Bruce & Anor v LM Investment Management Limited (Administrators Appointed) & ors
Queensland Supreme Court Proceeding 3383 of 2013
Summary of Court Proceedings

1. Background

1.1 General

On 19 March, 2013, Ginette Muller and John Park of FTI Consulting (Australia) Pty Limited ("**FTI**") were appointed administrators of LM Investment Management Limited (Administrators Appointed) ("**LMIM**").

LMIM is the responsible entity of, relevantly, the LM First Mortgage Income Fund ("**LMFMIF**").

1.2 Suspension of AFSL

On 9 April, 2013, ASIC suspended LMIM's Australian Financial Services Licence, pursuant to s915B(3)(b) of the *Corporations Act* ("**Act**").

However, pursuant to s915H of the Act, ASIC specified that the licence continued in effect as though the suspension had not happened:

(a) for the purposes of the provisions of Chapter 5C (Managed Investment Schemes) and Chapter 7 (Financial Services and Markets) other than the provisions in Parts 7.2, 7.3, 7.4 and 7.5; and

(b) regarding the provision by LMIM of financial services which are reasonably necessary for, or incidental to:

(i) the transfer to a new responsible entity;

(ii) investigating or preserving the assets and affairs of; or

(iii) winding up of,

the LM First Mortgage Income Fund, the LM Currency Protected Australian Income Fund, the LM Institutional Currency Protected Australian Income Fund and four other funds.

2. Court Proceedings

2.1 Bruce Originating Application

On 15 April, 2013 an originating application was filed in the Supreme Court of Queensland by Mr and Mrs Bruce, unit holders [1] in the LMFMIF. It was served on LMIM on or about 19 April, 2013.

By it, Mr and Mrs Bruce sought the following orders:

(a) pursuant to s.601FN and 601FP of the Act (or alternatively, regulation 5C.2.02 of the Corporations Regulations 2001 (Cth)) ("**Regulations**"), that Trilogy Funds Management Limited ("**Trilogy**") (or such other company as the court determines appropriate) be appointed temporary responsible entity of the LMFMIF;

(b) alternatively, pursuant to s.80 of the *Trusts Act* (Qld) 1973, that Trilogy (or such other company as the court determines appropriate) be appointed responsible entity/trustee of the LMFMIF until further order of the court or an extraordinary resolution of the Income Fund's members providing for an alternative appointment.

Trilogy agreed to indemnify Mr and Mrs Bruce for the costs of the proceeding. Mr and Mrs Bruce did not attend court. Several officers of Trilogy swore affidavits and attended court.

2.2 Shotton Application

On or about 29 April, 2013, Mr Roger Shotton, another unit holder[2] in the LMFMIF, filed and served an application seeking the following orders:

(a) pursuant to s.601NF(1) of the Act, that David Whyte (or such other person as the Court may deem appropriate) be appointed to take responsibility for ensuring that the LMFMIF is wound up in accordance with its constitution;

(b) pursuant to s.601ND of the Act, LMIM (in its capacity as the responsible entity of the LMFMIF), be directed to wind up the LMFMIF;

(c) such further directions as the court thinks necessary about how the LMFMIF ought to be wound up.

[1] Mr and Mrs Bruce hold approximately (0.03%) of the total value of units in the LMFMIF.
[2] Mr Shotton holds approximately (0.06%) of the total value of units in the LMFMIF

2.3 ASIC Intervener Application

On 3 May, 2013, the Australian Securities & Investments Commission intervened in the proceeding and filed an interlocutory application seeking the following orders:

(a) pursuant to s.601ND(1) of the Act, LMIM be directed to wind up the LMFMIF;

(b) pursuant to s.601NF(1) of the Act, Derrick Vickers, Darryl Kirk and Gregory Hall (each of PriceWaterhouseCoopers), be appointed to take responsibility for ensuring that the LMFMIF is wound up in accordance with its constitution;

(c) pursuant to s.1101B(1) or s.601NF(2) of the Act, Mr Vickers, Mr Kirk and Mr Hall be appointed as joint and several receivers of the property of the FMIF.

ASIC also sought orders ancillary to those orders.

LMIM, in its capacity as responsible entity of the LMFMIF is the First respondent to each of the three applications. The members of the LMFMIF were the second respondents to the applications.

3. Chronology of Proceeding

3.1 Applications

The Bruce originating application was originally set down to be heard on 29 April, 2013. However, that hearing was unilaterally changed by the solicitors for Mr and Mrs Bruce speaking with the court registry, to 2 May, 2013.

On 2 May, 2013, P. Lyons J ordered that the Shotton application be heard on 13 May, 2013 and, subject to the discretion of the trial judge, that the Bruce originating application be heard on the same date.

In light of affidavit material served 3 May, 2013, on 7 May, 2013 the First Respondent sought and obtained an adjournment of the hearing of the applications until 15 July, 2013, for three days, which were the next available court hearing dates.

3.2 Subpoenas to Produce

On 30 April, 2013, subpoenas were issued by the Supreme Court of Queensland on behalf of the First Respondent, directed to Trilogy, Piper Alderman (Mr and Mrs Bruce's and Trilogy's solicitors), Ms Amanda Banton (the partner with the conduct of the matter at Piper Alderman), KordaMentha Pty Limited and Mr Winterbottom of KordaMentha Pty Ltd.

Applications by Trilogy, Piper Alderman and Ms Banton to set aside the subpoenas were unsuccessful and documents were subsequently produced.

On or about 28 June and 1 July, 2013, subpoenas were issued by the Supreme Court of Queensland on behalf of Mr and Mrs Bruce which sought a wide range of categories of documents. At a hearing to set aside the subpoenas, the categories were amended to reduce the scope of the documents sought. Nonetheless, a large number of documents were still required to be produced by FTI and LMIM in response to the amended subpoenas.

