When is a person responsible as an "officer" of a company?

Australian Securities and Investments Commission v King

Matthew Brady QC[1]

In March 2020, the High Court changed the law concerning when a person is an "officer" of a corporation for the purposes of s.9 of the *Corporations Act 2001* (Cth).

Until the decision in *Australian Securities and Investments Commission v King*[2] (***King***), intermediate appellate courts had held that in order for a person to be an "officer" for these purposes, it was necessary that the person acted in an "office" of the company, in the sense of a "recognised position with rights and duties attached to it".[3] The High Court's decision in *King* swept away the limitation on the definition requiring an officer to "act in an office"; instead the courts' future focus should be on whether the putative director has the necessary capacity to affect significantly the corporation's financial standing by reason of his or her involvement in the management of the company, regardless of whether or not the person acts in an office of the company.

Relevant facts

Mr King was the chief executive officer (**CEO**) and an executive director of MFS Ltd. MFS Ltd was a listed public company that was the parent company of an empire of hundreds of separate companies (**MFS Group**) that conducted a wide array of businesses. As part of its business empire, the MFS Group had a funds management and financial services group. This financial services group included a number of managed investment schemes.

The "flagship" managed investment scheme of the MFS Group was the Premium Investment Fund (**PIF**) which by 2007 had more than $750 million in funds under management. MFS Investment Management (**MFSIM**) was the responsible entity of the PIF. MFSIM was ultimately wholly owned by MFS Ltd. MFSIM had its own CEO (Guy Hutchings) and own board. Craig White was an executive director of MFSIM and also was the deputy CEO of MFS Limited – in effect, Mr White was Mr King's deputy and had day-to-day management of MFSIM.

In 2007, the PIF had a $200 million facility with the Royal Bank of Scotland (**RBS**), to be used for the purposes of the PIF investment fund. It was not permitted to be used for the purposes of the wider MFS Group.

By November 2007, other parts of the MFS Group were suffering financial stress. One area of particular concern at that time was the fact that on 30 November 2007, a $250 million facility which had been obtained by the wider corporate group was due for repayment to Fortress Credit Corporation (**Fortress**). That facility was secured by various means,

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[1] The author appeared in this case for ASIC at first instance, in the Queensland Court of Appeal and in the High Court. Another member of Higgins Chambers, Kate Slack, also appeared for ASIC in the Court of Appeal. The law is stated as at 17 June 2020.

[2] (2020) 94 ALJR 293; [2020] HCA 4.

[3] *King v Australian Securities and Investments Commission* (2018) 134 ACSR 105 at 160-161 [246], 161 [249], following what it understood to be the law following the decision of the Full Federal Court in *Grimaldi v Chameleon Mining NL* (No 2) (2012) 200 FCR 296 at 324-325

including a guarantee by MFS Ltd as the parent of the MFS Group. Failure to repay that facility, or to negotiate its deferral, would have been devastating to the future of the MFS Group.

In late November, Mr King negotiated with Fortress for the deferral of a part of the repayment due on 30 November 2007. However, the agreement was that MFS would still repay $103 million of the amount due by 30 November 2007 with the balance being deferred for some months.

The issue then was how the MFS Group was to raise $103 million within the few days left until the end of November and in circumstances where the MFS Group was under considerable financial stress and could not, itself, fund the payment without recourse to further borrowing or a capital raising.

The answer to the MFS Group's problems was provided by PIF. In late November, MFSIM and its senior staff arranged to draw down $150 million from PIF's loan facility with the RBS. Through a series of transactions, ultimately $103 million of that RBS money was paid to Fortress in order to meet the debts of the wider MFS Group, despite the fact that PIF had no liability in respect of the Fortress debt.

In effect, PIF borrowed money on its own investment facility in order to meet the debts of the wider MFS Group. It did so without any consideration being agreed for PIF to prop up the MFS Group and without any documentation at the time of the payments. There was not even a promise of repayment of the $103 million that PIF paid to settle the debts of another part of the corporate empire.

Ultimately the MFS Group collapsed in 2008, leaving PIF and its investors with a significant shortfall in light of PIF's money which had been used to support the wider MFS Group.

