ABN AMRO Bank NV v Bathurst Regional Council - [2014] FCAFC 65

FEDERAL COURT OF AUSTRALIA

ABN AMRO Bank NV v Bathurst Regional Council [2014] FCAFC 65

Citation:	ABN AMRO Bank NV v Bathurst Regional Council [2014] FCAFC 65
Appeal from:	Bathurst Regional Council v Local Government Financial Services Pty Ltd (No 5) [2012] FCA 1200
Parties:	**ABN AMRO BANK NV (ARBN 84 079 478 612), McGRAW-HILL INTERNATIONAL (UK) LIMITED, LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741), AMERICAN HOME ASSURANCE COMPANY (ABN 007 483 267753) v BATHURST REGIONAL COUNCIL, COOMA MONARO SHIRE COUNCIL (ABN 19 204 741 100), COROWA SHIRE COUNCIL (ABN 43 874 223 315), DENILIQUIN COUNCIL (ABN 41 992 919 200), EUROBODALLA SHIRE COUNCIL (ABN 47 504 455 945), MOREE PLAINS SHIRE COUNCIL (ABN 46 566 790 582), MURRAY SHIRE COUNCIL (ABN 77 334 235 304), NARRANDERA SHIRE COUNCIL (ABN 96 547 765 569), NARROMINE SHIRE COUNCIL (ABN 99 352 328 504), OBERON COUNCIL (ABN 13 632 416 736), ORANGE CITY COUNCIL**

(ABN 85 985 402 386), PARKES SHIRE COUNCIL (ABN 96 299 629 630), CITY OF RYDE (ABN 81 627 292 610), ABN AMRO BANK NV (ARBN 84 079 478 612), MCGRAW-HILL INTERNATIONAL (UK) LIMITED, LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741) and AMERICAN HOME ASSURANCE COMPANY (ABN 007 483 267753)

BATHURST REGIONAL COUNCIL v LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)

COOMA MONARO SHIRE COUNCIL (ABN 19 204 741 100), COROWA SHIRE COUNCIL (ABN 43 874 223 315), DENILIQUIN COUNCIL (ABN 41 992 919 200), EUROBODALLA SHIRE COUNCIL (ABN 47 504 455 945), MOREE PLAINS SHIRE COUNCIL (ABN 46 566 790 582), MURRAY SHIRE COUNCIL (ABN 77 334 235 304), NARRANDERA SHIRE COUNCIL (ABN 96 547 765 569), NARROMINE SHIRE COUNCIL (ABN 99 352 328 504), OBERON COUNCIL (ABN 13 632 416 736), ORANGE CITY COUNCIL (ABN 85 985 402 386), PARKES SHIRE COUNCIL (ABN 96 299 629 630) and CITY OF RYDE (ABN 81 627 292 610) v LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)

MCGRAW-HILL INTERNATIONAL (UK) LIMITED v BATHURST REGIONAL COUNCIL, LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741) and ABN AMRO BANK NV (ARBN 84 079 478 612)

MCGRAW-HILL INTERNATIONAL (UK) LIMITED v COOMA MONARO SHIRE COUNCIL (ABN 19 204 741 100), COROWA SHIRE COUNCIL (ABN 43 874 223 315), DENILIQUIN COUNCIL (ABN 41 992 919 200), EUROBODALLA SHIRE COUNCIL (ABN 47 504 455 945), MOREE PLAINS SHIRE COUNCIL (ABN 46 566 790 582), MURRAY SHIRE COUNCIL (ABN 77 334 235 304), NARRANDERA SHIRE COUNCIL (ABN 96 547 765 569), NARROMINE SHIRE COUNCIL (ABN 99 352 328 504), OBERON COUNCIL (ABN 13 632 416 736), ORANGE CITY COUNCIL (ABN 85 985 402 386), PARKES SHIRE COUNCIL (ABN 96 299 629 630), CITY OF RYDE (ABN 81 627 292 610), LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741) and ABN AMRO BANK NV (ARBN 84 079 478 612)

LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741) v BATHURST REGIONAL COUNCIL, COOMA MONARO SHIRE COUNCIL (ABN 19 204 741 100), COROWA SHIRE COUNCIL (ABN 43 874 223 315), DENILIQUIN COUNCIL (ABN 41 992 919 200), EUROBODALLA SHIRE COUNCIL (ABN 47 504 455 945), MOREE PLAINS SHIRE COUNCIL (ABN 46 566 790 582), MURRAY SHIRE COUNCIL (ABN 77 334 235 304), NARRANDERA SHIRE COUNCIL (ABN 96 547 765 569), NARROMINE SHIRE COUNCIL (ABN 99 352 328 504), OBERON COUNCIL (ABN 13 632 416 736), ORANGE CITY COUNCIL (ABN 85 985 402 386), PARKES SHIRE COUNCIL (ABN 96 299 629 630), CITY OF RYDE (ABN 81 627 292 610), ABN AMRO BANK NV (ARBN 84 079 478 612), MCGRAW-HILL INTERNATIONAL (UK) LIMITED and AMERICAN HOME ASSURANCE COMPANY (ABN 67 007 483 267)

MCGRAW-HILL INTERNATIONAL (UK) LIMITED v LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741) and ABN AMRO BANK NV (ARBN 84 079 478 612)

AMERICAN HOME ASSURANCE COMPANY (ABN 67 007 483 267) vBATHURST REGIONAL COUNCIL, LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741), ABN AMRO BANK NV (ARBN 84 079 478 612) and MCGRAW-HILL INTERNATIONAL (UK) LIMITED

AMERICAN HOME ASSURANCE COMPANY (ABN 67 007 483 267) vCOOMA MONARO SHIRE COUNCIL (ABN 19 204 741 100), COROWA SHIRE COUNCIL (ABN 43 874 223 315), DENILIQUIN COUNCIL (ABN 41 992 919 200), EUROBODALLA SHIRE COUNCIL (ABN 47 504 455 945), MOREE PLAINS SHIRE COUNCIL (ABN 46 566 790 582), MURRAY SHIRE COUNCIL (ABN 77 334 235 304), NARRANDERA SHIRE COUNCIL (ABN 96 547 765 569), NARROMINE SHIRE COUNCIL (ABN 99 352 328 504), OBERON COUNCIL (ABN 13 632 416 736), ORANGE CITY COUNCIL (ABN 85 985 402 386), PARKES SHIRE COUNCIL (ABN 96 299 629 630), CITY OF RYDE (ABN 81 627 292 610), LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741), ABN AMRO BANK NV (ARBN 84 079 478 612) and MCGRAW-HILL INTERNATIONAL (UK) LIMITED

AMERICAN HOME ASSURANCE COMPANY (ABN 67 007 483 267) v LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741), ABN

AMRO BANK NV (ARBN 84 079 478 612) and MCGRAW-HILL INTERNATIONAL (UK) LIMITED

File numbers:	NSD 501 of 2013 NSD 502 of 2013 NSD 503 of 2013 NSD 504 of 2013 NSD 505 of 2013 NSD 507 of 2013 NSD 508 of 2013 NSD 522 of 2013 NSD 523 of 2013 NSD 524 of 2013
Judges:	**JACOBSON, GILMOUR AND GORDON JJ**
Date of judgment:	6 June 2014
Catchwords:	**CONTRACT** – breach of contract – contract for provision of financial services – implied warranties in s 12ED of *Australian Securities and Investments Commission Act 2001* (Cth) – damages for breach of contract **CORPORATIONS** – financial products – breach of Australian financial services licence under s 912A of *Corporations Act 2001* (Cth) – meaning of derivative in s 761D(1) of *Corporations Act 2001* (Cth) – meaning of debenture in s 9 of *Corporations Act 2001* (Cth) **CORPORATIONS** – misleading and deceptive statements – whether statements based on reasonable grounds and result of exercise of reasonable care and skill – effect of disclaimers – proportionate liability provisions **CORPORATIONS** – rescission – requirements of s 924A of *Corporations Act*

2001 (Cth) – notice under s 925A of *Corporations Act 2001* (Cth) – whether notice given within a "reasonable period"

DAMAGES – causation – remoteness – "rule" in *Potts v Miller* (1940) 64 CLR 282 – contributory negligence – statutory damages – measure for damages – apportionment – proportionate liability

EQUITY – fiduciary obligations – informal advisory relationship arising from conduct – whether breach of fiduciary duty – equitable compensation – equitable contribution

INSURANCE – whether insured entity a party to contract of insurance – effect of s 48 of *Insurance Contracts Act 1984* (Cth) – duty of disclosure – construction of terms

PRACTICE AND PROCEDURE – entitlement to raise new matters on appeal

STATUTORY INTERPRETATION – whether investment permissible under s 625 of *Local Government Act 1993* (NSW) – whether product a security within the meaning of relevant Ministerial order

TORT – whether duty of care owed – negligent misstatement – indeterminate liability – vulnerability – causation – unlawful conduct – effect of disclaimers – contributory negligence

	TRADE PRACTICES – misleading and deceptive conduct – whether conduct engaged in "in this jurisdiction" – whether conduct in relation to financial product or financial services – "mere conduit"
Legislation:	*Acts Interpretation Act 1901* (Cth) *Australian Securities and Investments Commission Act 2001* (Cth) *Competition and Consumer Act 2010* (Cth) *Corporations Act 2001* (Cth) *Evidence Act 1995* (Cth) *Civil Liability Act 2002* (NSW) *Law Reform (Miscellaneous Provisions) Act 1965* (NSW) *Local Government Act 1993* (NSW) *Trustee Act 1925* (NSW) *Wrongs Act 1958* (Vic)
Cases cited:	*Abigroup Contractors Pty Ltd v Sydney Catchment Authority (No 3)* (2006) 67 NSWLR 341 *Advance (NSW) Insurance Agencies Pty Limited v Matthews* (1989) 166 CLR 606 *Aiken v Stewart Wrightson Members Agency Limited* [1995] 1 WLR 1281 *Al Saudi Banque v Clark Pixley* [1990] Ch 313 *Astley v Austrust Ltd* (1999) 197 CLR 1 *Austral Mining Construction Pty Ltd v NZI Capital Corp Ltd* (1991) 4 ACSR 57 *Australian Broadcasting Corporation v XIVth Commonwealth Games* (1988) 18 NSWLR 540 *Australian Securities and Investments Commission v Australian Lending Centre Pty Limited (No 3)* (2012) 213 FCR 380 *Australian Securities and Investments Commission v Citigroup Global Markets Australia Pty Ltd (No 4)* (2007) 160 FCR 35 *Australian Securities and Investments Commission v Healey* (2011) 196 FCR 291 *Australian Securities and Investments Commission v Narain* (2008) 169 FCR 211

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Date of hearing:	3, 4, 5, 6, 7, 10, 11, 12, 13 and 14 March 2014
Date of last submissions:	26 March 2014
Place:	Sydney
Division:	GENERAL DIVISION

Category:	Catchwords
Number of paragraphs:	1,859
Counsel for ABN AMRO Bank NV:	I Jackman SC with M Darke
Solicitor for ABN AMRO Bank NV:	Allens
Counsel for McGraw-Hill International (UK) Limited:	SG Finch SC with KH Barrett and IJM Ahmed
Solicitor for McGraw-Hill International (UK) Limited:	Clayton Utz
Counsel for Local Government Financial Services Pty Ltd:	G Parker SC with J Giles
Solicitor for Local Government Financial Services Pty Ltd:	Norton Rose Australia
Counsel for American Home Assurance Company:	S Couper QC with J Gooley
Solicitor for American Home Assurance Company:	Wotton Kearney
Counsel for Bathurst Regional Council:	J Thomson
Solicitor for Bathurst Regional Council:	McIntosh McPhillamy & Co
Counsel for PA Councils:	N Hutley SC with A Coleman SC and C Withers
Solicitor for PA Councils:	Piper Alderman

IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

NSD 501 of 2013

GENERAL DIVISION

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN: ABN AMRO BANK NV (ARBN 84 079 478 612)
First Appellant

MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Second Appellant

LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)
Third Appellant

AMERICAN HOME ASSURANCE COMPANY (ABN 007 483 267753)
Fourth Appellant

AND: BATHURST REGIONAL COUNCIL
First Respondent

COOMA MONARO SHIRE COUNCIL (ABN 19 204 741 100)
Second Respondent

COROWA SHIRE COUNCIL (ABN 43 874 223 315)
Third Respondent

DENILIQUIN COUNCIL (ABN 41 992 919 200)
Fourth Respondent

EUROBODALLA SHIRE COUNCIL (ABN 47 504 455 945)
Fifth Respondent

MOREE PLAINS SHIRE COUNCIL (ABN 46 566 790 582)
Sixth Respondent

MURRAY SHIRE COUNCIL (ABN 77 334 235 304)
Seventh Respondent

NARRANDERA SHIRE COUNCIL (ABN 96 547 765 569)
Eighth Respondent

NARROMINE SHIRE COUNCIL (ABN 99 352 328 504)
Ninth Respondent

OBERON COUNCIL (ABN 13 632 416 736)
Tenth Respondent

ORANGE CITY COUNCIL (ABN 85 985 402 386)
Eleventh Respondent

PARKES SHIRE COUNCIL (ABN 96 299 629 630)
Twelfth Respondent

CITY OF RYDE (ABN 81 627 292 610)
Thirteenth Respondent

ABN AMRO BANK NV (ARBN 84 079 478 612)
Fourteenth Respondent

MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Fifteenth Respondent

LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)
Sixteenth Respondent

AMERICAN HOME ASSURANCE COMPANY (ABN 007 483 267753)
Seventeenth Respondent

JUDGES:	JACOBSON, GILMOUR AND GORDON JJ
DATE OF ORDER:	6 june 2014
WHERE MADE:	SYDNEY

THE COURT ORDERS THAT:

1. The parties are directed to confer and bring in agreed orders to give effect to these reasons for judgment including the question of costs by 4:00pm on 13 June 2014. If the orders cannot be agreed, then the parties are to file a joint document which identifies the areas of agreement, the areas of disagreement and, for the areas of disagreement, the reason or reasons for that disagreement by 4:00pm on 13 June 2014.

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

IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

NSD 502 of 2013

GENERAL DIVISION

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN: MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Appellant

AND: BATHURST REGIONAL COUNCIL
First Respondent

LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED
(ACN 001 681 741)
Second Respondent

ABN AMRO BANK NV (ARBN 84 079 478 612)
Third Respondent

JUDGES: JACOBSON, GILMOUR AND GORDON JJ

DATE OF ORDER: **6 june 2014**

WHERE MADE: **SYDNEY**

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IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

GENERAL DIVISION **NSD 503 of 2013**

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN: **ABN AMRO BANK NV (ARBN 84 079 478 612)**
Appellant

AND: **COOMA MONARO SHIRE COUNCIL (ABN 19 204 741 100)**
First Respondent

COROWA SHIRE COUNCIL (ABN 43 874 223 315)
Second Respondent

DENILIQUIN COUNCIL (ABN 41 992 919 200)
Third Respondent

EUROBODALLA SHIRE COUNCIL (ABN 47 504 455 945)
Fourth Respondent

MOREE PLAINS SHIRE COUNCIL (ABN 46 566 790 582)
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MURRAY SHIRE COUNCIL (ABN 77 334 235 304)
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Ninth Respondent

ORANGE CITY COUNCIL (ABN 85 985 402 386)
Tenth Respondent

PARKES SHIRE COUNCIL (ABN 96 299 629 630)
Eleventh Respondent

CITY OF RYDE (ABN 81 627 292 610)
Twelfth Cross Appellant

LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)
Thirteenth Respondent
MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Fourteenth Respondent

JUDGES:	**JACOBSON, GILMOUR AND GORDON JJ**
DATE OF ORDER:	**6 june 2014**
WHERE MADE:	**SYDNEY**

THE COURT ORDERS THAT:

1. The parties are directed to confer and bring in agreed orders to give effect to these reasons for judgment including the question of costs by 4:00pm on 13 June 2014. If the orders cannot be agreed, then the parties are to file a joint document which identifies the areas of agreement, the areas of disagreement and, for the areas of disagreement, the reason or reasons for that disagreement by 4:00pm on 13 June 2014.