4. The Hearing

Ultimately, the hearing of the Originating Application, the Shotton Application and the ASIC Application was held on 15, 16 and 17 July before Dalton J.

Her Honour has reserved her decision.

Prior to the hearing, written submissions were filed on behalf of each of the parties, which were supplemented by oral submissions during the hearing.

A number of issues were covered by the four parties, over three days.

The main arguments for each of the parties are summarised below, to provide an overview of the positions of the parties. The summaries are not exhaustive, comprehensive lists of all the arguments that were raised.

Copies of the full transcripts of the hearing are available from Auscript, via the Supreme Court of Queensland.

4.1 Bruce Submissions

(a) Trilogy should replace LMIM as the responsible entity of the LMFMIF because:

(i) LMIM does not have an Australian Financial Services Licence that meets the requirements of s.601FA of the Act, because the terms of the suspended AFSL are such that LMIM is not able to "operate" the scheme to the required full scope. The word, "operate" means to operate with the full suite of powers and duties of the scheme;

(ii) the power under s.601FN of the Act for a registered member to apply to the court for the appointment of a temporary responsible entity under s.601FP has been enlivened;

(iii) the appointment of Trilogy as a responsible entity is "in the interests of members" under s.601FP;

(b) regulation 5C.2.02 of the *Corporations Regulations* provides an alternative basis upon which Trilogy may be appointed as the responsible entity. The appointment of Trilogy under regulation 5C.2.02 is necessary to protect the interests of members;

(c) other grounds upon which LMIM's AFSL is liable to be suspended or cancelled are:

(i) LMIM had not lodged the scheme's financial report for the half-year ending 31 December, 2012 by 15 March, 2013; and

(ii) the administrators are investigating whether the prepayment of managements fees alters the Net Tangible Asset requirements of the AFSL;

(d) LMIM's AFSL is still susceptible to cancellation because ASIC has not said it will not cancel it. ASIC has said it is not right to have an insolvent company as responsible entity and LMIM is heading towards insolvency. It is a condition of the AFSL that the responsible entity be able to pay their debts as and when they fell due. The court should not lend its aid to enable a bankrupt to continue as responsible entity;

(e) if Trilogy is the responsible entity of the LMFMIF, there is not a certainty of insolvency of the responsible entity, which means the AFSL held by the responsible entity is not under risk of being cancelled and there is not a responsible entity which seems to have engaged in deteriorating relations with the regulator;

(f) the LMFMIF should be wound up;

(g) the Bruces are opposed to the appointment of receivers. The LMFMIF is not insolvent but is illiquid;

(h) receivers should not be appointed to the LMFMIF, including for the reason that doing so would introduce unnecessary costs;

(i) in relation to the meeting of members to consider and vote upon the resolutions to remove LMIM as the responsible entity and appoint Trilogy as a temporary responsible entity of the LMFMIF:

(i) the meeting was not called upon a proper statutory basis;

(ii) the meeting was only called by the custodian of the assets of the LM Currency Protected Australian Income Fund (which is a member of the LMFMIF), at the direction of LMIM, to generate evidence for the purpose of the hearing and to achieve a forensic advantage;

(iii) the meeting was called upon an artificial basis, which was not disclosed to members of the LMFMIF;

(iv) Trilogy did not consent to being appointed as the new responsible entity as a result of the voting at the meeting;

(v) Trilogy preferred the issue to be determined by the court;

(j) members of the LMFMIF were not told, but should have been told, ASIC's views that the meeting of members was called for an ulterior purpose for forensic advantage, was a waste of money and lacked utility;

(j) if Trilogy is appointed as the temporary responsible entity of the LMFMIF, it is obliged to call a meeting of members within 3 months to appoint a permanent responsible entity and at that time a valid meeting could be called to canvass the views of members, which may lead to a different outcome to the outcome of the meeting of members on 13 June, 2013. No other relief that is sought provides the opportunity for members to have a say;

(k) under the LMFMIF constitution LMIM, as responsible entity, is entitled to charge a management fee of up to 5.5% (including GST) of the net fund value;

(l) the voluntary administrators have not obtained updated valuations of the assets of the LMFMIF, which would allow a higher calculation of management fees;

(m) the management fee when LMIM was the responsible entity prior to the appointment of liquidators, was higher in value than perhaps it should have been, which may give the LMFMIF a claim against LMIM and/or a claim against LM Administration Pty Ltd ("**LMA**");

(n) although the administrators have said they do not intend to charge the management fee, there is no document to record that arrangement. In relation to LMA, it would not be in its interests, or in the interests of LMA's creditors to give away that right;

(o) the fees Trilogy will charge have been put into evidence, at a set rate cascading down as the assets are realised. Trilogy will charge the lesser of the 1.5% it has said it will change and 5% under PWC's rates;

(p) the work that has been undertaken by the voluntary administrators since their appointment can be used by Trilogy if it is appointed as the temporary responsible entity of the LMFMIF, so that work will not be wasted or duplicated;

(q) the risk of increased costs if LMIM remains the responsible entity is greater than the risk of increased costs if Trilogy is appointed as the temporary responsible entity;

(r) the voluntary administrators have not investigated potential claims against LMIM and its former directors in relation to, for example:

  (i) the amendments made to the LMFMIF constitution, that permitted the increase of the loan to value ratio for investments by the LMFMIF, which was inappropriate; and

  (ii) related party transactions;

(s) prior to the appointment of the administrators, there has been an increase in the loan to value ratio and there were related entity payments;

(t) Trilogy is the responsible entity of the LM Wholesale First Mortgage Income Fund and therefore owns 20% of the LMFMIF. If Trilogy is the responsible entity of the LMFMIF, it must act in the interests of the unitholders and would pursue all appropriate claims.