ASIC's proceedings against Mr King

ASIC commenced proceedings against MFSIM and also 5 individuals involved in these transactions alleging contraventions of the *Corporations Act* in relation to the $103 million payment, as well as another later payment which is irrelevant for present purposes. ASIC also alleged that various false documents were later created in order to effectively "cover up" the subject transactions. ASIC's case against each defendant succeeded at first instance.[4]

Mr King, the MFS Group CEO, was one of the defendants. The case against him was limited to his involvement in the $103 million payment.

ASIC put its case against Mr King in two ways. Firstly, ASIC alleged that Mr King contravened the *Corporations Act* because he was knowingly concerned in MFSIM's contraventions of the Act concerning the $103 million payment. ASIC's argument succeeded at trial and on appeal and was not the subject of any argument in the High Court.

The High Court appeal concerned the second way in which ASIC put its case against Mr King: ASIC contended that Mr King was also liable under s.601FD of the *Corporations Act* as an "officer" of MFSIM.

Thus, the Court was called upon to decide whether Mr King, as the CEO of the MFS Group, breached duties as an officer of one of the MFS Group subsidiary companies, MFSIM, of which he was not a director or executive.

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[4] *Australian Securities and Investments Commission v Managed Investments Ltd [No 9]* (2016) 308 FLR 216 per Douglas J

The relevant statutory provision was s.9 *Corporations Act* which provided:

> *"officer" of a corporation means:*
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> *…*
>
> *(b) a person*
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> > *(i) who makes, or participates in making, decisions that affect the whole, or a substantial part, of the business of the corporation; or*
> >
> > *(ii) who has the capacity to affect significantly the corporation's financial standing; or*
> >
> > *(iii) in accordance with whose instructions or wishes the directors of the corporation are accustomed to act (excluding advice given by the person on the proper performance of functions attaching to the person's professional capacity or their business relationship with the directors of the corporation)…"*

ASIC's case at trial was that Mr King fell within the definition of officer in s.9(b)(ii) of the definition above: that is, he had the capacity to affect significantly the corporation's financial standing.

The primary judge was satisfied that Mr King was an officer of MFSIM because he had the requisite capacity.[5]

The Court of Appeal decision

The Queensland Court of Appeal[6] did not disturb the primary judge's findings of fact as to the nature and extent of Mr King's involvement in relation to the operations of MFSIM. It concluded that Mr King, as MFS Group CEO and an executive director of MFS Ltd, acted as the "overall boss of the MFS Group" and assumed "overall responsibility for MFSIM". Mr King spoke daily with Mr White, who took instructions from Mr King as to proprietary matters of MFSIM's business.[7] Mr King negotiated the variation to the facility agreement with Fortress by which the $103 million became payable. He was in frequent contact with Mr White about efforts that Mr White was making to procure funds by which the $103 million to Fortress could be made. The Court accepted that Mr White would not have allowed PIF's money to be used to pay the Fortress debt without the imprimatur of Mr King.[8]

Despite those findings of fact, the Court of Appeal upheld Mr King's argument that he did not have the capacity to significantly affect MFSIM's financial standing because any capacity he held to affect MFSIM's financial standing did not derive from his occupation of an "office" within MFSIM in the sense of "a recognised position with rights and duties attached to it".[9] In other words, the Court of Appeal held that it was necessary for ASIC to prove that Mr King had acted in such an office of MFSIM in order for him to be an "officer" of MFSIM. As Mr

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5 *Australian Securities and Investments Commission v Managed Investments Ltd [No 9]* (2016) 308 FLR 216 at 345 [769]

6 Morrison and McMurdo JJA and Applegarth J

7 *King v Australian Securities and Investments Commission* (2018) 134 ACSR 105 at 111 [19]

8 *King v Australian Securities and Investments Commission* (2018) 134 ACSR 105 at 141-143 [163]-[169]

9 *King v Australian Securities and Investments Commission* (2018) 134 ACSR 105 at 160-161 [246], 171 [288]

King was the CEO of the parent company MFS Ltd and did not act in any particular office of MFSIM (the subsidiary), he was therefore not an officer of MFSIM.