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

IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

NSD 504 of 2013

GENERAL DIVISION

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN: MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Appellant

AND: COOMA MONARO SHIRE COUNCIL (ABN 19 204 741 100)
First Respondent

CORowa SHIRE COUNCIL (ABN 43 874 223 315)
Second Respondent

DENILIQUIN COUNCIL (ABN 41 992 919 200)
Third Respondent

EUROBODALLA SHIRE COUNCIL (ABN 47 504 455 945)
Fourth Respondent

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CITY OF RYDE (ABN 81 627 292 610)
Twelfth Cross Appellant

LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)
Thirteenth Respondent

ABN AMRO BANK NV (ARBN 84 079 478 612)
Fourteenth Respondent

JUDGES: **JACOBSON, GILMOUR AND GORDON JJ**

DATE OF ORDER: **6 june 2014**

WHERE MADE: **SYDNEY**

THE COURT ORDERS THAT:

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IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

GENERAL DIVISION **NSD 505 of 2013**

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN:

LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED
(ACN 001 681 741)
Appellant

AND: BATHURST REGIONAL COUNCIL
First Respondent

COOMA MONARO SHIRE COUNCIL (ABN 19 204 741 100)
Second Respondent

COROWA SHIRE COUNCIL (ABN 43 874 223 315)
Third Respondent

DENILIQUIN COUNCIL (ABN 41 992 919 200)
Fourth Respondent

EUROBODALLA SHIRE COUNCIL (ABN 47 504 455 945)
Fifth Respondent

MOREE PLAINS SHIRE COUNCIL (ABN 46 566 790 582)
Sixth Respondent

MURRAY SHIRE COUNCIL (ABN 77 334 235 304)
Seventh Respondent

NARRANDERA SHIRE COUNCIL (ABN 96 547 765 569)
Eighth Respondent

NARROMINE SHIRE COUNCIL (ABN 99 352 328 504)
Ninth Respondent

OBERON COUNCIL (ABN 13 632 416 736)
Tenth Respondent

ORANGE CITY COUNCIL (ABN 85 985 402 386)
Eleventh Respondent

PARKES SHIRE COUNCIL (ABN 96 299 629 630)
Twelfth Respondent

CITY OF RYDE (ABN 81 627 292 610)
Thirteenth Respondent

ABN AMRO BANK NV (ARBN 84 079 478 612)
Fourteenth Respondent

MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Fifteenth Respondent

AMERICAN HOME ASSURANCE COMPANY (ABN 67 007 483 267)
Sixteenth Respondent

JUDGES: JACOBSON, GILMOUR AND GORDON JJ

DATE OF ORDER: 6 june 2014

WHERE MADE: SYDNEY

THE COURT ORDERS THAT:

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IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

GENERAL DIVISION **NSD 507 of 2013**

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN: **ABN AMRO BANK NV (ARBN 84 079 478 612)**
Appellant

AND: **LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)**
First Respondent

MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Second Respondent

JUDGES: JACOBSON, GILMOUR AND GORDON JJ

DATE OF ORDER: 6 june 2014

WHERE MADE: SYDNEY

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IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

GENERAL DIVISION **NSD 508 of 2013**

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN: **MCGRAW-HILL INTERNATIONAL (UK) LIMITED**
Appellant

AND: **LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)**
First Respondent

ABN AMRO BANK NV (ARBN 84 079 478 612)
Second Respondent

JUDGES: **JACOBSON, GILMOUR AND GORDON JJ**

DATE OF ORDER: **6 JUNE 2014**

WHERE MADE: **SYDNEY**

THE COURT ORDERS THAT:

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IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

NSD 522 of 2013

GENERAL DIVISION

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN: AMERICAN HOME ASSURANCE COMPANY (ABN 67 007 483 267)
Appellant

AND: BATHURST REGIONAL COUNCIL
First Respondent

LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)
Second Respondent

ABN AMRO BANK NV (ARBN 84 079 478 612)
Third Respondent

MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Fourth Respondent

JUDGES: JACOBSON, GILMOUR AND GORDON JJ

DATE OF ORDER: 6 JUNE 2014

WHERE MADE: **SYDNEY**

THE COURT ORDERS THAT:

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IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

GENERAL DIVISION **NSD 523 of 2013**

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN: **AMERICAN HOME ASSURANCE COMPANY (ABN 67 007 483 267)**
Appellant

AND: COOMA MONARO SHIRE COUNCIL (ABN 19 204 741 100)
First Respondent

COROWA SHIRE COUNCIL (ABN 43 874 223 315)
Second Respondent

DENILIQUIN COUNCIL (ABN 41 992 919 200)
Third Respondent

EUROBODALLA SHIRE COUNCIL (ABN 47 504 455 945)
Fourth Respondent

MOREE PLAINS SHIRE COUNCIL (ABN 46 566 790 582)
Fifth Respondent

MURRAY SHIRE COUNCIL (ABN 77 334 235 304)
Sixth Respondent

NARRANDERA SHIRE COUNCIL (ABN 96 547 765 569)
Seventh Respondent

NARROMINE SHIRE COUNCIL (ABN 99 352 328 504)
Eighth Respondent

OBERON COUNCIL (ABN 13 632 416 736)
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ORANGE CITY COUNCIL (ABN 85 985 402 386)
Tenth Respondent

PARKES SHIRE COUNCIL (ABN 96 299 629 630)
Eleventh Respondent

CITY OF RYDE (ABN 81 627 292 610)
Twelfth Respondent

LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)
Thirteenth Respondent

ABN AMRO BANK NV (ARBN 84 079 478 612)
Fourteenth Respondent

MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Fifteenth Respondent

JUDGES: JACOBSON, GILMOUR AND GORDON JJ

DATE OF ORDER: 6 JUNE 2014

WHERE MADE: SYDNEY

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IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

GENERAL DIVISION **NSD 524 of 2013**

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN: **AMERICAN HOME ASSURANCE COMPANY (ABN 67 007 483 267)**
Appellant

AND: **LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)**
First Respondent

ABN AMRO BANK NV (ARBN 84 079 478 612)
Second Respondent

MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Third Respondent

JUDGES: **JACOBSON, GILMOUR AND GORDON JJ**

DATE OF ORDER: 6 june 2014

WHERE MADE: SYDNEY

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IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

NSD 501 of 2013

GENERAL DIVISION

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN: **ABN AMRO BANK NV (ARBN 84 079 478 612)** and others named in the attached Schedule of Parties
Appellant

AND: **BATHURST REGIONAL COUNCIL** and others named in the attached Schedule of Parties
First Respondent

IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

NSD 502 of 2013

GENERAL DIVISION

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN: **MCGRAW-HILL INTERNATIONAL (UK) LIMITED**
Appellant

AND: **BATHURST REGIONAL COUNCIL** and others named in the attached Schedule of Parties
First Respondent

IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

NSD 503 of 2013

GENERAL DIVISION

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN: **ABN AMRO BANK NV (ARBN 84 079 478 612)**
Appellant

AND: **COOMA MONARO SHIRE COUNCIL (ABN 19 204 741 100)**
First Respondent and others named in the attached Schedule of Parties

IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

NSD 504 of 2013

GENERAL DIVISION

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN:

MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Appellant

AND: **COOMA MONARO SHIRE COUNCIL (ABN 19 204 741 100)** and others named in the attached Schedule of Parties
First Respondent

IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

NSD 505 of 2013

GENERAL DIVISION

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN: **LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)**
Appellant

AND: **BATHURST REGIONAL COUNCIL** and others named in the attached Schedule of Parties
First Respondent

IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

NSD 507 of 2013

GENERAL DIVISION

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN: ABN AMRO BANK NV (ARBN 84 079 478 612)
Appellant

AND: LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)

First Respondent

MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Second Respondent

IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

NSD 508 of 2013

GENERAL DIVISION

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN: MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Appellant

AND:	**LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)** **First Respondent**
	ABN AMRO BANK NV (ARBN 84 079 478 612) **Second Respondent**

IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

NSD 522 of 2013

GENERAL DIVISION

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN:	**AMERICAN HOME ASSURANCE COMPANY (ABN 67 007 483 267)** **Appellant**
AND:	**BATHURST REGIONAL COUNCIL** and others named in the attached Schedule of Parties **First Respondent**

IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

NSD 523 of 2013

GENERAL DIVISION

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN: **AMERICAN HOME ASSURANCE COMPANY (ABN 67 007 483 267)**
Appellant

AND: **COOMA MONARO SHIRE COUNCIL (ABN 19 204 741 100)** and others named in the attached Schedule of Parties
First Respondent

IN THE FEDERAL COURT OF AUSTRALIA

NEW SOUTH WALES DISTRICT REGISTRY

NSD 524 of 2013

GENERAL DIVISION

ON APPEAL FROM THE FEDERAL COURT OF AUSTRALIA

BETWEEN: **AMERICAN HOME ASSURANCE COMPANY (ABN 67 007 483 267)**
Appellant

AND: **LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)** and others named in the attached Schedule of Parties
First Respondent

JUDGES: JACOBSON, GILMOUR AND GORDON JJ

DATE: 6 JUNE 2014

PLACE: SYDNEY

REASONS FOR JUDGMENT

PART 1: INTRODUCTION

1. ABN AMRO Bank NV (**ABN Amro**) is an investment bank. In 2006, it created a "CPDO" (a form of financial instrument or "structured financial product"), which it proposed to sell in AUD under the name "**Rembrandt notes**". Standard & Poors (**S&P**) was a division of McGraw-Hill Companies Inc. At the request of the issuer of a financial instrument, S&P would assign a rating to the instrument. The rating was intended to describe the likelihood that principal and interest due under the instrument would be paid in accordance with its terms. ABN Amro asked S&P to rate the Rembrandt notes. S&P rated them AAA (the highest rating assigned by S&P). S&P accepted on appeal that the rating was flawed.

2. ABN Amro marketed and sold the Rembrandt notes to Local Government Financial Services Pty Ltd (**LGFS**). The two Australian dollar issues were known as the Rembrandt 2006-2 and Rembrandt 2006-3 notes (collectively, the **Rembrandt notes**). As its name suggests, LGFS dealt with local government authorities. LGFS purchased $10 million of the Rembrandt 2006-2 notes ($6 million on behalf of StateCover Mutual Limited (**StateCover**) and $4 million which it purchased in its own name and subsequently transferred to StateCover). LGFS then purchased $45 million of the Rembrandt 2006-3 notes. LGFS sold a substantial portion of the Rembrandt 2006-3 notes to 13 municipal councils in New South Wales (the **Councils**). StateC over and the Councils lost much of the amounts they invested in the Rembrandt notes. StateCover and the Councils sued ABN Amro, S&P and LGFS for damages.

3. After a trial occupying 53 days, judgment was entered for the Councils against ABN Amro, S&P and LGFS and orders were made apportioning liability between them. LGFS also established an entitlement to equitable contribution from ABN Amro and S&P including on account of LGFS' payment to StateCover to discharge StateCover's claims against LGFS, S&P and ABN Amro (the **StateCover settlement**). The primary judge dealt also with other claims which are described in more detail below.

4. Ten separate proceedings were brought in the appellate jurisdiction of this Court and have been heard together. There are appeals and cross appeals. In their appeals, ABN Amro, S&P and LGFS advanced so many different appeal grounds that it was necessary to tabulate those grounds in tables comprising 306 entries set out over more than 120 pages. To assist the parties, and to the extent that it is feasible, we have endeavoured to note these tabulated appeal grounds in the course of our reasons. The grounds are identified in the following way "[Party Name] Appeal Grounds Matrix Row [##]". By their appeal grounds, ABN Amro, S&P and LGFS put in issue just about every finding of fact and conclusion of law made by the primary judge and for the most part pursued each allegation of error with undiscriminating vigour. As a result, these reasons for judgment must be, and are, very long and very complex. But, subject to some qualifications, the attacks made on the findings made, and conclusions reached, by the primary judge fail. The qualifications have only a limited effect on the primary judge's final orders. Defined terms are used throughout these reasons for judgment. For the assistance of the reader, a glossary of those terms is set out in Attachment A. Paragraphs of the trial judgment are identified by the prefix J[***]. On appeal, the parties also filed a statement of agreed facts. That statement was not comprehensive. Paragraphs of that statement are identified by the prefix [SAF***].

5. At trial, three proceedings were heard together ([SAF2]):

    1. Proceedings commenced by Corowa Shire Council and 11 other New South Wales regional councils (the **PA Councils**) against LGFS, ABN Amro and S&P, in which cross claims were made between those parties and American Home Assurance Company (**AHAC**) (**Corowa Proceedings**);

    2. Proceedings commenced by Bathurst Regional Council (**Bathurst**) against LGFS, ABN Amro and S&P, in which cross claims were made between those parties and AHAC (**Bathurst Proceedings**); and

    3. Proceedings commenced by StateCover against LGFS, ABN Amro and S&P, in which cross claims were made between those parties and AHAC (**StateCover P roceedings**).

6. LGFS also sued both ABN Amro and S&P: (1) on account of LGFS' payment under the StateCover settlement; (2) LGFS' own losses incurred on the sale of the Rembrandt 2006-3 notes to its parent company, Local Government Superannuation Scheme (**LGSS**) and (3) any liability that LGFS might be found to have to the Councils in respect of their claims against LGFS. In addition, because LGFS' insurer, AHAC, denied LGFS cover for the StateCover settlement and the claims of the Councils, LGFS sued AHAC for indemnity under its insurance policy: [SAF1].

7. LGFS, ABN Amro, S&P and AHAC all denied liability and raised various defences and cross-claims to the claims against them. The cross-claims included not only those of LGFS against S&P and ABN Amro but also those of S&P and ABN Amro against each other and of AHAC against LGFS for the repayment of defence costs already paid. Issues of contributory negligence were raised against the Councils and LGFS by S&P and ABN Amro. Issues of proportionate liability were raised between LGFS, S&P and ABN Amro in respect of claims against and between them other than the claims of AHAC which were separate: [SAF1].

8. The PA Councils were commonly represented: [SAF4]. Bathurst was separately represented. Despite some differences in the formulation of the claims made by Bathurst and the PA Councils (including an unconscionable conduct claim by Bathurst against LGFS), the claims may be described together: [SAF1].

9. The Councils' and LGFS' claims may be described as follows:

   1. The Councils against LGFS: (i) misleading and deceptive conduct; (ii) negligence; (iii) in respect of two of the councils, Cooma and Corowa, breach of contract; (iv) an unlicensed to deal claim and (v) breach of fiduciary duty. Bathurst also brought a claim for restitution based on an allegation that councils were not permitted to invest in the Rembrandt notes, a claim which the PA Councils made in the alternative only to their primary case that the Councils were permitted to invest in the Rembrandt notes. The remedies sought for the unlicensed to deal claim and the fiduciary duty claim included rescission of the Councils' agreements to purchase the Rembrandt notes with associated restitution and equitable compensation. The remedies sought for the other claims were damages: [SAF1]. On appeal, the PA Councils did not pursue their rescission claim.

   2. The Councils against S&P: (i) misleading and deceptive conduct and (ii) negligence. The remedies sought were damages: [SAF1].