(u) contrary to the suggestion made in the proceeding, Trilogy is not insolvent;

(v) Trilogy should be permitted to undertake the winding up of the LMFMIF because it is an experienced responsible entity. It is familiar with other schemes and is experienced in property of the nature of the assets of the LMFMIF and its sort of mortgage portfolio. Trilogy is familiar with the LMFMIF as it has been looking at it since 2012;

(w) LMIM is facing substantial potential conflicts:

(i) as responsible entity it must act in the interests of members of the main fund;

(ii) as responsible entity of feeder funds, it must act in the interests of members of those funds;

(iii) when LMIM goes into liquidation, there will be duties owed to creditors, which are not necessarily coincident with duties owed to unitholders;

(x) the conflict issues are not present if Trilogy is appointed as the responsible entity of LMFMIF;

(y) the access to the books and records that was offered to the solicitors for the Bruces and Trilogy by the solicitors for LMIM is not the same as if Trilogy was acting in the role as responsible entity;

4.2 Shotton Submissions

(a) Mr Shotton does not support the appointment of Trilogy to replace LMIM as the responsible entity of the LMFMIF, including because:

(i) there is no statutory power to appoint Trilogy as the new responsible entity. The jurisdiction is not enlivened because the LMFMIF has a current responsible entity and an AFSL;

(ii) Trilogy has not identified any good reason why a new responsible entity should be appointed;

(iii) the LMFMIF should be wound up;

(iv) a new responsible entity would be entitled to charge up to 5.5% of the value of the assets under management (said to be approximately $300 million). Although Trilogy has said it will charge a management fee of 1.5% per annum, doing so is not in the interests of members;

(v) the members voted at a meeting of members on whether Trilogy should be appointed as the new temporary responsible entity and that resolution was resoundingly defeated;

(vi) save for possible conflicts that have been indentified, there is no good reason to appoint a new responsible entity. It is not in the interests of members to do so;

(vii) winding up the LMFMIF will avoid the costs of undertaking an annual audit;

(viii) the appointment that is sought is as a temporary responsible entity only. A further meeting will be required to appoint a permanent responsible entity, at further cost;

(ix) Trilogy is not an appropriate new responsible entity as it has a conflict of interest because it is also the responsible entity of one of the feeder funds into the LMFMIF, namely the LM Wholesale First Mortgage Income Fund. This is also relevant to any claims brought in the future against LMIM and any of its directors;

(b) the voluntary administrators have informed the court of their intention to wind up the LMFMIF;

(c) the identity of the responsible entity is a matter within the discretion of the court;

(d) the LMFMIF should be wound up by LMIM, acting as the responsible entity of the LMFMIF, upon the ground that it is just and equitable to do so;

(e) there is no limit on the matters which the court may take into account in determining whether to appoint a person other than the responsible entity to conduct the winding up, other than that the power must be exercise by reference to the subject matter, scope and purpose of the legislation which created it (namely the LMFMIF constitution);

(f) FTI should not conduct the winding up, because of possible conflicts of interest, including in relation to:

(i) the management fee structure;

(ii) the feeder fund potential conflict as LMIM is also the responsible entity of the LM Currency Protected Australian Income Fund and the LM Institutional Currency Protected Australian Income Fund;

(iii) LM Administration Limited, as FTI is also the administrator of it;

(iv) the investigation of related party transactions;

(g) it is necessary in the interests of members to have Mr Whyte appointed, because of the potential conflicts Mr Shotton has identified;

(h) in seeking the appointment of Mr Whyte as the person to take responsibility for the winding up of the LMFMIF, Mr Shotton is relying upon a similar approach taken in the decision of *Equititrust Limited v The Members of the Equititrust Income Fund* [2011] QSC 353;

(i) a special purpose liquidator could be appointed;

(j) the capital distribution to members should not have been paid and the funds should instead have been applied to reduce the debt owing to Deutsche Bank;

(k) if Mr Whyte is appointed to conduct the winding up, he will utilise as much of the work undertaken by FTI as possible, to avoid duplicating the work and costs;

(l) the fact the administrators have been working in that role for a few months should not be treated as reflecting they are entrenched in that position to preclude the appointment of Mr Whyte.

4.3 ASIC Submissions

(a) the Bruce's application should be dismissed because there is no statutory or other basis upon which the court can order, on that application, the change of the responsible entity to Trilogy;

(b) s601FA does not require an AFSL to permit the full exercise of all powers provided under the constitution of the scheme;

(c) as long as the AFSL held by the first respondent permits those acts which constitute "*the management of or the carrying out of the activities which constitute*" the LMFMIF, then it will permit the first respondent to operate the LMFMIF;

(d) the first respondent has met the requirements of s601FA and accordingly the power granted to the court under s601FN is not available;

(e) Regulation 5C.2.02 should not provide an alternative avenue of relief for the Originating Application;

(f) there is no ability for an application by a minority of scheme members under s80 of the *Trust Act*.