In reaching that conclusion, the Court of Appeal relied upon what it saw as authority for this interpretation of the meaning of officer in the decision of the Full Federal Court in *Grimaldi v Chameleon Mining NL*.[10]

The High Court decision

The High Court[11] rejected the Court of Appeal's construction of the meaning of "officer" in s.9 *Corporations Act*. It held that Mr King did have the necessary capacity and that he was an "officer" of MFSIM.

In a very detailed judgment, the Court considered the legislative context, the history and purpose of the relevant legislative provisions and concluded that there was no reason to put a gloss on the relevant definition or to depart from a literal interpretation of the text.[12]

Consideration of whether a person falls under para (b)(ii) of the definition of "'officer' of a corporation" requires consideration of the role the person actually played in the management of the corporation.[13] That requires determining whether the person has a capacity to significantly affect a corporation's financial standing by identifying their role in relation to the corporation; what they did or did not (whether on particular occasions or over time) and the relationship between their actions or inaction and the financial standing of the corporation.[14]

Mr King argued that if para (b)(ii) of the definition is read literally, then it would capture persons who are, on any realistic view, unrelated to the management of the company. For example, external consultants or advisors, bankers and even the Commissioner of Taxation are all persons who could have the capacity to affect significantly the financial standing of a particular company and who could be considered therefore to be an "officer" of that company unless the definition was restricted in some way.[15]

The High Court rejected that concern. The definition in s.9 is that of an "officer of a corporation". The words "of a corporation" mean that even where para (b) of the definition of officer is satisfied, it remains necessary to ask whether the person is relevantly "of" the corporation. Questions of fact and degree arise as to whether the putative officer answers the description of being "of" the company in the sense of being engaged, in fact, in the management of its affairs or property.[16] However, it is difficult to see any circumstance in which a party wholly external to the company and having no involvement in its management could answer the description of being "of" the company.

Nettle and Gordon JJ expressly recognised the possibility that "third parties" such as bankers might fall within the reach of the para (b) definition of "'officer' of a corporation". At [96] their Honours noted that the question did not arise directly in the litigation, but that

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10 (2012) 200 FCR 296

11 Kiefel CJ, Gageler, Keane, Nettle and Gordon JJ

12 *Australian Securities and Investments Commission v King* (2020) 94 ALJR 293; [2020] HCA 4 at [24]-[28] per Kiefel CJ, Gageler and Keane JJ; [185] per Nettle and Gordon JJ

13 *Australian Securities and Investments Commission v King* (2020) 94 ALJR 293; [2020] HCA 4 at [39] per Kiefel CJ, Gageler and Keane JJ; [91] per Nettle and Gordon JJ

14 *Australian Securities and Investments Commission v King* (2020) 94 ALJR 293; [2020] HCA 4 at [91] per Nettle and Gordon JJ

15 *Australian Securities and Investments Commission v King* (2020) 94 ALJR 293; [2020] HCA 4 at [38]

16 *Australian Securities and Investments Commission v King* (2020) 94 ALJR 293; [2020] HCA 4 at [39], [96]

lenders managing the way in which a company attempts to work its way out of financial distress may present real issues about the application of these provisions.

In other words, an external party who sufficiently involves himself or herself in the management of the affairs of the company may potentially be exposed to the duties of an "officer" of the corporation in some circumstances.

Consequences of the decision

The immediate consequence of the decision in *King* is that there is no longer a need for the party contending that a person is an "officer" within the meaning in para (b) of the definition to plead and prove that the person acts in an office of the corporation, in the sense of a recognised position with rights and duties attached to it. It is sufficient for a person to be an officer if it is proved that the person had the necessary capacity to affect significantly the financial standing of the corporation and that the person was "of" the corporation in the sense of being engaged in the management of its affairs or property.

The Court's broadening of the test for being an "officer" gives rise to the possibility that persons who are wholly external to the company may be subject to the duties of an "officer" of the company if they are sufficiently involved in its management as to conclude that the person is "of" the company. This potentially involves difficult questions of fact and degree which may ultimately lead to the need for further judicial guidance on the application of this test.