   3. The Councils against ABN Amro: (i) misleading and deceptive conduct; (ii) knowing involvement in S&P's misleading and deceptive conduct and (iii) negligence. The remedies sought were damages: [SAF1].

   4. LGFS against S&P: (i) misleading and deceptive conduct and (ii) negligence. The remedies sought were damages: [SAF1].

   5. LGFS against ABN Amro: (i) misleading and deceptive conduct; (ii) negligence and (iii) a contract claim in respect of the Rembrandt 2006-3 notes. The remedies sought were damages: [SAF1].

10. S&P's claims against ABN Amro only arose if S&P was found liable to LGFS and / or the Councils. In that event, S&P brought proportionate liability claims against ABN Amro as a concurrent wrongdoer: [SAF1]. ABN Amro's claims against S&P only arose if ABN Amro was found liable to LGFS and/or the Councils. In that event, ABN Amro brought proportionate liability claims against S&P as a concurrent wrongdoer: [SAF1].

11. LGFS claimed that AHAC was liable to indemnify LGFS for any liability it had in respect of the claims of the Councils and in respect of the StateCover settlement and its defence costs in connection with each. AHAC denied that LGFS has any right to indemnity under the contract of insurance on various grounds and sought repayment from LGFS of the defence costs already paid: [SAF1].

12. The primary judge held, and we would uphold on appeal, that:

1. S&P’s assignment of a AAA rating to the Rembrandt notes was misleading and deceptive and involved the publication of information or statements false in material particulars and otherwise involved negligent misrepresentations to the class of potential investors in Australia, which included LGFS and the Councils, because by the AAA rating there was conveyed a representation that in S&P’s opinion the capacity of the notes to meet all financial obligations was “extremely strong” and a representation that S&P had reached this opinion based on reasonable grounds and as the result of an exercise of reasonable care and skill when neither was true and S&P also knew them not to be true when they were made;

2. ABN Amro was knowingly concerned in S&P’s contraventions of the various statutory provisions proscribing such misleading and deceptive conduct, and also itself engaged in conduct that was misleading and deceptive and published information or statements false in material particulars and otherwise involved negligent misrepresentations to LGFS specifically and the class of potential investors with which ABN Amro knew LGFS intended to deal, being the Councils, by reason of ABN Amro’s deployment of the AAA rating and its own representations as to the meaning and reliability of the AAA rating which also were not true and ABN Amro knew them not to be true when they were made;

3. ABN Amro breached its contract with LGFS under which ABN Amro was to model and structure the transaction by which LGFS would purchase the notes having a degree of security commensurate with a rating of AAA assigned by S&P; and

4. LGFS engaged in misleading and deceptive conduct and in one respect the publication of information or a statement false in material particulars and otherwise made negligent misrepresentations to the Councils about the Rembrandt 2006-3 notes and, in addition, breached its Australian Financial Services Licence (**AFSL**) in advising the Councils about and selling to them the notes because the notes were not a debenture and thus not a security but a derivative under the *Corporations Act 2001* (Cth) (***Corporations Act***) in which LGFS was not licensed to deal.

13. The primary judge also held that LGFS was in a fiduciary relationship with each Council and, in its dealings with the Councils, LGFS breached its fiduciary obligations to avoid conflicts of interest in respect of the notes, or to disclose and obtain fully informed consent to such conflicts. The relationship between LGFS and each Council was of a fiduciary nature. LGFS breached its fiduciary obligations by failing to avoid conflicts of interest in respect of the notes although the conflict (and therefore the nature of the breach) we would describe differently.

14. In relation to the damages, contributory negligence and apportionment, the primary judge held:

1. The arguments made by:

1.1 LGFS, S&P and ABN Amro of contributory negligence or the equivalent by the Councils; and

1.2 S&P and ABN Amro of contributory negligence or the equivalent by LGFS in respect of, relevantly, the Rembrandt notes,

were rejected.

2. LGFS established its entitlement to damages against S&P and ABN Amro (which were held to be proportionally liable as to 50% each) for LGFS' loss incurred on the sale of the downgraded Rembrandt 2006-3 notes to its parent company LGSS ($15,970,184.72).

3. LGFS established its entitlement to damages or equitable contribution from S&P and ABN Amro (which were proportionally liable as to $33^{1/3}$% each with LGFS liable for the other $33^{1/3}$%) in respect of the settlement LGFS made of the StateCover proceedings against LGFS, S&P and ABN Amro ($3.175 million).

4. The Councils established their entitlement to damages from S&P, ABN Amro and LGFS (which were held to be proportionally liable as to $33^{1/3}$% each) being the difference between the principal amount each paid and the payment they received on the cash out of the notes.

5. The Councils also established their entitlement to equitable compensation from LGFS for breach of fiduciary duty but the measure of equitable compensation was held to be the same as the damages otherwise payable by S&P, ABN Amro and LGFS as to $33^{1/3}$% each.

6. LGFS established it was entitled to indemnity under the contract of insurance between FuturePlus Financial Services Pty Ltd (**FuturePlus**) and AHAC.

15. On appeal, we would uphold these findings in relation to damages, contributory negligence and apportionment except that we would hold that the damages assessed in relation to the claim under s 1041E of the *Corporations Act* are not apportionable.

16. The balance of the judgment is divided into Parts as follows:

1. The Facts: Part 2 ;

2. S&P's Rating and ABN Amro's knowledge that the rating lacked reasonable grounds and was misleading: Part 3;

3. LGFS' purchase of the Rembrandt 2006-3 notes:

3.1 As against S&P: Part 4 ;

3.2 As against ABN Amro: Part 5;

3.3 As against ABN Amro and S&P for losses on LGFS' Retained Notes: Part 6;

4. LGFS' claim against ABN Amro and S&P in relation to StateCover: Part 7;

5. The PA Councils' purchase of the Rembrandt 2006-3 notes:

   5.1 As against LGFS: Part 8;

   5.2 As against S&P: Part 9;

   5.3 As against ABN Amro: Part 10;

6. Bathurst's purchase of the Rembrandt 2006-3 notes: Part 11;

7. The Cross-Claims: Part 12;

8. Contributory negligence, apportionment, pre-judgment interest and costs: Part 13;

9. Insurance Claim between LGFS and AHAC: Part 14;

10. The Orders: Part 15.

PART 2 : THE FACTS

17. This part of the judgment is divided into the following sections:

1. The Councils;

2. LGFS;

3. CPDOs and Structured Finance Products;

4. ABN Amro;

5. S&P;

6. Sale of Rembrandt notes to LGFS;

7. Sale of Rembrandt notes to the Councils; and

8. Decline of the Rembrandt notes.

1. THE COUNCILS

1.1 Introduction

18. The Councils are bodies corporate constituted under the *Local Government Act 1993* (NSW) (***Local Government Act***) and are the local government authorities for various shires in New South Wales: [SAF5].

1.2 Ministerial Order and s 625 of the Local Government Act

19. In making investments with council funds, the Councils were required to comply with s 625(1) of the *Local Government Act* which provides that a council "*may invest money that is not, for the time being, required by the council for any other purpose*": [SAF8]. Under s 625(2) , "*[m]*

oney may be invested only in a form of investment notified by order of the Minister published in the Gazette": [SAF8]. Ministerial orders were published in the Gazette in 2000 and 2005: [SAF8].

20. The Ministerial order of 15 July 2005 (**Ministerial Order**) permitted investments in nominated assets. The Ministerial Order relevantly stated that investment was permitted in (see [SAF8] and J[2214]):

    (a) any public funds or Government stock or Government securities of the Commonwealth or any State of the Commonwealth;

    (b) any debentures or securities guaranteed by the Government of New South Wales;

    (c) any debentures or securities, issued by a public or local authority, or a statutory body representing the Crown, constituted by or under any law of the Commonwealth, of any State of the Commonwealth or of the Northern Territory or of the Australian Capital Territory and guaranteed by the Commonwealth, any State of the Commonwealth or a Territory;

    (d) any debentures or securities issued by a Territory and guaranteed by the Commonwealth;

    (e) any debentures or securities issued by a council (within the meaning of the Local Government Act 1993);

    (f) mortgage of land in any State or Territory of the Commonwealth;

    (g) purchase of land (including any lot within the meaning of the Strata Schemes Management Act 1996) in any State or Territory of the Commonwealth;

    (h) interest bearing deposits in a bank authorised to carry on the business of banking under any law of the Commonwealth or of a State or Territory of the Commonwealth;

    (i) interest bearing deposits with a building society or credit union.

    (j) any bill of exchange which has a maturity date of not more than 200 days; and if purchased for value confers on the holder in due course a right of recourse against a bank, building society or credit union as the acceptor or endorser of the bill for an amount equal to the face value of the bill;

    (k) any *securities* which are issued by a body or company (or controlled parent entity either immediate or ultimate) with a Moody's Investors Service, Inc. credit rating of "Aaa", "Aa1", "a2", "Aa3", "A1" or "A2" or a Standard & Poor's Investors Service, Inc credit rating of "AAA'', "AA+", "AA", "AA-"; "A+", or "A" or a Fitch Rating credit rating of "AAA", "AA+", "AA", "AA-", "A+" or "A";

(l) any *securities* which are given a Moody's Investors Service Inc credit rating of "Aaa", "Aa1", "Aa2", "Aa3", "A1"; "A2" or "Prime-1" or a Standard and Poor's Investors Service, Inc credit rating of "AAA", "AA+", "AA", "AA-", "A+"; "A"; "A1+" or "A1" or a Fitch Rating credit rating of "AAA", "AA+", "AA", "AA-", "A+" or "A";

(m) any debentures or securities issued by a bank, building society or credit union;

(n) a deposit with the Local Government Investment Service Pty Ltd;

(o) a deposit with the New South Wales Treasury Corporation or investments in an Hour-Glass investment facility of the New South Wales Treasury Corporation.

(Emphasis added.)

1.3 Investment Guidelines

21. On 29 November 2000, the Director-General of the Department of Local Government issued a circular (**DLG 2000 Circular**) to all councils attaching a copy of the relevant ministerial order as then in force: [SAF 11] and J[27]. The last two paragraphs of the circular stated:

> In addition, Councils (sic) attention is drawn to Update 8 of the Code of Accounting Practice and Financial Reporting that contains a policy direction that states "councils must maintain an investment policy". That investment policy must comply with the legislation and investment guidelines.
>
> In keeping with existing arrangements it is the responsibility of each individual council to determine that its investments are authorised in terms of the listed securities. Note that the Guidelines issued with the previous Order remain unchanged.

Those paragraphs of the DLG 2000 Circular provided that: (1) the councils must maintain an investment policy; (2) the investment policy must comply with the legislation and investment guidelines and (3) it is the responsibility of each individual council to determine that its investments are authorised in terms of the listed securities: [SAF 11] and J[27].

22. Under s 23A of the *Local Government Act* , the Director-General was authorised to issue guidelines to councils about the exercise of their functions: [SAF12] and J[28]. By s 23A(3) , "*a council must take any relevant guidelines issued under [s 23A] into consideration before exercising any of its functions*". [SAF12] and J[28].

23. The investment guidelines referred to in the DLG 2000 Circular (**Investment Guidelines**) stated that ratings were an independent assessment of the capacity of an instrument to meet its

obligations and, whilst ratings were in no way a guarantee against loss, "ratings provide the best independent information available": [SAF13], J[30] and J[2524].

24. On 27 November 2006, a date which is after Corowa, Eurobodalla, Parkes and Orange invested in Rembrandt 2006-3 but before the other Councils did so (although only by a few days in some cases), the Director-General of the Department of Local Government issued a further circular to all councils (**DLG 2006 Circular**): [SAF14] and J[31]. Part of the DLG 2006 Circular ([SAF14] and J[31]) stated:

> Following a recent survey it is apparent that some councils are not adhering to the current Ministerial Investment Order regarding the investment of funds. As a consequence, this circular replaces Circular 00/71 and should be read in conjunction with Circular 05/53 to further remind councils of their responsibilities.
>
> Councils must comply with the Ministerial Investment Order, section 625 of the *Local Government Act* 1993 and clause 212 of the *Local Government (General) Regulation* 2005 .
> ...
>
> Councils must consider the following when considering an investment:
>
> · the purpose of the investment
> · the desirability of investment diversification
> · the nature and risks associated with the investments
> · the likely income return and timing of any income return
> · the length of the proposed investment
> · the costs involved in making the investment
>
> · other matters as appropriate
>
> Councils need to be aware of their obligation to be transparent when reporting changes of value in investments. The onus for investments is to be on preservation of capital rather than the rate of return.
>
> As part of its overall financial plan, each council should develop and maintain an investment strategy/policy. The strategy/policy should, as a minimum, consider the desirability of diversifying investments and the nature and risk associated with the investments.
> ...

1.4 NSW Local Government Investments Best Practice Guide

25. The NSW Local Government Investments Best Practice Guide, referred to in the DLG 2006 Circular, was a draft document prepared by two industry bodies, Local Government Financial Professionals and Local Government Managers' Association: [SAF15] and J[32]. A number of the Councils were aware of, and had regard to, this document in preparing their investment policies and otherwise when undertaking investments: [SAF15] and J[32]. The draft document, which was initially issued in 2000 and re-issued in April 2006, included the following statements ([SAF15] and J[32]):

2. The Requirement for a 'Prudent Person' Approach to Funds Management

Section 11.3.5 of the Local Government (Financial Management) Regulation requires council to ensure

'it or its representatives exercise care, diligence and skill that a prudent person would exercise in investing council funds.'

Based on the above a prudent person is one who exercises the key elements of care, diligence and skill.

Whilst not exhaustive the following is a list of the matters a prudent person would be expected to consider:

i) read and understand the legislative framework around which council is to exercise its powers of investment
ii) adopt an investment policy and strategy (see examples in Appendix (4) to this guide)
iii) confirm who has the authority to place investments on council's behalf
iv) identify any internal gaps in knowledge required to adequately manage council's investments
v) ensure a suitably skilled member of staff is given day to day responsibility for the management of councils (sic) investments
vi) ensure staff involved in managing council's investments receive adequate training to undertake their role(s)
vii) consider the use of advisers (appropriately licenced (sic) by ASIC) to fill any knowledge gaps and to provide expert advice on individual investments and portfolio design and construction. Refer to Appendix 7 for suggested evaluation criteria for selecting an adviser.
viii) invest only in accordance with the legislation, investment policy and strategy
ix) determine the purpose of the investment (e.g. future needs of funds invested)
x) do not invest in products you do not understand and take the time to learn/understand available products
xi) consider how any proposed investment compliments other investments in the portfolio as part of ensuring appropriate diversification of investment style, issuer/manager and maturity profile.
xii) review investment performance and portfolio mix at least monthly with reference to a set market benchmark and council objectives
xiii) request investment institutions/managers/advisers/brokers to provide immediate feedback when significant and/or adverse events occur that relate to your investments
xiv) ensure council maintains title to funds invested
xv) report to council monthly in accordance with the legislation
xvi) reconcile investments held to general ledger at least monthly

xvii) review investment strategy at least annually
xviii) seek independent research and advice before investing in sophisticated investment types (eg. managed funds, floating rate notes – FRN’s or collateralised debt obligations – CDO’s)
xix) refer to Appendix 6 of this guide – ‘CDO Checklist’ before placing CDO investments

xx) Refer to Appendix 8 of this guide – ‘General Investments Checklist’ before placing general investments (ie. cash funds, enhanced cash funds, fixed interest funds, bank bills/NCD’s, floating rate notes, asset backed securities and bonds.

3. Development of an Investment Policy and Strategy

The Local Government Code of Accounting Practice & Financial Reporting requires council to maintain an investment policy and strategy and to review the strategy at least annually as part of its overall financial plan.

Example Investment Policy and Strategy documents are attached to this guide as Appendix (4).