(g) the LMFMIF should be wound up because:

(i) the LMFMIF has been closed since 2009;

(ii) the annual report for the year ending 30 June, 2012 indicated that during the reporting period the first respondent announced that the LMFMIF would not reopen;

(iii) the first respondent has determined under s601NC of the Act that the purpose of the scheme cannot be accomplished and that it should be wound up;

(iv) the suspended AFSL permits only the transfer to another responsible entity or the winding up and as LMIM is not retiring as the responsible entity, the only available option is to wind up the LMFMIF;

(h) the winding up should be carried out by ASIC's nominees because:

(i) the "zealousness" of LMIM's response to the Originating Application appear to have distracted it from focusing on the interests of members and complying with its suspended AFSL;

(ii) LMIM has rejected the opportunity to enter into an enforceable undertaking proposed by ASIC;

(iii) the person(s) responsible for the winding up should be appropriately independent to ensure that the winding up proceeds in the most efficient and cost effective way to provide the best chance of achieving the maximum return for investors;

(i) in relation to the meeting of members:

(i) the use of the procedures in Part 2G.4 of the Act was inappropriate;

(ii) the meeting had to be called by a person who could cast votes on the resolutions. The meeting was called by the custodian, Trust Company, which is the custodian of the LM Currency Protected Australian Income Fund. LMIM is the responsible entity of the LMCPAIF. The responsible entity and its associates are not entitled to vote. Trust Company is an associate of LMIM. Trust Company requisitioned the meeting at the direction of LMIM;

(iii) the meeting was not a meeting called under s.601FL because LMIM did not intend to retire as the responsible entity of the LMFMIF;

(iv) the administrators' level of engagement in the adversarial process is surprising;

(v) the calling of the meeting of members was not authorised by the suspended AFSL;

(vi) the notice of meeting was misleading, although this submission was substantially withdrawn;

(j) in relation to the notice of meeting provided to members:

(i) the notice states that if a liquidator is appointed, and assuming it is the administrators, they will have powers of clawback that liquidators have, to undo transactions which have been entered into by the company. That is misleading. They are not liquidators. Anything recovered in so called clawback transactions goes to the responsible entity. There is no reason to assume there are such claims. It was misleading to suggest that this was some benefit without actually identifying or having made enquiries about that facts that there might be such claims;

(ii) the notice of meeting did not say LMIM had an interest in continuing to be the responsible entity of the LMFMIF, because it would have been entitled to fees;

(k) the responsible entity is a trustee of the LMFMIF for members. Faced with the application by Trilogy to replace it, LMIM should have come to the court for advice as to whether or not it should close the Trilogy application. If it had done so, it would have been told to call a meeting at which it said it wanted to resign, or to wind up the fund and would have avoided fighting the application as it has done, at the expense of the LMFMIF;

(l) the litigation has not been defended to protect members. It has been done by a responsible entity who was required to retire fighting a person that wanted to take its place;

(m) ASIC is concerned that the "zealousness" of the first respondent's conduct of the proceeding is disproportionate to the extent to which the interests of unit-holders of the scheme are likely to be advanced, as evidenced, for example, by the volume of affidavit material produced;

(n) section 1101B of the act is invoked by the first respondent's breach of s.320 in failing to lodge a financial report for the half year ending 31 December, 2012, by 15 March, 2013;

(o) the fees proposed to be charged by Messrs Vickers, Kirk and Hall are significantly less than the fees proposed to be charged by the administrators and by Mr Whyte;

(p) the insolvency practitioners proposed by ASIC have not been criticised by any party.

4.4 First Respondent's Submissions

The submissions below have been set out for to reflect the submissions made in response to the other parties' submissions. However, a number of points made on behalf of the First Respondent related to submissions made by more than one party.

(a) the first respondent's primary position is that all the applications against it should be dismissed;

4.4.1 Re: Originating Application by Mr and Mrs Bruce

(a) there is no statutory basis to order that Trilogy replace LMIM as the responsible entity of the LMFMIF, under the Act or the Regulations;

(b) even if there was, the discretion contained within s.601FP means such an order should only be made when it is in the interests of members to do so, which is not the present case;

(c) Mr and Mrs Bruce did not raise any complaint about LMIM acting as responsible entity in the three years after 2009, when the LMFMIF ceased accepting new investments and froze the redemptions. If they did have concerns during that time, the concerns would not survive the appointment of the voluntary administrators. The evidence does not support any sound basis for the concerns expressed by Mr and Mrs Bruce;

(d) the primary basis upon which the Bruces (and Trilogy) now rely is the assertion that an independent party is required to investigate potential claims against LMIM on behalf of the members of the LMFMIF;

(e) The administrators have a statutory duty to investigate the conduct of the directors of LMIM. They are currently undertaking those investigations;

(f) Trilogy has standing to bring proceedings against LMIM and its former directors, if there is sufficient evidence. However, the Bruces and Trilogy want investigations they wish to pursue to be funded by all members of the LMFMIF and Trilogy wishes for its fees to be paid by the other members of the Fund, for investigations it wants conducted in the interests of the Fund, of which it will be the responsible entity, if appointed;

(g) where a member asserts a claim against a responsible entity, then primarily, the member should investigate and substantiate that claim;

(h) the suggestion that LMIM suffers from a conflict of duty and duty or duty and interest, because of related party transactions, has no foundation;

(i) the constitution of LMIM has provided for the payment of management fees by the LMFMIF to LMIM. There is no evidence, nor any expression of concern by any witness, that the fees were ever exceeded;

(j) complaint is made regarding amendments made to the LMFMIF constitution, in relation to the loan to value ratio. There is no suggestion that any of the loans made by LMIM were made in breach of the provisions of the constitution. Property values on the Gold Coast have declined, which has adversely affected loan to value ratios;

(k) the ASIC regulatory guide upon which Mr Wood, on behalf of Trilogy relied, regarding loan to value ratios has no force of law. Additionally, it refers to the loan to value ratios at the time the loans were made;

(l) although the administrators have not closed their minds to the matters of concern asserted by Mr Wood, nothing has yet emerged from their investigations to substantiate those concerns;

(m) at least at this stage, there is insufficient evidence to establish:

(i) the members of the LMFMIF have any claims against LMIM;

(ii) Trilogy has been precluded from investigating the alleged claims by being unable to access the books and records of LMIM;

(iii) the administrators are unwilling or unable themselves to investigate the matters raised by Mr Wood;

(iv) the appointment of a new responsible entity to investigate the matters raised by MR Wood is necessary or in the interests of members;

