.

29 SHOULD SUCH A PROVISION APPLY TO ALL TRUSTS? IF NOT, WHICH TYPES OF TRUSTS SHOULD BE COVERED?

29.1 In Mr Bergman's view, it should apply to all trusts, including managed investment schemes, but excluding superannuation funds and charitable trusts. In our view, it should also not apply to discretionary trusts.

30 ARE THERE ANY ALTERNATIVE LEGISLATIVE REFORMS THAT, IN YOUR VIEW, SHOULD BE CONSIDERED TO PROTECT THE RIGHTS OF OPPRESSED BENEFICIARIES?

30.1 In Mr Bergman's view, the following alternative legislative reforms might be considered:

30.1.1 Allowing discretionary trusts to opt in to the Oppression Remedies. A register should be maintained to keep records of the discretionary trusts subject to the regime.

30.1.2 If under a registration process, payment of fees to access the remedies.

30.1.3 Providing for "derivative action" rights for beneficiaries against directors of corporate trustees, and for personal liability of directors of trustees.

31 WOULD THE INTRODUCTION OF STATUTORY OPPRESSION REMEDIES FOR BENEFICIARIES OF TRADING TRUSTS AFFECT THE INTERESTS OF DIRECTORS OR TRUSTEES? IF SO, HOW?

31.1 The introduction of statutory oppression remedies for beneficiaries of trading trusts would potentially expose the trustee and directors of the corporate trustees to greater liabilities than those to which they are currently subjected.

32 WOULD THE INTRODUCTION OF STATUTORY OPPRESSION REMEDIES FOR BENEFICIARIES OF TRADING TRUSTS AFFECT THE INTERESTS OF CREDITORS? IF SO, HOW?

32.1 The introduction of statutory oppression remedies for beneficiaries of trading trusts should not affect the interests of creditors.

32.2 In determining appropriate remedies, the Court often has regard to the interests of creditors.

33 WOULD THE INTRODUCTION OF STATUTORY OPPRESSION REMEDIES FOR BENEFICIARIES OF TRADING TRUSTS AFFECT THE INTERESTS OF EMPLOYEES? IF SO, HOW?

33.1 No.