In addition to the matters referred to in the example documents, in putting an Investment Policy and Strategy together you should consider the following:

i) are council’s objectives and philosophy in relation to desired investment outcomes clear eg. is council seeking to maximise returns within regulatory investment boundaries, or to generate reasonable (nominated by council) returns with lowest risk exposure to achieve that return
ii) have you assessed your council’s tolerance to risk (eg. to what levels is council willing to accept capital losses or significant fluctuations in returns)
iii) are council’s objectives in relation to return and risk reconcilable
iv) have you assessed your council’s expectations regards (sic) investment returns
v) does council have any environmental/ethical investment policies
vi) does council have any existing specific future uses for invested funds that would impact on the manner funds should be invested
vii) have you assessed the maximum and minimum terms over which investments should be placed
viii) does council have the systems in place to record and report on the investments it makes
ix) has council provided a commitment to staff training in relation to council’s investing activities
x) does council have a formal process for determining what funds should be invested (eg. daily cash-flow analysis)

xi) what are the benchmarks against which you will measure the performance of council’s portfolio.

2. LGFS

26. LGFS was established in 1979 as the financial services arm of the Local Government and Shires Associations, which operated as peak industry bodies for local government in New South Wales: [SAF40] and J[960]. In October 2004, LGFS was purchased by LGSS, a division of FuturePlus: [SAF40] and J[961].

27. Prior to its purchase by LGSS, all LGFS board members were councillors from New South Wales councils. After its purchase by LGSS, the LGFS board had six directors: three representatives of LGSS (who were also councillors) and three representatives of "various [l]ocal [g]overnment affiliated trade unions". The board later came to include a seventh member – a nominee of the Local Government Professionals Association: [SAF120] and J[1139].

28. Between 1986 and 1997, LGFS operated a deposit-taking institution for councils: [SAF121]. In 1997 or 1998, it launched its own funds management service, which involved accepting deposits from councils which were then deposited in a nominated LGFS facility (usually a short-term cash facility): [SAF123] and J[961]. LGFS would then aggregate the deposits for a particular facility and re-invest them with external fund managers: [SAF123] and J[961]. Mr Warwick Hilder was appointed as LGFS' Chief Executive Officer (**CEO**) in 1998: [SAF41] and J[1140]. One of his functions at the time of his appointment was to expand LGFS' operations to include a funds management service: [SAF41] and J[1140]. Subsequent initiatives included the development of a "Local Government Facility", which was a managed cash facility providing "socially responsible investment options for councils" and a "Committed Rolling Investment", which provided a floating rate of return and constituted "a series of term deposits joined together to provide an investment with a longer term": J[961]. By 2006, LGFS' "key business activity" was (as described by Mr Hilder) providing management services and facilities for local government entities in New South Wales: J[1140].

29. LGFS had a lengthy history of interactions with councils in New South Wales: [SAF42] and J [963]. LGFS presented its role to councils as helping councils to get the most out of financial markets: J[1141]. LGFS wanted the councils to "feel a strong relationship" with LGFS, acting as a sounding board by providing financial advice on an ongoing but informal (i.e., unpaid) basis: J[1141] and J[1147]. Both Mr Hilder and Mr Mark Tischler, a financial markets specialist with LGFS (who reported to Mr Hilder) agreed that LGFS wanted to be perceived by the councils as their confidant: J[1147] and J[1148]. The councils could only make investments in accordance with the relevant Ministerial Order, the relevant terms of which are set out at [20] above. Under the terms of the Ministerial Order in force at the relevant times, the councils could invest with LGFS regardless of whether LGFS carried a credit rating: J [962]. Nonetheless, LGFS sought and obtained a credit rating. At all material times, LGFS' rating was A/A1: [SAF122] and J[962].

30. During the relevant period, LGFS held two AFSLs: [SAF47] and J[2939]. The first was effective in the period from 5 November 2004 to 17 January 2007 (**First AFSL**). The second was effective in the period from 18 January 2007 until 30 June 2007 (**Second AFSL**): J [2939]. The First AFSL relevantly provided:

AUTHORISATION

This licence authorises the licensee to carry on a financial services business to:

(a) *provide financial product advice for* the following classes of financial products:

(i) deposit and payment products limited to:

A. basic deposit products;

B. deposit products other than basic deposit products;

(ii) *debentures, stocks or bonds issued or proposed to be issued by a government*;

…

(iv) *securities*; and

(b) *deal in a financial product* by:

(i) issuing, *applying for*, *acquiring*, varying or *disposing of a financial product in respect of* the following classes of financial products:

A. *securities limited to:*

1) *debentures of a body corporate or unincorporated body only*; and

(ii) applying for, acquiring, varying or disposing of a financial product on behalf of another person in respect of the following classes of products:

A. deposit and payment products limited to:

1) basic deposit products;

2) deposit products other than basic deposit products;

B. debentures, stocks or bonds issued or proposed to be issued by a government;

…

D. securities;

to wholesale clients.

(Emphasis added.)

31. In the Second AFSL, sub-paragraph (b) was altered to read as follows (emphasis added):

(b) *deal in a financial product by*:

(i) issuing, *applying for, acquiring*, varying or *disposing of a financial product in respect of* the following classes of financial products:

…

B. *securities limited to:*

1) *debentures of a body corporate or unincorporated body only.*

3. CPDOS AND STRUCTURED FINANCE PRODUCTS

32. The CPDO is a form of structured finance product: [SAF82] and J[55]. Structured finance products use mechanisms and instruments to transfer and allocate cash flows and risks associated with a pool or portfolio of assets. A mechanism commonly used in structured finance products is leverage. An instrument commonly used in structured finance products is the credit default swap (**CDS**): [SAF82] and J[55].

33. A CDS is a contract relating to credit default risk: [SAF83] and J[56]. A typical CDS involves one party (the protection seller) selling to another party (the protection buyer) protection against the risk of a credit event. The credit event, for example, may be a default (such as failure to pay or bankruptcy) by a single entity or a pool of entities. The protection buyer pays the protection seller a fee for the protection against the risk of the credit event (the **CDS premium fee**). In return, the protection seller pays a sum to the protection buyer on the occurrence of the credit event (the **CDS default payment**). The CDS premium fee is usually fixed at the outset and paid quarterly. The method of calculating the CDS default payment is also fixed at the outset and is paid only after the occurrence of a credit event. In other words, the CDS premium fee is certain (or subject only to the risk of default by the protection buyer under the CDS) whereas the CDS default payment is contingent on an event which may or may not occur in the future (the credit event in respect of the referenced entity or entities): [SAF83] and J[56].

34. The mechanisms which apply to an actual CDS can also be applied to a notional or synthetic CDS: [SAF84] and J[58]. A notional or synthetic CDS still involves a contract but the contract need not involve any actual CDS: [SAF84] and J[58]. Instead the contractual provisions create an arrangement which mirrors the cash flows that would occur if an actual CDS had been executed: [SAF84] and J[58].

35. The pool or portfolio which a CDS can reference is also flexible. Instead of referring to a single entity (or obligor) a CDS can refer to a pool of entities (or obligors). The entities are obligors because they are subject to credit obligations. In or about late 2003 and early 2004, the CDX North America Investment Grade Index (the **CDX**) and the iTraxx Europe Index (**iTraxx**) were created. The CDX lists 125 US investment grade obligors and the iTraxx lists 125 European investment grade obligors. Investment grade means the obligor is rated BBB or above by S&P (or its equivalent by other ratings agencies). The obligors are included in the

list by reference to a process which takes into account investment grade, liquidity and diversification across industry sectors. Both of these indices are rolled every six months in March and September of each year. On each roll, the identity of the obligors in the indices is reviewed. Obligors who have become sub-investment grade or illiquid (by reference to the index criteria) are removed from the index and replaced with investment grade obligors with the object of maintaining the index as one containing the most liquid 125 investment grade obligors across the diversified industry sectors: [SAF85] and J[59].

36. Together, if weighted 50% each, the CDX and iTraxx are referred to as the Globoxx Index (**Globoxx**): [SAF86] and J[60]. Globoxx consists of 250 obligors made up of the 125 US investment grade obligors on the CDX and the 125 European investment grade obligors on the iTraxx: [SAF86] and J[60]. The background to the development of the CDOs is described further in Part 3, Section 1.2 below.

4. ABN AMRO

37. Purchased by the Royal Bank of Scotland in 2007, ABN Amro is an investment bank with its headquarters in London: [SAF52] and J[678]. It created the CPDO in early 2006: [SAF53] and J[1].

38. The first tranche of CPDOs were issued in Euros, US dollars and Yen: [SAF53] and J[390]. Later in 2006, ABN Amro decided to market the CPDOs in other currencies, including the Australian dollar: [SAF53] and J[1]. The two Australian dollar issues were known as the Rembrandt 2006-2 and Rembrandt 2006-3 notes: [SAF53] and J[1]. The Rembrandt notes aimed to pay high periodic coupons by taking leveraged exposure to a notional portfolio of credit indices: [SAF88] and J[41]. The notional CDS index contract referred to the CDX and iTraxx indices (which were known as the Globoxx index when weighted 50% each): [SAF87] and J[61]. Under the notional CDS contracts, the investors were the notional sellers of protection against default by entities listed on the indices and the counterparty was the notional buyer of such protection: J[5] and [SAF87]. Although the CPDO evolved out of other structured financial products which ABN Amro and other financial institutions had developed (such as collateral debt obligations (**CDOs**) and constant proportion principal insurance (**CPPI**) and variants thereof), ABN Amro's CPDO was a new structured financial product which the market had not previously seen and which no ratings agency had previously rated: [SAF87] and J[61].

39. In early May 2006, ABN Amro approached S&P for the purposes of obtaining a credit rating for the CPDO: [SAF104] and J[95]-J[99]. ABN Amro obtained the rating because many potential investors would not have the resources or expertise to assess the creditworthiness of the CPDO or to second-guess the rating of a structured financial product and many institutional investors could only invest in products with an investment grade rating: J[2759] and J[2816]. ABN Amro's role is further explained below.

5. S&P

5.1 S&P's Ratings Business and General Practice

40. S&P, at the relevant time a division of the McGraw-Hill Companies, Inc., carried on a business of providing credit ratings, including through McGraw Hill International (UK) Limited, at the request of the issuer of an instrument to be rated: [SAF63], J[23] and J

[381]. S&P's business model for rating structured financial products depended on potential investors requiring banks and financial institutions to obtain ratings from internationally recognised credit rating agencies such as S&P: J[2524].

41. S&P was paid a substantial fee to assign a rating "knowing that the only purpose of its rating is to facilitate the marketing of the product": J[2787].

42. S&P described the meaning of its credit ratings in a document entitled "Issue Credit Ratings Definitions" which was available, amongst other places, on its public website: J[34], J[35] and J[1463(1)]. This publication does not suggest that the ratings scale can be understood only in the context of a report by S&P explaining the particular rating. It is a stand-alone document which assumes that the reader will correlate a rating to the definition. Relevantly, it described a AAA rating in the following way ([SAF103] and J[35]):

> An obligation rated 'AAA' has the highest rating assigned by [S&P]. The obligor's [the instrument's] capacity to meet its financial commitment on the obligation is *extremely strong*.
>
> (Emphasis added.)

S&P's default probability criterion for a 10 year financial instrument or product rated AAA was 0.728%: J[65]-J[66].

43. In its public statements, S&P explained that "an S&P rating of a financial instrument or product concerns only the likelihood that the principal and interest will be paid in accordance with the terms of the instrument or product being rated. An S&P rating of a financial instrument or product is not concerned with the nature, magnitude or consequences of default": [SAF102], J[35], J[63] and J[381]. Once a rating is assigned by S&P, S&P generally publishes the rating, including on its website: J[383]. It did so in this case.

44. S&P had specialised skills and knowledge relevant to forming an opinion as to the creditworthiness of obligors in general and of complex structured products in particular: J[68]-J[69].

5.2 Rembrandt 2006-2 and 2006-3

45. Rembrandt 2006-2 was issued on 5 September 2006: [SAF95] and J[670]. It was denominated in Australian dollars and had a subscription amount of AUD $50 million: [SAF95], J[670] and J[2754]. Rembrandt 2006-3 was issued on 2 November 2006: [SAF96] and J[670]. It was denominated in Australian dollars and had an initial subscription amount of AUD $40 million: [SAF96], J[670] and J[2754]. In January 2007, the subscription for Rembrandt 2006-3 was increased by $5 million: [SAF96], J[670] and J[2754]. S&P knew the Rembrandt notes were to be marketed by ABN Amro in Australia: J[227], J[229]-J[231], J[260] and J[290]. S&P knew that the notes could only be dealt with in tranches with a minimum issue price of $500,000 ([SAF98] and J[2754]) and consequently knew that the class of purchasers of Rembrandt 2006-2 was not more than 100 buyers and that the class of purchasers of Rembrandt 2006-3 was limited to not more than 80 buyers: J[495].

5.3 Rating of Rembrandt 2006-2 and 2006-3

46. S&P assigned ratings of AAA to the Rembrandt 2006-2 and 2006-3 notes: [SAF64], J[1], J[267], J[268] and J[318]. The sequence of events leading up to those ratings may be summarised as follows.

47. In early May 2006, ABN Amro retained S&P to rate the "anti-DPN" or Surf CPDO: [SAF104] and J[95]-J[99]. The anti-DPN is described at [164] below. On 6 June 2006, S&P informed ABN Amro that it was comfortable that the CPDO structure could be rated: [SAF105] and J[200].

48. S&P had access to substantial amounts of data, historical knowledge, complex modelling and the resources and personnel of ABN Amro's London office necessary to model the initial CPDO notes, a process which took well over a month and the expertise of a number of S&P skilled employees: J[76]-J[376], J[385]-J[388], J[498]-J[501] and J[691]-J[959].

49. S&P prepared and issued reports about Rembrandt 2006-2 (the **Pre-Sale Report**) and Rembrandt 2006-3 (the **Post-Sale Report**) (collectively, the **S&P Reports**): [SAF65] and J[43]-J[46]. The Pre-Sale Report prepared and issued by S&P on 11 August 2006 assigned a preliminary 'AAA' rating to Rembrandt 2006-2 and included the statement that (J[2530]):

> Information has been obtained by Standard & Poor's from sources believed to be reliable. However, because of the possibility of human or mechanical error by our sources, Standard & Poor's does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or the result obtained from the use of such information. Ratings are statements of opinion, not statements of fact or recommendations to buy, hold or sell any securities.
>
> …
>
> *Analytic services provided by Standard & Poor's Ratings Services (Ratings Services) are the result of separate activities designed to preserve the independence and objectivity of ratings opinions.* Ratings are statements of opinion, not statements of fact or recommendations to buy, hold, or sell any securities. Ratings are based on information received by Ratings Services.
>
> (Emphasis added.)

50. The Pre-Sale Report included the following (J[45]):

> **Constant Proportion Debt Obligation Synthetic Presale Report**
>
> **Rembrandt Australia Trust No. 2006-2**
> **A$100 Million Floating-Rate Notes**
>
> …
>
> This presale report is based on information as of Aug 11, 2006. The credit rating shown is preliminary. This report does not constitute a recommendation to buy, hold or sell securities. Subsequent information may result in the assignment of a final credit rating that differs from the preliminary credit rating. …

Class	Prelim	Prelim	Interest	Average	Legal

	rating*	amount (Mil A$)		life	final maturity
A	AAA	100	Three-month BBSW plus a margin	August 2013	August 2016

*The rating on each class of securities is preliminary as of Aug. 11, 2006 and subject to change at any time. Final credit ratings are expected to be assigned on the closing date subject to a satisfactory review of the transaction documents and legal opinion, and completion of a corporate overview. Standard & Poor's ratings address timely interest and principal on the notes.