(n) LMIM is not in breach of the net tangible asset requirements of its AFSL. ASIC has not taken any action regarding any purported infringement. The contention that the net tangible asset requirement has been contravened is based on an erroneous assumption. The opinion of the Bruce's expert witness about the net tangible assert position is based upon assumptions which have not been proved;

(o) there is no evidence to suggest the assets of the LMFMIF are in jeopardy;

(p) LMIM, through the administrators, has the benefit of detailed knowledge of the LMFMIF and its assets. A substantial amount of work has been undertaken by the administrators and their staff in reviewing the affairs of the LMFMIF, including a detailed review of the individual assets of the LMFMIF. They have developed a plan for the development and disposal of those assets, repayment of the loan facility with Deutsche Bank and a return of capital to members within the shortest possible timeframe;

(q) if a replacement responsible entity is appointed, there is likely to be a significant duplication of work and wasted costs as the new responsible entity becomes informed about the matters already known to the LMIM, as responsible entity, via the administrators' work;

(r) if Trilogy was appointed as the new responsible entity, in order to go into possession of property to enforce LMIM's securities, it would need to appoint qualified person, registered liquidators, as receivers and controllers, which would incur costs in addition to the management fee of 1.5% Trilogy proposes to charge as responsible entity. If LMIM remained as the responsible entity, the administrators see no need to incur the cost of other insolvency practitioners;

(s) the administrators have sworn evidence that they do not intend to charge any management fee and will charge only their usual rates (which will be subject to review by creditors and the courts);

(t) the court has the benefit of the views of members on whether LMIM should be removed as responsible entity and replaced by Trilogy as responsible entity of the LMFMIF. Members who attended the meeting of members on 13 June, 2013 voted overwhelmingly against each resolution;

(u) there can be no reasonable criticism of the meeting of members being called. The meeting of members was convened for the purpose of providing members with an appropriate forum in which they could express their views on whether LMIM should be removed as the responsible entity and whether Trilogy should be appointed as the new responsible entity;

(v) the identity of the responsible entity of the LMFMIF is an important matter and it is entirely appropriate to consult members about their views;

(w) Trilogy had the opportunity to provide members with information for the purpose of considering the resolutions;

(x) by withdrawing its consent to be appointed as the responsible entity of the LMFMIF, had the vote carried that resolution at the meeting of members that was held, Trilogy spurned the process and was trying to frustrate it by absenting itself from the process. However, the vast majority of members opposed the resolutions to replace LMIM with Trilogy. It was not wrong and certainly not evidence of bad faith and certainly not misleading or deceptive for the administrators to hold out to the members of the LMFMIF their genuine belief that there was a prospect of the meeting of members saving costs;

(y) Trilogy has claimed that if it was appointed as a temporary responsible entity, then within 3 months it would call a meeting of members, at which time the members' views would be obtained as the identity of the permanent responsible entity. However, that will only occur if the litigation brought by the Bruces is successful. In fact, the meeting called by the first respondent was the only opportunity for members to decide between Trilogy and LMIM to act as the responsible entity of the LMFMIF. Accordingly, the criticism about the calling of the meeting is misconceived;

(z) the evidence suggests the originating application was brought with a view to commencing legal proceedings against LMIM. The solicitors for Mr and Mrs Bruce also act for Trilogy. They have advertised that they intend to bring a class action

against LMIM. Trilogy has provided an indemnity to the Bruces for the costs of the originating application;

(aa) the jurisdiction of the court to appoint Trilogy as temporary responsible entity has not been engaged and even if it had, discretionary factors heavily weight against making such an order;

(ab) the originating application in respect of the *Trusts Act* is not pressed by the Bruces.

4.4.2 Re: Shotton Application

(a) LMIM does not dispute that the LMFMIF should be wound up. The question is whether that winding up should be conducted by LMIM (through the Administrators) or by a new insolvency practitioner appointed under s.601NF of the Act, to take responsibility for ensuring that the LMFMIF is would up in accordance with its constitution;

(b) section 601NF(1) confirms a discretion of the Court to appoint a person to take responsibility of the winding up of the scheme, but only if the Court thinks it is "necessary" to do so;

(c) the words in s.601NF(1), "*take responsibility for ensuring that the scheme is wound up in accordance with its constitution*" change their shape as the circumstances require. Combined with the word "necessity", s.601NF(1) is directed at extreme circumstances;

(d) the suggested appointed under s.601NF(1) will be "necessary" only in circumstances where it has been demonstrated the responsible entity, for some reason, is unable or unwilling to wind up the scheme in accordance with the constitution and any relevant orders;

(e) no party has shown that an appointment under s.601NF(1) is necessary. LMIM is under the control of administrators who are experienced insolvency practitioners and independent of former management of LMIM;

(f) similarly, s.601NF(2) provides that a court may give directions about how a registered scheme is to be wound up if the court thinks it is "necessary" to do so;

(g) the power to give directions about how a registered scheme is to be wound up, contained in s.601NF(2) is not the kind of language that would ordinarily be associated with a grant of a power to the Court to alter propriety relationships in relation to property by imposition of a receivership and to create compulsory agency relationships between the responsible entity and third parties. A receiver takes control of property to deal with it to effect the purposes of the appointment, typically, to realise the assets under the receiver's control as agents of the owner and to pay the proceeds to the persons entitled. A receiver appointed under s.601NF(2) would be an agent for the responsible entity. However, there is no suggestion that LMIM would be in any way incapable or inappropriate as a person to perform the tasks that

could otherwise be undertaken by a receiver. Accordingly, the role of a receiver does not add anything to what could be done by LMIM.