Transaction Participants

Arranger	ABN AMRO Bank NV
Issuer	Rembrandt Australia Trust No 2006-2
Credit index portfolio administrator	ABN AMRO Bank NV
Reserve account provider	ABN AMRO Bank NV
Swap counter party	ABN AMRO Bank NV

Transaction Key Features

Expected closing date	August 2006
Structure type	Synthetic debt obligation
Portfolio composition	Corporate credit indices
Purpose of transaction	Arbitrage
Portfolio management type	Rules based rebalancing
Reinvestment period (years)	10
Weighted-average maturity of assets (years)	5

Supporting Ratings

Institution/role	Rating
ABN AMRO Bank NV as swap counterparty and reserve account provider	AA-/Stable /A-1*

Transaction Summary

Preliminary credit ratings have been assigned to the constant proportion debt obligations (CPDOs) to be issued by Rembrandt Australia Trust No. 2006-2.

Notable Features

This is the second CPDO structure rated by Standard & Poor’s that addresses the timely payment of interest and payment of principal. Previously, Standard & Poor’s has rated other credit CPPI transactions that have principal protection, and CDO transactions that have timely payment of interest and principal.

For this transaction, Standard & Poor’s assessed the possibility of the returns on the risky portfolio, plus the interest received on the risk-less deposit covering the full interest due on the note and principal at maturity. The analysis models the spreads on the credit indices, the default probability of constituents of these indices, the interest rate curve, and the effect of these on the returns earned through the structure.

The CPDO is a fixed-income instrument. It targets the payment of the stated coupons by taking variable leveraged exposure to a credit portfolio to generate sufficient returns to enable the coupon payments to be made.

The credit portfolio comprises two credit indexes (the credit index portfolio). The risk of these indexes will be passed on to investors, potentially until September 2016, through CDSs. The leveraged exposure will change over time. The arranger will calculate this exposure using a transparent and contractually agreed dynamic leverage control formula.

In addition, a CPDO differs from a standard single-tranche synthetic CDO in the following two ways:

- Under a standard single-tranche synthetic CDO, leverage is achieved by selling protection only on a specified tranche of a portfolio’s theoretical capital structure. Under the CPDO, protection will be sold on the full theoretical capital structure of the portfolio, on a non-tranched basis. In other words, investors will be exposed to the full loss risk on the index portfolios subject to a maximum loss equal to their investment. Mark-to-market gains, or losses on the sold protection do not depend on correlation, as the protection is sold on a non-tranched basis. However, leverage is created by the fact that the amount of protection sold can be a multiple of the total note notional amount.

- There is possibility of “cashing-in” to a risk-free coupon-paying bond before maturity. This would mean that credit risk is not taken for the full life of the note, as the credit portfolio will be unwound after a “cash-in” event.

Mechanics Of The Structure

Under a swap agreement, the proceeds of the notes will be deposited with ABN AMRO Bank N.V. (AA-/Stable/A-1+). At the same time, CDS protection will be sold on the credit-index portfolio (see chart 1).

The total notional amount of protection sold on the credit index portfolio will be such that the present value of the expected income from the credit index portfolio will sufficiently cover the difference between: (i) the present value of the coupons and the principal due under the note, and (ii) the net asset value (NAV) of the note.

The total notional amount is referred to as the target portfolio size. The NAV of the notes is calculated as the sum of the deposit value and the mark-to-market of the credit-index portfolio.

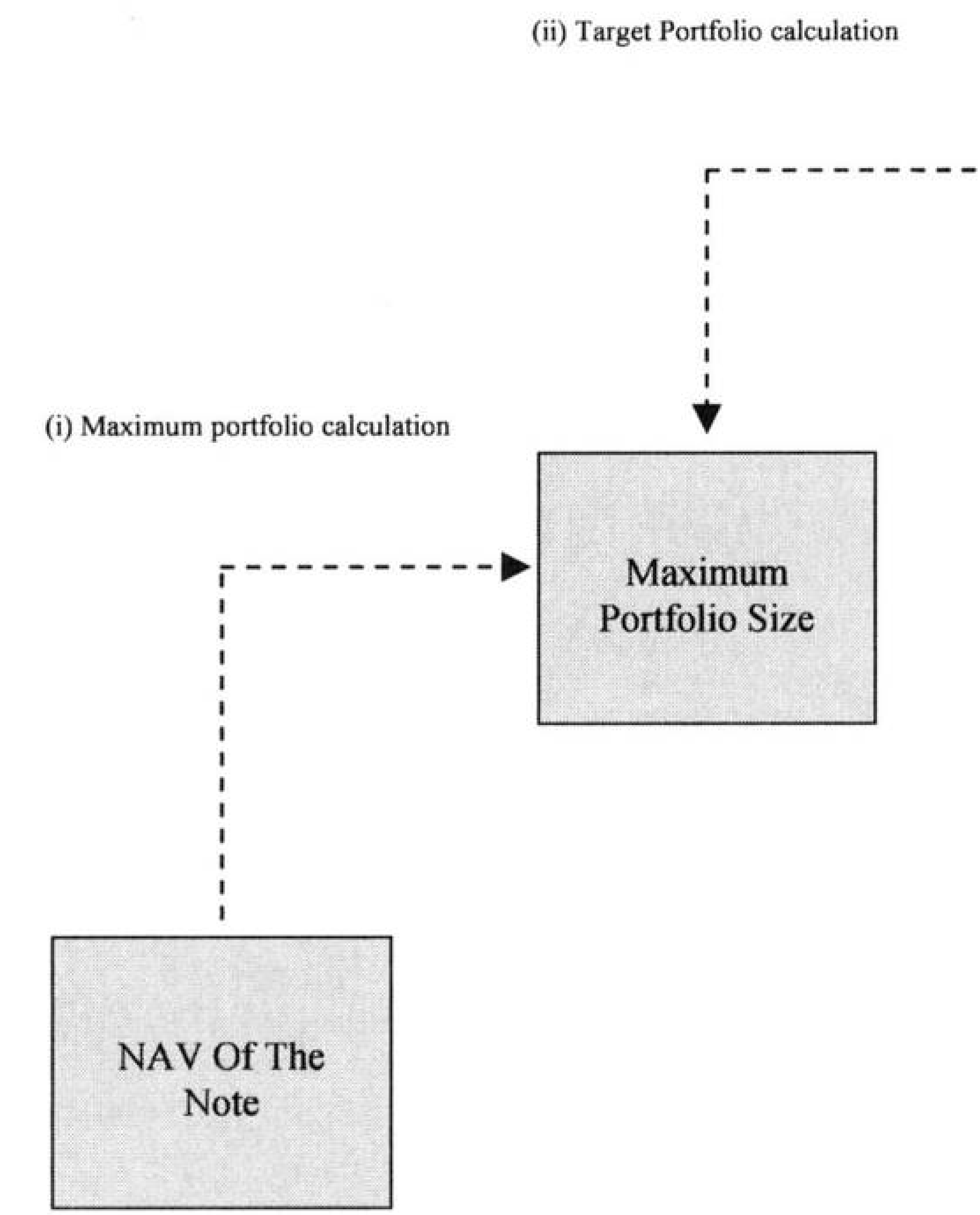
In addition, the target credit portfolio size has certain maximum size constraints. If the actual credit portfolio size differs from the target credit portfolio size by more than 25%, then the actual credit portfolio size is adjusted to equal the target credit portfolio size, subject to the maximum size constraints.

In other words, the CPDO only uses the leverage it needs to make the scheduled principal and interest payments. If the NAV increases, the target portfolio size will generally decrease as the portfolio needs to generate less income to meet coupon and principal payments. This mechanic constitutes the dynamic leverage control formula.

Once the current note NAV equals the present value of the payments under the note, the credit-index portfolio will be unwound and no further credit exposure will be taken (a cash-in event). If this occurs, all future payments due under the notes will be made, and no more exposure to a credit portfolio will be taken.

Conversely, if the current note NAV is equal to or lower than 10% of par, the credit-index portfolio will be unwound and no further credit exposure will be taken (a "cash-out" event). If this occurs, all coupon payments under the note will cease and the proceeds of the cash deposit will be returned to the noteholder (see chart 2 for the CPDO process).

Chart 2: CPDO Process



Standard & Poor's 2006

Strengths, Concerns, And Mitigating Factors

Strengths

CPDOs are designed with a high likelihood of cashing-in to a risk-free investment that pays the stated coupons and principal at maturity.

A highly rated bank will hold the note proceeds.

When compared with a static portfolio comprised of identical underlying reference entities, rolling the indices acts as a defensive mechanism that limits negative credit migration and default risk.

There is a high degree of transparency and liquidity in the on-the-run Dow Jones CDX, and the iTraxx European indices, which comprise the index portfolio.

The index credit portfolio is untranched. Therefore, correlation is unnecessary for the calculation of the CPDO NAV.

Concerns

A cash-out event will negatively affect interest payments and principal payment to investors.

Credit risk and marked-to-market losses associated with the index investments and the rules governing them, may negatively affect interest payments and principal payments to investors.

The extent of the portfolio's unfunded leverage is a source of risk.

Forward interest rate risk movements will affect the target portfolio size and leverage adjustments.

Mitigating factors

Standard & Poor's has analyzed the impact of the cash-out risk on interest and principal and has deemed it consistent with a 'AAA' rating.

Standard & Poor's has analyzed the various risks associated with the transaction, particularly expected marked-to-market losses (and gains), interest rate movements, credit losses due to defaults, and has concluded that the net impact on the probability of paying timely interest and full principal is consistent with a 'AAA' rating.

Spread widening, attended by no corresponding defaults, is beneficial to the structure.

The structure's leverage decreases with the net present value (NPV) of future coupons promised on the structure. Consequently, the cash-in time of the structure is modelled to be less than the actual maturity of the note.

Credit Portfolio Characteristics And Management

The credit portfolio is initially invested in two credit indexes – the Dow Jones CDX 6 and the iTraxx Europe 5. Dow Jones and iTraxx Ltd, publish a new series of indices at six-month intervals. The index rules determine which credits are discarded and which are added. Generally, these rules seek to maximize the liquidity of the names in the indexes, and to substitute out credits that are no longer eligible credits. One aspect of eligibility in the Dow Jones CDX 6 and iTraxx Europe 5, is that all credits must be investment–grade. This serves to limit the credit risk in the transaction. Under the terms of this issuance, the transaction will be rolled out of the old and into the new indexes with the index roll dates. The marked-to-market gains or losses incurred due to this rolling feature will be deducted or added to the deposit.

Redemption Of The Notes

The notes will be redeemed at maturity using the balance of the deposit account.

General Modelling Framework

Modelling of this CPDO transaction broadly falls into five categories: credit spread dynamics, interest rate movements, default correlation and timing, cashflow mechanics, and trading rules.

Spread dynamics

A logged "Ornstein-Uehlenbeck" spread process is employed to model the portfolio spread with the specifications of:

- A long-term mean (), a mean reversion speed (), and volatility ().

This spread process represents the weighed-average spread of the pool at any given time. The mean reversion speed and volatility are calibrated from historical indices data. For the long-term mean, instead of applying it as a constant throughout the life of the transaction in our modelling, Standard & Poor's uses a slightly lower number for the first year because of the benign spread environment. Standard & Poor's then increases the long-term mean at year two, and keeps it constant until the maturity.

This spread determines the yield received on CDSs held in the credit-risk portfolio. Referencing the duration of assets in the index and a credit DV01, spread changes translate directly into mark-to-market changes in credit-risky holdings. Naturally, spread changes also determine rebalancing events, or in extreme circumstances, cash-out events.

Interest rate movement

Standard & Poor's uses two separate interest rate processes to model the short-time rate and the full-term structure: (i) a mean reverting interest rate process used to model the short-term three-month bank bill swap rate accrued by the cash deposit account, and (ii) a single-factor mean reverting interest rate process used to model the full-term structure of the interest rate movement, and applied in the present value calculation. This "parametization" is consistent with Standard & Poor's interest rate criteria.

Default correlation and timing

The default times are generated by Standard & Poor's CDO Evaluator, and loss paths are computed. Recovery rates on any default are taken to be the average portfolio recovery at trade inception.

Depending on the notional value of protection sold and size of the reserve, losses may imply rebalancings or – in more extreme scenarios – cash-out events. Correlated defaults may cause shortfalls between the NPV of future promised cash flows, and the current portfolio value that exceeds the structure's ability to rebalance.

Cash flow mechanics

The treatment of index rolls, bid-offer spread effects, running fees reflecting transaction costs, and payment of coupons are a critical component of the model.

Trading rules

The enforcement of trade rebalancing rules determines the evolution of the size of the credit portfolio. These rules are based on monetary ratios, and are therefore dependent on the cash flow mechanics outlined in "Cash Flow Mechanics".

…

All criteria and related articles are available on RatingsDirect, the real-time Web-based source for Standard & Poor's credit ratings, research, and risk analysis, at www.ratingsdirect.com. The criteria can also be found on Standard & Poor's Web site at www.standardpoors.com.

51. On 5 September 2006, S&P issued a ratings letter to ABN Amro confirming that it had assigned a public credit rating of AAA to Rembrandt 2006-2 (**R-2 Ratings Letter**): [SAF68], [SAF110], J[268] and J[2528]. The R-2 Ratings Letter relevantly stated:

> Pursuant to your request that Standard & Poor's assign ***public*** *ratings* to the above-mentioned Notes, we have reviewed the information submitted to us and can confirm that we have assigned a ***public*** *rating of 'AAA' to the Notes*. If you have any questions concerning our approach to the assignment of the ratings, we will be pleased to answer them for you.
>
> *The rating is not investment, financial, or other advice and you should not and cannot rely upon the rating as such. The rating is based on information supplied to us by you or by your agents but does not represent an audit.* We undertake no duty of due diligence or independent verification of any information. *The assignment of a rating does not create a fiduciary relationship between you and us or between us and other recipients of the rating.* We have not consented to and will not consent to being named an "expert" under any applicable securities laws. The rating is not a "market rating" nor is it a recommendation to buy, hold, or sell any obligations.
>
> Standard & Poor's relies on the issuer and its counsel, accountants, and other experts for the accuracy and completeness of the information submitted in connection with the rating. *This rating is based on financial information and documents we received prior to the issuance of this letter.* Standard & Poor's assumes that the documents you have provided to us are final. If any subsequent changes were made in the final documents, you must notify us of such changes by sending us the revised final documents with the changes clearly marked. If the documents were not final, please be sure to send us black lined copies of the executed final documentation as soon as it becomes available along with a letter indicating that all changes have been so marked. In the event that we do not receive final papers within a reasonable amount of time, we reserve the right to withdraw our rating.
>
> *We will maintain continuous rating surveillance until the above-named securities mature or are otherwise retired.* To maintain the rating, Standard & Poor's must receive all relevant financial information as soon as such information is available. You must promptly notify us of all material changes in the financial information and the documents. In order to maintain our rating surveillance, we must receive all reports submitted to the Trustee in regard to the above captioned issue and all publicly distributed financial information, the absence of which may result in withdrawal of the ratings. Placing us on a distribution list for this information would facilitate the process. Standard & Poor's may change, suspend, withdraw, or place on Credit Watch the rating as a result of changes in, or unavailability of, such information. Standard & Poor's reserves the right to request additional information, if necessary, to maintain the rating. Please send all information to European CDO Surveillance, at Standard & Poor' s Ratings Services, 20 Canada Square, Canary Wharf, London, United Kingdom, E14 5LH, email: europeansurveillance@sandp.com.
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> We're pleased to have had the opportunity to be of service to you. Our bill for the analytical work performed on this financing will be sent to you in due course. For more information pleases visit our website at www.standardandpoors.com. If we can be of help in any other way, please do not hesitate to call upon us. Thank you for choosing Standard & Poor's, and we look forward to working with you.
>
> (Emphasis added.)