(h) doing all the sorts of property management and realisation work that is done by all kinds of insolvency practitioners and can be done by LMIM under its current administrators or liquidators, should they become appointed. The only point at which the receiver appears to do something that is different is in conducting litigation, not generally, but specifically, against LMIM;

(i) the whole receivership structure is directed at creating an advantage for the unit holders in one respect and that is if it comes to a situation where LMIM, as responsible entity, wants to sue LMIM in its personal capacity. That job would be done by a receiver, otherwise, everything that is to be done by the receiver could conveniently and properly be done by LMIM, without the receivers. The relief that is sought overreaches. A simple and once and for all mechanism to deal with the possible conflict, if it arises, has been proposed by the administrators, namely, to appoint a special purpose liquidator to the company, the liquidation being the liquidation of all of its assets other than the assets that it has as a responsible entity;

(j) Mr Shotton has not demonstrated any basis for his concern about the independence of the administrators. The administrators have a statutory duty to investigate the conduct of the directors of LMIM and are currently undertaking those investigations. The administrators have a statutory duty to investigate the conduct of the directors of LMIM and are currently undertaking those investigations. The administrators have no difficultly investigating and pursuing arguable and costs effective claims against any current or former officers of LMIM. Although the administrators have not closed their minds to such matters, nothing has yet emerged from their investigations to substantiate any concerns. If any conflict between LMIM and LMFMIF arises, the administrators are willing to seek to appoint special purpose liquidators to the assets of LMIM;

(k) there is no suggestion that LMIM, being in control of the assets of the LMFMIF, is putting them at risk in any way or undertaking any mismanagement;

(l) since their appointment, the administrators have not caused LMIM to charge any management fee from the assets of the LMFMIF and nor do the administrators intend to cause LMIM to charge the LMFMIF such management fees in the future;

(m) Mr Shotton has complained about the capital distribution recently paid to members of the LMFMIF. However, that capital distribution was paid because:

(i) using that money would not have reduced the interest payable under the Deutsche Bank facility; and

(ii) LMIM had informed members, prior to the appointment of the administrators, that the distribution would be paid and the administrators expected that many members had budgeted to receive those funds. No other member has complained about the interim capital distribution;

(n) Mr Shotton has asserted that LMIM is a significant debtor of the LMFMIF, so that the interests of the responsible entity in winding up the LMFMIF would be in conflict of the interest of members. However, there is no evidence that LMIM is a significant debtor of the LMFMIF. No such indebtedness was recorded in the audited accounts of the LMFMIF as at 30 June, 2012 and a management balance sheet for the LMFMIF, as at 31 March, 2013, shows that the LMFMIF actually owes LMIM a small sum;

(o) Mr Shotton asserts that it is not appropriate to put the recovery of bad loans in the hands of the party (LMIM) which arranged the loans. However, the administrators are experienced insolvency practitioners who are independent from the directors of LMIM. Mr Shotton has not identified any valid basis to impugn the conduct of the administrators in managing the affairs of the LMFMIF since their appointment and, ultimately, resolving to wind up the LMFMIF;

(p) Mr Shotton's assertions that the administrators have delayed the hearing of Mr Shotton's application is rejected. The proceedings were subject to several lengthy directions hearings and the need for adjournments was caused by the late delivery, on two occasions, of affidavit material by the Bruces;

(q) against the weak arguments raised by Mr Shotton for seeking the appointment of an insolvency practitioner under s.601NF the Court must consider the potential detriment that would be caused to members if such an appointment was made.

(r) the loss of knowledge which the administrators and their staff have acquired concerning the affairs of the LMFMIF and the appropriate strategy to be adopted in winding up the LMFMIF, would be a significant detriment. Any practitioner appointed under s.601NF would necessarily have to spend time undertaking similar investigations to gain the same level of familiarity already possessed by the administrators and their staff, which will:

    (i) lengthen the winding up process;

    (ii) increase the costs of the winding up; and

    (ii) reduce the return to members.

    LMIM relies on its submissions in connection with the Bruces' application regarding the duplication of work and increased costs associated with the appointment of another person;

(s) the orders that are sought by Mr Shotton and ASIC go well beyond what is necessary to overcome any of the difficulties that have been the subject of the submissions;

(t) Mr Shotton's application ought to be dismissed.

(u) the matters that have been raised by Mr Shotton against LMIM have not established "necessity" for the purposes s.601NF(1) nor s.601NF(2).

4.4.3 Re: ASIC Application

(a) ASIC's application for an appointment to be made under s.601NF should also be dismissed upon the same basis of the application made by Mr Shotton. It has not been demonstrated the appointment is "necessary";

(b) ASIC's submissions do not go close to establishing that to ensure that the LMFMIF is wound up in accordance with its constitution, it is "necessary" to make an order of the kind that ASIC seeks. LMIM is under the control of administrators, who are experienced insolvency practitioners and are independent of the directors of LMIM. ASIC has not provided a sufficient basis to conclude it was necessary for the Court to make an appointment under s.601NF(1);

(c) the circumstances of the LMFMIF are very different to those which led Applegarth J to make an appointment under s.601NF(1) in *Re Equititrust Ltd.* In that case, the proposed en masse resignation of the directors of the scheme, upon the expiration of the insurance cover, coupled with the fact that the Court's jurisdiction to appointment a responsible entity had not been engaged, necessitated the appointment under section 601NF(1);

(d) when ASIC suspended LMIM's AFSL on 9 April, 2013, ASIC specifically declared that the licence would remain effective insofar as required to permit LMIM to wind up the LMFMIF. Nothing has occurred since that time to justify a change in that position;

(e) although ASIC has relied on LMIM's failure to lodge half yearly accounts in breach of the Act as a ground for the appointment of receivers under s.1101B, LMIM does not understand that ASIC contends that the breach is a reason why it is necessary for the Court to make an appointment under s.601NF. Such a submission could not be sustained. That breach occurred on 15 March, 2013, before the administrators were appointed. It was notified and explained to ASIC following the appointment of the administrators. Despite that notice, prior to bringing its application, ASIC did not take any further issue with the reported breach. The administrators have made arrangement for the annual financial report for the LMFMIF to be prepared, audited and provided to members from three months after the end of the 2013 financial year;