52. On 16 October 2006, before assigning the rating to Rembrandt 2006-3, S&P was told by ABN Amro that there was to be a single subscriber or "bespoke investor" for Rembrandt 2006-3: [SAF186], J[290], J[495] and J[2755].

53. On 31 October 2006, S&P issued a ratings letter to ABN Amro confirming that it had assigned a public credit rating of AAA to Rembrandt 2006-3 (**R-3 Ratings Letter**): [SAF68], [SAF112], J[318], J[1077] and J[2528]. The letter contained the same statements as the R-2 Ratings Letter: see [51] above. The same day, S&P informed ABN Amro's Australian office that it had assigned a AAA rating to Rembrandt 2006-3: [SAF112].

54. The terms of the Ratings Letters for the Rembrandt notes are significant: J[268] and J[318]. Each rating is described as a "public rating": see [51] and [53] above. S&P expressly authorised ABN Amro to disseminate each rating to potential investors, without restriction or limitation, and reserved the right to disseminate the rating itself: see [51] and [53] above and J[1027]. S&P undertook to maintain "continuous rating surveillance" and expressly reserved the right to alter the rating. S&P also described what the rating was not. Each rating confirmed S&P's public statements that the rating was a statement of S&P's opinion as to the notes' creditworthiness. The Ratings Letters did not say that S&P may not have a reasonable basis for its opinion as to creditworthiness or disclaim the reliability of S&P's opinion.

55. The Post-Sale Report was published by S&P on 15 November 2006: J[357]. It confirmed that S&P had assigned a public credit rating of AAA to Rembrandt 2006-3. The Post-Sale Report was distributed in Australia and a copy was provided to ABN Amro. The report available on the internet (from Ratings Direct) contained a different disclaimer from that in the Pre-Sale Report sourced from S&P: J[2520]-J[2521]. The Post-Sale Report included the statement extracted at [49] above as well as a statement that (see [SAF 67], J[47], J[2519], J[2530], J[2532], J[2534] and J[2536]):

> The credit ratings and observations contained herein are solely statements of opinion and not statements of fact or recommendations to purchase, hold or sell any securities or make any investment decisions. Accordingly, any user of the information contained herein should not rely on any credit rating or other opinion contained herein in making any investment decision.

The Post-Sale Report was in the same relevant terms as the Pre-Sale Report (see [50] above) except for the publication date, the fact that the report was described as Post-Sale rather than Pre-Sale and the statements that the report was preliminary had been deleted: J[46].

56. S&P was paid a substantial fee by ABN Amro for providing the rating for the Rembrandt notes. An annual fee was also payable by ABN Amro to S&P while S&P maintained the rating as current through its "rating surveillance": J[62], J[268] and J[384].

57. ABN Amro's purpose in obtaining the rating was to disseminate the rating to potential investors so that those persons could rely on the rating as S&P's expert opinion as to the creditworthiness of the Rembrandt notes: J[2480] and J[2781]. S&P knew that was the purpose for which the rating was obtained, and that it was paid to assign the rating, so that ABN Amro could carry out that purpose: J[2816]. In fact, S&P spoke to potential investors about the rating of the CPDOs: J[222], J[233]-J[235], J[253]-J[254] and [49]ff above.

58. This analysis is to no ultimate different effect from the analysis which can be distilled from the primary judge's reasons. It will be necessary to return to consider these facts later in the reasons for judgment.

6. SALE OF NOTES TO LGFS

59. The Australian branch of ABN Amro marketed Rembrandt 2006-2 to a number of institutional investors: [SAF54], J[1], J[267] and J[318]. These investors included FuturePlus (LGFS' ultimate parent company), which was introduced to the notes in early July 2006 when Mr Elliot Levick of ABN Amro contacted Mr Brad Storey of FuturePlus to inform him about the creation of Rembrandt 2006-2: [SAF107] and J[680]. Mr Storey and other representatives of FuturePlus attended a presentation on the notes on around 14 July 2006: [SAF107] and J [680]. The presentation was delivered by Mr Bevan Silvester, ABN Amro's local specialist for the CPDO: [SAF107] and J[680]. Mr Levick and Mr Hilder of LGFS also attended: [SAF107] and J[680].

60. This was not the first time that ABN Amro and LGFS had met to discuss LGFS' potential investment in structured financial products. On 6 March 2006, Mr Tischler of LGFS had met with Mr Paul Cordeiro, ABN Amro's Director, Head of Structured Credit Products, to discuss the ways in which ABN Amro "could assist in the repackaging of a disparate assortment of Council held CDOs into a securitised structure to produce a superior security … for resale to councils": J[1011]. This was part of LGFS' desire to become a player in the structured financial products market, the details of which are set out at [98]- [109] below. In April 2006, Mr Cordeiro sent an email to Mr Hilder in which he proposed a meeting between ABN Amro and LGFS to discuss the possibility of "ABN Amro working with LGFS to create a high quality CDO investment which would meet the objectives of NSW councils (that is, return above BBSW) plus a *high degree of security* and *rating stability* of the structure" (emphasis added): J[1022] and J[2997(1)]. ABN Amro knew that, despite its apparent interest in exploring new products, LGFS would only be interested in a product with a high degree of security: J[3088]. It is unclear whether or when the proposed meeting took place, but in any event it appears that no real progress was made until ABN Amro commenced its marketing of the Rembrandt notes.

61. ABN Amro had prepared a presentation for the purposes of marketing the notes to its clients (the **Surf Presentation**). The Surf Presentation had been under preparation from relatively early in the development of the CPDO: J[36]. A version of the presentation was finalised for the first version of the CPDO (known as Chess), and subsequent versions were prepared in similar terms for later iterations of the CPDO, including for the Rembrandt notes: J[36]. Mr Silvester presented to the attendees at the meeting in July 2006 using the Surf Presentation: [SAF107] and J[3095].

62. The AAA rating was an important feature of the Surf Presentation: J[2997(4)]. With its knowledge that LGFS would only be interested in a product with a high degree of security, ABN Amro highlighted and explained the rating in the presentation to encourage interest in the Rembrandt notes: J[2997(4)]-J[2997(5)] and J[3088]. The contents of the Surf Presentation (excluding the disclaimers which were included in small print at the bottom of each page and at the end of the presentation) were set out by the primary judge at J[37]:

1 SURF – The First CPDO

A Breakthrough in Synthetic Credit Investments

…

FOR INSTITUTIONAL INVESTORS ONLY

August, 2006

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Executive Summary

ABN AMRO is pleased to present Surf – the first Constant Proportion Debt Obligation (CPDO)

Surf is a new form of synthetic credit investment that carries a full AAA rating from S&P on both principal and coupons and pays a coupon of BBSW+[190]bps pa

Surf is designed to have a stable rating with a high likelihood of "cashing-in". After cash-in the CDS portfolio is unwound and no further CDS exposure is taken and all scheduled coupons and principal will be paid until maturity

Surf aims to pay high coupons by taking leveraged exposure to a basket of credit indices. Surf utilises variable leverage in order to control risk

The CPDO is suitable for investors who:

– Seek to take high grade exposure in a form that has not had value eroded by movements in correlation as has occurred in the CDO market
– Require high rating of principal and coupon payments, but without the necessity of principal protection
– Wish to diversify their current structured credit portfolio
– Require liquidity for structured products

Structured Credit – Recent History

The theme for structured credit investments linked to Investment Grade credit portfolios, has been one of consistent spread tightening over the past 3 years

While a portion of this spread compression can be accounted for by tighter corporate credit spreads due to the strong bid for credit, the impact of correlation has played a very significant part

The credit correlation market of May 2005 highlighted the volatility of correlation – since then it has steadily declined

This movement in correlation has led to a large amount of the value in mezzanine and senior tranches of CDOs to be eroded away, shifting value into the far riskier equity portion of the capital structure

The CPDO is a new form of high quality structured credit investment which does not rely on the level of correlation for pricing

While the CPDO will display some similar characteristics to a traditional CDO, such as highly rated principal and coupon payments, the price of the CPDO is not directly impacted by movements in correlation

Summary Terms & Conditions

Issuer	Rembrandt Australia Trust	**Issue Price**	100%
Swap Counterparty	ABN AMRO NV.	**Issue Amount**	AUD [100,000,000]
Rating	[AAA] by Standard & Poors*	**Scheduled Redemption Amount**	100%**

Scheduled Coupon	BBSW+[190]BPS pa**	**Maturity**	10 years after issue date
Credit Portfolio	Linked to highly liquid credit indices. Size determined by transparent non-discretionary rules	**Liquidity**	Daily, provided by ABN AMRO
Credit Indices	50% iTraxx Europe, 50% DJ CDX IG	**Fees**	1% arrangement fee 20 bppa administration fee, 4 bppa Leverage Facility Fee
...		...	

What is the CPDO?

A CPDO is a fixed income instrument with cashflows that have a high and rated likelihood of payment

A CPDO aims to pay the stated coupons by taking leveraged exposure to a notional portfolio of credit indices. It comprises of exposure to a Credit Index Portfolio and a cash deposit

The Credit Index Portfolio aims to generate sufficient returns to enable the coupon payments to be made

The Target Portfolio Size of the Credit Index Portfolio is set such that the present value of the expected income from the Credit Index Portfolio is linked to the difference between the present value of the coupons and principal due under the Note and Note NAV

Once the current Note NAV equals the present value of the payments due under the Note, the Credit Index Portfolio will be unwound and no further credit exposure taken ...

Dynamic Leverage Control

The Portfolio Size is dynamically adjusted in order to actively target payment of the stated coupon (BBSW+190bps pa) and repayment of the principal at maturity

The Current Portfolio Size is adjusted to equal the Target Portfolio Size on each roll date

In addition, if at any time the Current Portfolio Size differs from the Target Portfolio Size by more than 25%, then the Current Portfolio Size is adjusted to equal the Target Portfolio Size

The Current Portfolio Size cannot be larger than the Maximum Portfolio Size

Taking leverage in this controlled manner mans that there is no potential upside from over-leveraging, however investors are rewarded with a very tight distribution of returns and the potential to reduce the risk in the later years of the transaction ...

Behaviour of the Target Portfolio Size

The Target Portfolio Size is a dynamic measure designed to increase and decrease risk in a controlled manner

The Target Portfolio Size calculation has been designed such that the coupon and principal can achieve a high and stable rating, comparable to a CDO. **In essence, the CPDO only uses the leverage it needs to make the scheduled principal and interest payments**

Behaviour of the Maximum Portfolio Size

The Maximum Portfolio Size is a dynamic measure designed to limit the risk of the note

The Maximum Portfolio size is capped at an absolute value of 15 times note notional to control maximum risk

The Maximum Portfolio size is limited such that the maximum assumed 1 day loss on the Credit Portfolio cannot be more than the Note NAV, subject to the application of the Cap which is normally expected to cap the portfolio size

Forced unwinding of credit portfolio positions due to a reduction in the Maximum Portfolio Size is unlikely due to the expected application of the Maximum Portfolio Cap

Parameter	Action	Maximum Portfolio Size	
Portfolio Spread	↑	↓	This c defau perioc incon wider
Note NAV	↓	↓	This c defau perioc increa
Absolute Maximum Portfolio Cap	≤ 15 x Note Notional		This c noteh positi usuall noteh

Portfolio Characteristics

The credit portfolio is comprised of credit swaps on 5 year DJ CDX and iTraxx indices

– DJ CDX and iTraxx are liquid indices and provide broad diversified exposure to the credit market

Every six months, current index positions are unwound and new index swaps are entered into. This has 3 key benefits

– The credit indices are rolled over each 6 months into new series of indices. Rolling the index swaps ensures that the credit portfolio always references the latest index series and benefits from the index selection rules, i.e. entities downgraded to below investment grade and less liquid credits are removed and replaced by investment grade and more liquid entities

– Older series become illiquid quickly. Rolling the index swaps each 6 months ensures greater liquidity in the credit portfolio and help to keep rebalancing costs low

– Under normal market conditions income from extra premium and mark-to-market gains may be generated by extending the maturity of the index swaps to 5.25 yrs from 4.75 yrs at each index roll date

When compared to a static portfolio comprised of 50% DJ CDX Series 2 and 50% iTraxx series 1, rolling the indices acts as a defensive mechanism that limits negative credit migration and default risk

...

"Cashing-In"

If the Note NAV rises above the value of a AAA bond paying BBSW + 190bps pa plus administration expenses, a "cash-in" event will be triggered and the credit index portfolio and deposit will be fully unwound

Under the base case scenario[1], a cash-in is expected to occur on average after 6.8 years. This means that there is no further credit risk for the investor until maturity and all scheduled coupons and principal will be paid until maturity

Under a stable credit environment[2] a cash-in is expected to occur on average after 3.8 years

...

Hypothetical historical Cash-In Analysis

A hypothetical CPDO issued on any date between Feb 1996 and Aug 2003 should have already cashed in – investors would have no exposure to further credit risk
…

Why "CPDO"?

"CP" stands for Constant Proportion and offer the following advantages over traditional CPPI

– The CPDO is the first product utilising Variable Leverage technology to structure a note for credit investors who require a full rating for both principal and coupons
– Normal CPPI technology on fixed income assets takes a fixed income underlying and repackages it to produce equity like return distributions by always running at maximum leverage. The CPDO only leverages sufficiently to pay the stated coupon and principal at maturity
– Unlike traditional CPPI, the CPDO is more likely to sell protection at higher levels and buy protection back at lower levels
– Unlike traditional CPPI, there is much less likelihood of forced unwinding of portfolio positions due to risk limit breaches
– Unlike traditional CPPI, there is no principal protection, but both coupon and principal are rated, making the CPDO ideal for investors who are comfortable with the risks in structured credit but do not wish to pay for principal protection

"DO" stands for Debt Obligation and offers the following advantages over CDOs

– Unlike CDOs, there is a possibility of cashing-in, where the CDS portfolio is unwound and no further CDS exposure is taken. This means that credit risk need not be taken for the full life of the note
– The CPDO has no direct price exposure to correlation
– Like CDOs, both the coupon and principal are rated
– The CPDO does not suffer from adverse portfolio selection as the credit portfolio is linked to the on-the-run credit default swap indices

…

S&P Rating Methodology

S&P has determined that Surf will earn sufficient returns to pay timely coupon of BBSW+[190]bps pa and principal at maturity to achieve a AAA rating

The probability of receiving the rated coupons and principal at maturity is benchmarked to the default probability of an S&P bond with the same rating and tenor

There are three issues that are paramount in assessing the risks at a given rating level

– **Credit Spread Movements**

– The quantitative analysis of the rated return must assess the income and mark-to-market gains and losses due to the reconfiguring and rebalancing of the CDS indices over the life of the transaction. Spread changes may also trigger a cash-out event

– Credit spreads are modelled using a modified Leverage Super Senior framework

– **Credit Defaults**

– Credit defaults are generated by S&P's CDO Evaluator

– **Structural Considerations**

– Rebalancing rules, treatment of index rolls, bid/offer spread effects, running fees, payment of coupons, in addition to the market and credit risk of the index portfolio, are taken into account in the rating modelling process

AAA Rating

Target rated return is BBSW+[190] bps pa

The S&P 10 year AAA cumulative default probability is [0.728]% (emph asis added)

The total numbers of paths in which the BBSW+[190]bps pa is not achieved must be lower than the target probability commensurate with a AAA rating and tenor

A return of at least BBSW+[190]bps is achieved in at least [99.272]% of the simulations, which is consistent with a 10 year AAA rating

	AAA	AA+	AA	AA-	A+	A	A-	BBB+
1	0.000%	0.002%	0.013%	0.024%	0.027%	0.033%	0.049%	0.234%
2	0.009%	0.017%	0.062%	0.078%	0.097%	0.121%	0.185%	0.514%
3	0.030%	0.050%	0.135%	0.166%	0.212%	0.263%	0.396%	0.850%
4	0.065%	0.104%	0.232%	0.290%	0.372%	0.459%	0.676%	1.246%
5	0.118%	0.182%	0.356%	0.452%	0.578%	0.709%	1.020%	1.704%
6	0.190%	0.287%	0.512%	0.654%	0.830%	1.013%	1.424%	2.221%
7	0.285%	0.420%	0.701%	0.897%	1.128%	1.368%	1.883%	2.792%
8	0.405%	0.584%	0.927%	1.182%	1.472%	1.774%	2.395%	3.413%
9	0.552%	0.781%	1.191%	1.509%	1.859%	2.226%	2.954%	4.076%
10	0.728%	1.013%	1.493%	1.876%	2.290%	2.724%	3.557%	4.777%

Rating Sensitivity

The performance and rating of the CPDO is sensitive to the evolution of credit spreads, defaults over time, and roll costs

The rating of the CPDO appears to be stable under a range of simulated default, credit spread scenarios, and roll costs as illustrated below

…

In the above analysis, the rating model was run from the issue date to the forward rating simulation point using the default end spread paths illustrated in order to model the note performance to the rating simulation point. The spread starts from an initial spread of 36bps and increases linearly at the rate shown per annum until the rating simulation point with S&P base case assumption for curve shape in all scenarios and roll cost for scenarios 1 and 2. The rating model is then re-run using the current S&P base case modelling assumptions at that future point in time to determine a potential rating. No assurance can be given with respect to future performance or future ratings. The assumptions underlying the analysis illustrated above are unlikely to be consistent with actual experience. In addition, S&P can change their rating assumptions, rating models and the way they monitor the rating at any time.

…

Conclusion

Surf is a unique assets class and is the first fully rated product in the credit market that uses an alternative leverage technology to traditional CDOs

Surf notes offer the opportunity for traditional fixed income investors to achieve stable, rated regular coupons with a tight fixed income like distribution of returns and will expand the universe of investors who can participate in the credit product space

As the value of AAA CDO and LSS tranches eroded over the past year largely because of correlation sensitivity, Surf can achieve superior returns in the form of a highly rated leveraged product where pricing is not dependent on correlation risk

When compared to similar fixed income synthetic credit products, Surf exhibits strong relative value

Surf references highly liquid credit indices which are transparent, rules based and non-proprietary. Exposure to these indices ensure liquidity, no adverse selection and relative WARF stability

Key Risk Factors

Credit Risk

Investors are exposed to the credit risk of the underlying credit portfolio

In case of defaults or spread widening, the Note NAV will be negatively affected and the size of the credit portfolio may be increased or reduced

Leverage may increase the magnitude of losses

The Note is not guaranteed by ABN AMRO. CPDO is not a principal protected note. Actual amounts of interest and principal paid on the notes are subject to the investment strategy performance

Correlation Risk

As Surf references index swaps, moves in correlation will not directly affect the NAV of the notes

Price Volatility

The NAV of the note is sensitive to credit spreads of the underlying portfolio of index swaps

The price of the notes may be lower than the initial purchase price

The traded price may be different from the NAV of the notes due to supply and demand issues

Leverage may increase the magnitude of price volatility

Cash-Out Event

If the NAV falls to 10% or lower, a "cash-out" event will be triggered and the credit portfolio is fully unwound

No coupon will be paid after a cash-out event and any recovered value will be paid to noteholders

Performance and modelling risk

Past performance may not be representative of future performance

Current modelling assumptions are unlikely to be consistent with actual performance of CPDO

Key modelling assumptions are set out in S&P base case assumption

63. The primary judge emphasised the following features of the Surf Presentation and how it described the CPDO (J[3095]):

1. It represented the CPDO as a breakthrough in synthetic credit investments, such breakthrough being the result of the combination of coupon at 190 bps and the rating of AAA on coupon and principal.

2. The product was "designed to have a stable rating", which the primary judge found could "mean only that it [was] designed to have a stable rating of AAA on both principal and coupon".

3. The product was suitable for investors who "require high rating of principal and coupon payments".

4. The target portfolio size calculations of the product had been "designed such that the coupon and principal can achieve a high and stable rating".

5. The product offered investors higher coupons than many other fixed income instruments with similar ratings.

6. It contained a detailed discussion of S&P's rating methodology, including the statement that the "probability of receiving the rated coupons and principal at maturity is benchmarked to the default probability of an S&P bond with the same rating and tenor" and that the "S&P 10 year AAA cumulative default probability is [0.728]%".

7. It stated that the "total number of paths in which the **BBSW** + [190] bps pa is not achieved must be lower than the target probability commensurate with a AAA rating and tenor" and a "rating of at least BBSW + [190] bps pa is achieved in at least [99.272]% of the simulations, which is consistent with a 10 year AAA rating".

8. It contained an extract from S&P's target probabilities or ratings quantiles tables.

9. It contained a section on rating sensitivity based on ABN Amro's modelling.

10. It repeated references to the product being the "first fully rated" product of its kind, with "stable, rated regulated coupons", and "superior returns in the form of a highly rated leveraged product".

64. In the course of oral submissions, counsel for LGFS identified particular aspects of the Surf Presentation. There is a degree of overlap between the aspects of the presentation we were taken to and those emphasised by the primary judge in her reasons but it is nonetheless necessary to consider these aspects of the Surf Presentation in some detail.

65. Page 3 of the Surf Presentation contained an executive summary of the presentation. It stated that the CPDO was "designed to have a stable rating with a high likelihood of 'cashing-in'". It further stated that:

> The CPDO is suitable for investors who:
> - Seek to take high grade exposure in a form that has not had value eroded by movements in correlation as has occurred in the CDO market
> - Require high rating of principal and coupon payments, but without the necessity of principal protection
> - Wish to diversify their current structured credit portfolio
> - Require liquidity for structured products

66. Page 6 of the presentation comprised a single heading – "Surf Structural Mechanics". What followed this page was a number of diagrams which described how the actual structure of the CPDO worked and how the relevant formula was supposed to work. Page 9, for instance, set out how the coupon reacted with various movements in the market. It stated that the "calculation [had] been designed such that the coupon and principal can achieve a high and stable rating, comparable to a CDO. In essence, the CPDO only uses the leverage it needs to make the scheduled principal and interest payments".

67. Page 17 of the presentation provided a favourable comparison of the CPDO with traditional CPPI. Notably, it stated that "[u]nlike the traditional CPPI, the CPDO is more likely to sell protection at high levels and buy back at lower levels".

68. Immediately preceding page 17 was a page headed "Hypothetical historical Cash-In Analysis". It set out a pro-forma spread history in graphical form and, importantly, showed that the CPDO retained the ability to cash-in despite an increase in spreads and defaults. There was a series of statements at the bottom of the page. One of these statements clarified that the parameters used for the production of the graph were "run through the CPDO model (which has certain other modelling assumptions, including roll cost and curve shape as per S&P base case assumptions)". The natural implication was that the graph had been produced by ABN Amro using its own model, albeit with certain assumptions that were consistent with the assumptions adopted by S&P. There was, however, no suggestion that S&P was responsible for the information being conveyed by the graph.

69. The last three pages of the Surf Presentation contained a disclaimer, the key aspects of which were as follows:

> No representation, warranty or assurance of any kind, express or implied, is made as to the accuracy or completeness of the information contained herein. ABN [Amro] accepts no obligation to any recipient to update or correct any such information. No act or omission of ABN [Amro] or any of its directors, officers, employees or agents in relation to the information contained herein shall constitute, or be deemed to constitute, a representation, warranty or undertaking of or by ABN [Amro] or any such person. This presentation may contain forward-looking information. Such information may include, among other things, projections, forecasts or estimates of cashflows, returns, scenario analyses and proposed or expected portfolio composition.
> …
> Further, the information in this presentation reflects ABN [Amro's] opinions or views prevailing as of this date, which are accordingly subject to change without prior notice to you. The information in this presentation does not take into account the effects of a possible transaction or transactions or any other event, including with limitation an actual or potential change of control in the relevant entity, which may have significant valuation and/or other effects on the proposed transaction or transactions.
> …
>
> By accessing this presentation and before entering into any transaction each recipient represents, warrants and agrees that (i) they are considering this investment for their own account, (ii) they are a professional/institutional/accredited/expert investor with sufficient knowledge, experience and professional advice to make their own evaluation of the merits and risks of making a complex investment of this type, (iii) they shall, at all times, be solely responsible for making their own independent appraisal of the reference entity(ies) and investigation into the business, financial condition and creditworthiness thereof, (iv) they are fully aware that they may lose a significant amount or all of their investment, (v) they are responsible for making their own independent investigation and appraisal of the risks, benefits and suitability of any investments envisaged by this document, and for obtaining their own independent financial advice, and (vi) ABN [Amro] shall not incur any responsibility or liability whatsoever to any recipient in respect thereof.

70. The primary judge held that the parts of the disclaimer which might be relevant were "not prominent" and there were no "headings or other signposts leading the reader to the statements which might be relevant": J[3101]. Her Honour found that the disclaimer as to the existence of any representation, warranty or assurance said "nothing about the reliability of the AAA rating and no reasonable reader would read it as saying anything about the rating": J [3101]. Further, the statement that the Surf Presentation reflected ABN Amro's "opinions or views prevailing as of this date" undermined ABN Amro's argument that it was merely passing on the rating: J[3102]. The primary judge held that the disclaimers were, therefore, ineffective.

71. On 18 July 2006, Mr Levick of ABN Amro emailed the draft term sheet for Rembrandt 2006-2 to Mr Storey of FuturePlus: [SAF152] and J[680]. Mr Storey forwarded that draft term sheet to Mr Hilder of LGFS on the same day: [SAF152] and J[1025]. In July or August 2006, Mr Hilder and Mr Tischler (from LGFS), who also attended the meeting on 14 July 2006, met with representatives of ABN Amro, at which they were given, and taken through, the Surf Presentation: [SAF155], J[1028], J[1164], J[1166], J[3095], J[3097] and J[3189]. Mr Hilder could not recall what was said at the meeting but remembered that either at the meeting or

shortly thereafter both he and Mr Tischler were informed that it was expected that the CPDO would carry a AAA rating: J[1164]. Mr Hilder recalled that Mr Tischler asked a number of questions at the meeting that lead him to believe that Mr Tischler had a better understanding of structured products generally and the CPDO specifically: J[1164]. But nonetheless Mr Hilder understood from the Surf Presentation that S&P had undertaken over 10,000 Monte Carlo modelling simulations to test the performance of the Rembrandt notes under different market conditions, and that S&P had estimated the 10 year cumulative default probability of the Rembrandt notes at "less than 1%": J[1167]. Mr Hilder understood from what he had read that the Rembrandt notes' AAA rating meant that they had a "0.76% chance of default": J[1167]. The only evidence of an explanation of the rating in terms of a percentage or numerical possibility of default was the explanation ABN Amro gave LGFS in and by speaking to the Surf Presentation: J[1167]. In the weeks following the meeting, Mr Hilder spent a lot of time "reading and re-reading" the Surf Presentation and the relevant term sheets in order to develop a level of understanding of the product to enable him to assess whether LGFS should purchase the Rembrandt notes for sale to the Councils: [SAF156] and J [1164]. At some point in August 2006, Mr Hilder believed that he had reached the point where he understood how the Rembrandt notes worked and each component of the notes: J [1172].

72. On 4 August 2006, Mr Levick emailed the draft of the Pre-Sale Report to Mr Storey: [SAF154] and J[231]. On 22 August 2006, Mr Tischler received a copy of the Pre-Sale Report: see [49] above and J[1173]. He considered the report to be "overall supportive of the Rembrandt notes" and that S&P considered the risk of loss involved to be "very low": J [1175]. Mr Hilder also read the Pre-Sale Report and, while he considered that it did not contain any information that was new to him, he noted the following aspects of the Pre-Sale Report: J[1173]:

> • Rembrandt was a "fixed-income instrument" which targeted the payment of coupons by "taking variable leveraged exposure to a credit portfolio to generate sufficient returns to enable the coupon payments to be made";
> • Rembrandt's credit portfolio comprised two credit indices, the risk of which would be "passed on to investors" through credit default swaps, with the leveraged exposure changing over time according to a "transparent and contractually agreed dynamic leverage control formula";
> • S&P had analysed "the various risks associated with the transaction" (particularly mark-to-market losses, interest rate movements, and the risk of credit defaults), and had concluded that "the net impact on the probability of paying timely interest and full principal" was "consistent with a AAA rating"; and
> • the statement that "spread widening, attended by no corresponding defaults, is beneficial to the structure".

LGFS did not know that ABN Amro had participated in the drafting of the Pre-Sale Report: J [3098].

73. On 11 August 2006, Mr Simon Michell, a financial markets dealer with LGFS, received an email from ratingsdirect@standardandpoors.com which contained a "research update" indicating that S&P had assigned a preliminary credit rating to Rembrandt 2006-2: [SAF157] and J[1027].

74. On 21 August 2006, Mr Hilder sent an email to Mr Levick stating that he "would like to progress the evaluation of this possible transaction" and that he also wanted to discuss white badging the product: [SAF160] and J[1178]. By this stage, Mr Hilder had effectively delegated to Mr Tischler the responsibility of dealing with ABN Amro: [SAF161] and J [1172]. Mr Tischler met with Mr Levick on or after 21 August 2006 to discuss the possibility of white badging the notes: [SAF162] and J[1178]. Mr Tischler accepted that LGFS was interested in white badging the notes so that councils would perceive LGFS to be "associated with" the product: J[1178]. This association would make the products more attractive to councils by giving it a local government "feel" and would assist LGFS to leverage off its rapport with councils: J[1178] and J[1278].

75. Mr Levick was subsequently involved in various email communications with LGFS. With some exceptions, he could not recall any specific dealings with LGFS. The extent of his recall was set out by the primary judge at J[682] (see also [SAF166]):

> Mr Levick was involved in various email communications with LGFS but had no specific recollection of other direct dealings with LGFS apart from: – (i) ABN Amro informing LGFS of its expectation, and then the fact, of S&P giving the Rembrandt CPDOs a rating of AAA, (ii) Mr Hilder proposing that an issue of the Rembrandt CPDO be "white-badged" for issue by LGFS to its clients, (iii) Mr Hilder saying to him that LGFS had to be "very thorough and make sure [we] understood the details of the CPDO before selling it to" LGFS's clients, (iv) Mr Hilder and Mr Tischler asking Mr Levick and Mr Silvester a lot of questions about the CPDO during LGFS's due diligence process, and (v) Mr Hilder and Mr Tischler never said anything to suggest that they did not understand the nature of, or risks associated with, the Rembrandt CPDOs.

Mr Levick's recollection of his communications with LGFS discloses that ABN Amro emphasised its expectation that the CPDO would receive a AAA rating. The AAA rating was extremely important to LGFS: J[1293]. The evidence before the primary judge disclosed that both Mr Hilder and Mr Tischler considered that a AAA rating was "essential" for any product which was to be marketed by LGFS: J[1293]. ABN Amro knew that it was a pre-condition of LGFS' purchase of the Rembrandt notes that they obtain a rating of AAA. This was especially so given LGFS' relative inexperience in dealing in structured financial products (J [1293]) and its inability to verify the reliability of the rating: J[3197].