(f) in relation to ASIC's application for the appointment of receivers to the assets of the LMFMIF under s.1101B, upon the basis that LMIM breached the Act in failing to lodge half of the yearly accounts:

(i) after learning of the default, ASIC modified LMIM's AFSL, to require it to either wind up the LMFMIF or to appoint another responsible entity to manage it, and gave a period of two years within which to do so;

(ii) while the breach may enliven the Court's jurisdiction to make an order under s.1101B, ASIC does not provide any sufficient basis for the exercise of the discretion to appoint receivers;

(iii) the power of the Court to appoint receivers is a remedial power directed towards the protection of assets. Moreover, s.1101B expressly provides

that such an order can be made only if the Court is satisfied that the order would not unfairly prejudice any person;

(iv) while there may be a theoretically power under s.1101B to appoint receivers of the kind that are sought, making such an order is not a proper remedial response to the contravention that has been established, which is simply a failure to lodge accounts in a timely way by persons who are no longer in control of the company;

(g) any general equitable power for the Court to provide relief has not been engaged. No-one has sought relief on that basis and if it were sought it would raise its own questions as to whether it was appropriate;

(h) there is no justification for an appointment of receivers in this case where there is no evidence the assets of the LMFMIF are in jeopardy;

(i) the first respondent rejects ASIC's criticism of the first respondent's alleged "zealousness" in relation to these proceedings. It specifically denies that the administrators, in conducting the proceeding, have not kept up and done all the things that they had to do in relation to the administration of the funds. There is no evidence to support the assertion that, by reason of this proceeding, the administrators have been distracted from properly focusing on the administration of the Funds;

(j) the work that has been undertaken is set out in detail in the evidence of Mr Corbett. It includes:

(i) undertaking a comprehensive strategy review, including a detailed analysis of financial and developmental positions for each asset;

(ii) seeking, obtaining, collating and reviewing information from the records about the loan and mortgage arrangements, proposes for development for each property;

(iii) physically inspecting each property to:

(A) understand its physical characteristics;

(B) assess the proposed development;

(C) identify opportunities that might be available to provide value;,

(D) consider whether the existing development proposals are appropriate, given the appropriate timeframes, market conditions and need to optimise returns as quickly as possible;

(iv) developing individual cashflow models for each asset, which feed into an overarching cash flow model, which plans the entire workout of the fund, development of the underlying properties to maximise profitability and repayment in full of the Deutsche Bank facility with a minimum of interest;

(k) although ASIC has raised concerns about the calling of the meeting of members:

(i) LMIM had the power to call the meeting under its constitution. Specifically, clause 28.1 gives the power to call a meeting for any purpose;

(ii) it would be wrong to attribute to LMIM any improper motive in calling the meeting of members;

(iii) LMIM considered it was important for members of the LMFMIF to be given an opportunity to vote on which company they wish to have act as responsible entity;

(iv) the administrators completely reject the suggestion that it was inappropriate to call and hold the meeting;

(v) even if the only possible consequence of the meeting was to ascertain the wishes of members about whether there should be a change of responsible entity from LMIM to Trilogy, consulting the members and obtaining their views was an entirely appropriate thing to do. The whole of chapter 5C proceeds on the basis that the views of members at every vital point are significant;

(vi) on Tuesday, 23 April, 2013 there was a meeting between representatives of ASIC and representatives of the first respondent. During the course of that meeting Ms Muller said that she would be able to form a view about whether to wind up the LMFMIF, within two weeks of that meeting. On Monday, 6 May, 2013, the administrators decided to wind up the LMFMIF. Monday, 6 May, 2013 is within 2 weeks of Tuesday, 23 April, 2013;

(vii) further, the draft enforceable undertaking prepared by ASIC records that:

(A) the administrators offered to cause LMIM to convene meetings with the unit holders of all of the LM funds in a timely manner, to provide unit holders with an opportunity to determine the future of the LM funds quickly, efficiently and with minimal expense to the LM funds; and

(B) at the meetings the resolutions put to unit holders will include resolutions for:

(I) the appointment of a responsible entity over each of the funds; and
(II) whether the funds should be wound up.

ASIC was planning on proceeding on the basis that the licence was only then very recently amended and committed the calling of the meetings;

(viii) it was a perfectly natural course for a meeting of members to be held, particularly given ASIC was asking the administrators to execute an enforceable undertaking to call a meeting of members to consider:

(A) winding up the LMFMIF; and

(B) the replacement of the responsible entity.

There is no question, as far as ASIC was concerned, that there should be a meeting of some kind. They wanted a meeting and asked for an enforceable undertaking to give rise to it. ASIC has no doubt about the power to call the meeting because under the constitution the responsible entity was entitled to call a meeting of members. The meeting only considered the replacement of the responsible entity;

(ix) when an application is made to the court to remove a liquidator, where it is only the court that has the power to do it, the court will often direct a meeting be held to find out the views of creditors. Those views have no legal operation, it is just a poll;

(x) under the Act there are two possible routes to obtain a resolution that will have legal effect:

(A) s.601FL concerns the retirement of the responsible entity; and

(B) s.601FM operates where there is a wish of members for the responsible entity to be removed.

A meeting called other than under those routes that results in a resolution of the kind proposed is simply an expression of the views of the members, that is, it is a poll;

(xi) ASIC has criticised the use of s.601FL. It is the case that LMIM did want to retire if the members voted in favour of the resolution. That is giving a purposive effect to the section rather than a narrow literal one;

(xii) the mechanism that was adopted, of LMIM directing the custodian to issue the request for the meeting, which was said to enliven s.601FM, was done to create the possibility that if the resolution was passed, LMIM would be removed. That was the only purpose of calling the meeting in

that way, that is, to ensure the meeting could fall within the provisions of the Act. As state, if the meeting didn't come within the provisions it would be a poll only. The whole point of trying to ensure the meeting fell within the statutory provisions was to create the risk that LMIM would be removed. Once that is understood, the force of the objections made by ASIC and Mr Shotton disappear.

(xiii) it is said that the calling of the meeting was merely a device to produce evidence for the Court. That theory has no explanatory power. LMIM went to a lot of trouble to try and make the outcome of the meeting binding if the resolution was passed. If the resolution failed it doesn't matter if the sections were engaged or not; the engagement of the sections only mattered if the resolution passes. Rightly or wrongly LMIM went to a lot of trouble to try and engage them and that attempt is only consistent with a desire to see the meetings as a mechanism for giving effect to the wishes of the members;

(xiv) ASIC has asserted that LMIM's AFSL did not give it power to call the meeting. In fact, the licence extends to the provision of financial services reasonably necessary for, or incidental to, a transfer to a new responsible entity and investigating or preserving the assets or affairs of the LMFMIF, including the affairs of a winding up. Accordingly, calling a meeting to consider the removal of LMIM as responsible entity and its replacement by Trilogy is plainly within the terms of the licence;

(l) in respect of ASIC's objection that Part 2G.4 was not properly engaged because the meeting of members was called by the custodian of one of the funds, at the direction of LMIM:

(i) LMIM has the power under the constitution of the LMF MIF to call a meeting. Once a meeting has been called, there is no power to cancel that meeting. If there is an extraordinary resolution of the members on a topic such as LMIM should be removed and replaced by Trilogy as the responsible entity, then that result will have been effective by virtue of s.1322(2) of the Act, which cures any irregularity, unless there is substantial prejudice to someone, and in this case there would not have been;

(ii) for the purposes of s.15 of the Act, the custodian was not acting "in concert" with LMIM in calling the meeting:

(A) if the custodian was acting in exercising independent discretion pursuant to their powers as a fiduciary at someone else's request, that is not "in concert";

(B) if it is at their direction, it is not "in concert";

(iii) s.12 is the relevant section and it does not make the custodian an associate of LMIM;

(m) although ASIC has raised concerns with LMIM about material sent to members in connection with the meeting held on 13 June, 2013, LMIM responded to those concerns by issuing further materials to members;

(n) ASIC's allegation that LMIM has "launched a very expensive litigation", is rejected. The first respondent is the respondent to three applications. The issues in the case, save for one or two exceptions and that have been disposed of, have been raised by the other parties, not by the first respondent. The first respondent must respond to the matters raised by the other parties, across a wide range of issues. The first respondent did not launch a very expensive litigation;

4.4.4 Re Potential Conflicts

In relation to the arguments put by the parties regarding potential conflicts of LMIM and the administrators:

(a) it is the sworn testimony of the administrators that they do not intend to charge the management fee which the responsible entity is otherwise entitled to charge under the LMFMIF constitution;

(b) if a conflict arises because LMIM is the responsible entity of the LMFMIF and two of the feeder funds, the administrators will:

(i) investigate the conflict and the circumstances in which it arises;

(ii) form a view on the proper course to take

(iii) if necessary, take legal advice;

(iv) if necessary, approach the court for directions;

(c) no money is owed by LMA to the LMFMIF. There is a small amount owed by the LMFMIF to LMA;

(d) in relation to the loan management services fee, if a conflict arises the administrators and any liquidators must:

(i) investigate the conflict and the circumstances in which it arises;

(ii) form a view on the proper course to take

(iii) if necessary, take legal advice;

(iv) if necessary, approach the court for directions;

(e) there are no related party transactions which give rise to a conflict of interest. There was no cross-examination of Ms Muller on this point;

(f) the administrators are entitled to claim the fees for their work and there is more than one source of funds available to pay those fees. It is the same as in the case of any liquidator appointed to more than one company in a corporate group. If either Mr Whyte or Trilogy is appointed to act, they will be in the same position;

(g) any responsible entity who is responsible for selling property and realising the assets will seek an indemnity from the fund for their proper expenses and they will be subject to appropriate oversight in doing so;

(h) at the moment there is a bare possibility of legal action against the responsible entity and if that matures, those who are running it will:

(i) investigate the conflict and the circumstances in which it arises;

(ii) form a view on the proper course to take

(iii) if necessary, take legal advice;

(iv) if necessary, approach the court for directions;

(v) if necessary, seek the appointment of a special purpose liquidator for the assets of the company in its own capacity;

(i) there is no evidence of joint lending between the LMFMIF and other funds;

(j) it is possible that claims will be made and proofs of debt will be submitted by the LMFMIF against the responsible entity. If that happens, those responsible for operating the fund will have to:

(i) investigate the conflict and the circumstances in which it arises;

(ii) form a view on the proper course to take

(iv) if necessary, take legal advice;

(v) if necessary, approach the court for directions;

(vi) if necessary, seek the appointment of a special purpose liquidator for the assets of the company in its own capacity;

(k) it would be a mistake to work on the assumption that the administrators or anyone else who is proposed for this administration, would try and bury a conflict, as opposed to responding to it appropriately by reporting it to the overseer, by getting advice and seeking directions if there was no overseer. There is a lot of speculation at the moment and conflicts may emerge. If they do, they will be dealt with in an

appropriate way and, in a more extreme solution, an appointment of a special purpose liquidator or overseer of some kind may be appropriate.

(l) however, currently, by the test of "necessity" the case is not made out.