76. On 31 August 2006, Mr Hilder and Mr Tischler met with representatives of ABN Amro: [SAF168] and J[1040]. Later that day, Mr Tischler sent an email to Mr Brandon Lewis, a member of ABN Amro's structured credit team in Australia, which stated that StateCover had authorised LGFS to transact on its behalf in relation to Rembrandt 2006-2: J [1040]. Mr Tischler's email also stated that LGFS would purchase $4 million of Rembrandt 2006-2 and confirmed that StateCover would purchase $6 million: J [1040]. LGFS subsequently transferred the notes it purchased in its own name to StateCover: J[2982]. On 1 September 2006, Mr Levick sent an email to Mr Tischler which confirmed LGFS' and StateCover's purchase of Rembrandt 2006-2 and which attached the final term sheet for the transaction: [SAF170] and J[1041]. The final term sheet mistakenly recorded the issue date: J[1041]. On the same day Mr Levick sent to Mr Tischler an amended version of the final term sheet: J[1041]. Mr Tischler forwarded the final term sheet to Mr Hilder: J[1041].

77. On 4 September 2006, Mr Levick sent an email to Mr Tischler which attached a transfer and acceptance form for LGFS' investment in Rembrandt 2006-2. On 5 September 2006, a StateCover Authorisation and Dealing Docket was completed for StateCover's purchase of Rembrandt 2006-2. Mr Hilder signed the transfer and acceptance form on behalf of StateCover on that day: J[1044]. S&P issued the R-2 Ratings Letter the same day and it was provided to LGFS before LGFS caused StateCover to purchase the Rembrandt 2006-2 notes: see [50] above.

78. LGFS purchased the Rembrandt 2006-2 notes on behalf of StateCover in its capacity as a fund management service provider: J[1176]. The terms of the parties' relationship were set out in an agreement embodied in a letter dated 14 September 2004 between LGFS and StateCover: [SAF221] and J[3681]. After Rembrandt 2006-2 cashed out, StateCover commenced proceedings against LGFS seeking in excess of $9 million (together with interest and costs): [SAF236], J[2400] and J[2980]. StateCover also claimed against ABN Amro and S&P: [SAF236], J[2400], J[2980] and J[1180]. On 29 August 2011, LGFS settled StateCover's claim as against all parties for a sum in excess of $3.1 million (including costs): [SAF236], J[2400] and J[2980].

79. On 7 September 2006, Mr Levick sent an email to Mr Tischler and Mr Hilder which outlined possible fee structures for the next issue of the CPDO, which became the Rembrandt 2006-3 issue: [SAF175], J[1045] and J[1046]. On the same day Mr Tischler sent an email to Mr Hilder indicating his preference with respect to the fee structures suggested by Mr Levick: [SAF175], J[1045] and J[1046].

80. In September 2006, Mr Hilder prepared a document entitled "ABN's SURF CPDO Product" which listed the pros and cons of CPDOs: [SAF173] and J[1049]. On 28 September 2006, Mr Tischler sent Mr Levick and Mr Lewis a marked-up term sheet which set out a number of further questions by Mr Tischler about the CPDO: [SAF177], J[1048] and J[1303]. Mr Silvester provided responses to Mr Tischler on 4 October and 6 October 2006, the former response in relation to the adjustment to the cash deposit value following a credit event and the latter response in relation to the Maximum Index Portfolio Amount: [SAF178] and [SAF180]. On 9 October 2006, Mr Silvester sent Mr Tischler a further email which provided some "additional scenarios" from Rembrandt 2006-2: [SAF181] and J[1054]. These additional scenarios covered "extreme movements in spread" which showed "the robustness of the structure": [SAF181] and J[1054]. Mr Tischler and Mr Hilder were also assisted by Mr Lewis, who attended a meeting with Mr Tischler and Mr Hilder at which a private placement of the notes to LGFS was discussed and who answered questions asked by Mr Tischler from time to time: [SAF187] and J[672]. When a question related to a matter outside his area of responsibility, Mr Lewis would refer Mr Tischler to Mr Silvester or Mr Levick: [SAF187] and J[672].

81. By October 2006, Mr Tischler considered that he "generally understood how the mechanics of [the Rembrandt notes] worked" and believed he had "taken [his] investigation of the [Rembrandt] notes as far as [he] could". Mr Tischler recalled a conversation with Mr Silvester in or about mid October 2006 during which Mr Silvester said words to the following effect (J[1181]):

1. As the spread movement in the indices was over par, LGFS should settle the purchase of Rembrandt 2006-3 in order to take advantage of spread tightening;

2. This would result in LGFS making a capital gain;

3. If spreads widened again, the value of Rembrandt 2006-3 would decrease as demonstrated by the scenarios ABN Amro had sent to Mr Tischler;

4. Rembrandt 2006-3 was a robust structure which could withstand even significant spread widening; and

5. Mr Silvester would send Mr Tischler further information on the current movement of credit spreads.

82. On 11 October 2006, Mr Tischler emailed Mr Silvester requesting a soft copy of what was termed a Mandate Letter which it was proposed would be executed by LGFS and ABN Amro: [SAF183] and J[1058]. The purpose of the Mandate Letter was to set out the "terms upon which [LGFS was] invited to appoint ABN Amro as structurer in relation to [LGFS'] firm order [of Rembrandt 2006-3]": J[1061]. Mr Silvester complied with Mr Tischler's request: [SAF183] and J[1058].

83. On 13 October 2006, Mr Tischler once again wrote to Mr Silvester, informing him that LGFS had provided the Mandate Letter to its solicitors, Mallesons Stephen Jaques, for review and they had identified certain issues which were contained in a single-page document headed "Issues with ABN Mandate Letter": [SAF184] and J[1059]. On 16 October 2006, Mr Silvester replied to Mr Tischler indicating that ABN Amro had amended the Mandate Letter to address the issues raised by LGFS' solicitors and that a signed copy would be sent to LGFS once it had agreed to the changes: [SAF184] and J[1059]. The **Mandate Letter** relevantly stated (at J[1061]):

> Dear Sirs,
>
> **MANDATE FOR STRUCTURING A SURF CPDO NOTE THAT LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED WILL PURCHASE.**
>
> ABN AMRO Bank NV ("**ABN [Amro]**") is pleased to set out in this mandate letter ("**Mandate Letter**") the terms upon which Local Government Financial Services Pty Limited (the "**Company**") (each of ABN [Amro] and the Company a "**Party**" and together the "**Parties**") is invited to appoint ABN [Amro] as a structurer in relation to their firm order to purchase of AUD 40 million of SURF, a CPDO Note linked to a portfolio of Credit Indices managed by ABN [Amro] (*as described in the attached indicative termsheet*). Such proposed purchase is referred to in this Mandate Letter as the "**Transaction**".
>
> …
>
> **1. SERVICES**
>
> 1.1 The Company hereby appoints ABN [Amro] to use all reasonable endeavours to perform such services as both ABN [Amro] and the Company agree to be necessary to successfully close the Transaction (the "**Services**"). The Company agrees that ABN [Amro] shall be the only party appointed to carry out the Services and it will not engage (directly or

indirectly) any other party in connection with the Services without ABN [Amro's] prior written approval.

1.2 The Services will include, but are not limited to, the following:

1.2.1 to model and structure the Transaction;

1.2.2 to prepare a termsheet which will detail, *inter alia*, the following items: (i) the structure of the Transaction, and (ii) the size and characteristics in respect of the Transaction;

1.2.3 to perform such other services as may be mutually agreed in writing between the Company and ABN [Amro] as necessary to successfully Close the Transaction.

1.3 The obligations of ABN [Amro] in respect of the Transaction are several and not joint vis-à-vis the obligations of any third party appointed in respect of the Transaction.

1.4 The Company hereby authorises ABN [Amro] to do all such things that are reasonably necessary for the proper performance of its engagement as sole structurer in respect of the Transaction.

…

3 PARAMETERS OF ABN AMRO'S ROLE

3.1 Until Close of the Transaction or termination of ABN Amro's engagement pursuant to clause 7 below, neither the Company nor any of the Company's Associates will initiate discussions with or respond to proposals from third parties other than its own independent legal or accounting advisors regarding the Transaction … except with the prior consent of ABN Amro. …

3.2 ABN [Amro] will have no responsibility for providing or obtaining on the Company's behalf any legal, regulatory, accounting, taxation or other specialist advice in connection with the Transaction. The Company shall be responsible for obtaining any such advice from independent advisors which the Company has chosen and may not rely on ABN [Amro] for any such advice. Any such advice provided to the Company shall be the direct legal responsibility of the provider of such advice and not of ABN [Amro].

…

3.4 The Company acknowledges that ABN [Amro] is not acting as fiduciary but is an independent contractor retained solely for this Transaction. Defining the scope of any due diligence exercise, conducting any due diligence, analysis of any due diligence results, and the prudence, desirability and commercial merits of the Transaction are all entirely decisions for and ultimately the sole responsibility of the Company. Any valuation or other analysis undertaken by ABN [Amro] is provided on the

> understanding that ABN [Amro] does not accept responsibility for the accounting or other data (including commercial or technical assumptions) on which such analysis is based and it is the Company's sole responsibility to assess and evaluate such analysis, advice, data and assumptions. Advice, communications and services provided by ABN [Amro] under this Mandate Letter are intended solely for the benefit of the Company in relation to this Transaction and shall not be used for any other purpose and may not be disclosed to, used or relied upon by any other person without ABN [Amro's] prior written consent. No opinion or advice rendered by ABN [Amro] or any of its Associates may be construed as a recommendation to any person as to what action they should take in relation to the Transaction.

(Emphasis added.)

84. The indicative draft term sheet relevantly stated:

The Notes are expected to receive a full AAA rating from S&P.

Issuer	Rembrandt Australia Trust
Arranger	ABN AMRO Bank NV
Issue Price	100%
Issue Date	[27 October] 2006
Maturity Date	[27 October] 2016 (10 years after the Issue Date, subject to the Early Redemption Provisions (which include following a Strategy Unwind Event))
Note Type	Unsecured Floating Rate Notes
Expected Rating	The Notes are expected to be rated AAA by Standard & Poor's ("S&P") on the Issue Date as to the timely payment of their coupons and principal.
Currency of Issue	Australian Dollars (A$)
	[A$40,000,000.00]

Series Face Value	

…

Secondary Market Repurchase	The Dealer intends to make secondary markets in the Notes subject to normal market conditions. The price paid by the Dealer for any repurchase of Notes will be the price determined by the Dealer (the price determined by the Dealer will reflect supply and demand and therefore not necessarily be equal to the Net Transaction Value).

…

ABN AMRO make (sic) no representation and give (sic) no advice in respect of any tax, legal or accounting matters in any applicable jurisdiction. Each recipient represents, warrants and agrees that (i) they are considering this investment for their own account, (ii) they are a professional investor with sufficient knowledge, experience and professional advice to make their own evaluation of the merits and risks of making a complex investment of this type … (iv) they are fully aware that they may lose a significant amount or all of their investment, (v) they are responsible for making their own independent investigation and appraisal of the risks, benefits and suitability of any investments envisaged by this document, and (vi) ABN AMRO shall not incur any responsibility or liability whatsoever to any recipients in respect thereof.

The securities described in this termsheet may be assigned a credit rating by one or more rating agencies. A credit rating is not a recommendation to buy, sell or hold securities and may be revised or withdrawn by the relevant rating agency at any time. Each rating agency has its own methodology and modelling assumptions for rating transactions; ratings are sensitive to the methodology and modelling assumptions used and different methodologies, models and/or assumptions may, and in all likelihood will, produce different ratings. Any rating assigned to the securities represents the relevant rating agency's opinions regarding the credit quality of such securities; it is not a guarantee of quality or performance, nor is it an evaluation or indication of the likelihood or risks of fluctuations in market value. Any rating assigned to the securities may not fully reflect the true risks of an investment therein and may, in the event, be subject to qualifications. The risks, returns and performance of the securities described in this presentation may differ from those of an equivalently-rated corporate bond.

85. On 16 October 2006, LGFS confirmed that it was "happy to sign" the Mandate Letter: [SAF185] and J[1060]. ABN Amro replied by providing a signed copy of the Mandate Letter and by stating that once the letter was signed it (ABN Amro) could "execute the hedge" which would protect LGFS from further spread tightening: [SAF185] and J [1060]. On 18 October 2006, Mr Tischler confirmed by email to Mr Silvester (with a copy to Mr Hilder) that LGFS was happy for ABN Amro to execute the hedge: [SAF189] and J [1063].

86. In the present circumstances, ABN Amro knew that LGFS would only purchase the Rembrandt notes if they carried a rating of AAA: J[3199] and J[3272]. ABN Amro wanted the AAA rating: J[3089]. It made sure S&P was in no doubt as to its desire: J [3089]. ABN Amro would not accept anything less.

87. On 17 October 2006, Mr Silvester emailed a document to Mr Tischler which set out information regarding the credit spreads on a range of credit default swap indices, including the iTraxx and CDX indices: [SAF188] and J[1062]. Mr Silvester said that he would provide that information to Mr Tischler on a daily basis so that Mr Tischler could "monitor what the spreads [were] doing": [SAF188] and J[1062]. A subsequent email from Mr Silvester to Mr Tischler on 20 October 2006 stated that "[s]preads continue[d] to grind lower": [SAF192] and J[1066].

88. On 24 October 2006, Mr Silvester sent Mr Tischler an email about the price of Rembrandt 2006-2 and Mr Tischler sent an email to Mr Hilder conveying, among other things, his view that the price of Rembrandt 2006-3 should not be published until the "pricing [was] above 100": [SAF193] and J[1067]. Mr Tischler conveyed this view a short time later by email to Mr Silvester: [SAF193] and J[1068]. Mr Tischler also informed Mr Silvester that LGFS, as part of its white badging of the notes, had elected to rename Rembrandt 2006-3 as the "**Community Income CPDO Notes**" and requested a draft of the term sheet, updated to include this information: J[1069]. On that same day, Mr Lewis sent the draft term sheet to Mr Tischler (with a copy to Mr Silvester and Mr Levick) which incorporated the name change to "Community Income CPDO Notes" and the new issue and maturity dates: [SAF194] and J [1069].

89. On 25 October 2006, LGFS held a board meeting at which the proposed purchase of the Rembrandt 2006-3 notes (which were described as having a AAA rating) was discussed. Mr Hilder gave a presentation entitled "Community Income CPDO Notes" outlining the key features of the product. By this time, Mr Hilder said that he was "generally satisfied" with the additional information he had obtained about the Rembrandt notes, and that he would have decided not to proceed only if "something had arisen during [his] consideration of the product which caused [him] to believe it had any problems": J[1182]. But the information provided by ABN Amro to LGFS did not give Mr Hilder cause to reconsider. On the contrary, ABN Amro's marketing of the Rembrandt notes (including its emphasis on the robustness of the product's structure and its AAA rating), and its minimisation of any potential difficulty as set out in [91] below, indicated that all was well with the product. LGFS resolved to "approve the release" of the notes: [SAF195], J[1071] and J[1074].

90. The board papers for the board meeting of 25 October 2006 (at J[1071]-J[1072]) disclosed LGFS' concerns about the risk of its proposed purchase and on-sale to councils of the Rembrandt 2006-3 notes. Relevantly, the papers disclosed that a reason for a delay in the purchase of the notes was that credit spreads "had recently moved adversely from the point of view of launching the transaction in the near future". They also disclosed that the fact that LGFS would "have to purchase the issue [of the Rembrandt 2006-3 notes] from [ABN Amro] and progressively sell parcels to [councils]" would have a "number of ramifications for LGFS" including that "LGFS could end up holding inventory with no available purchaser". Part of the problem with such a scenario would be that while "the asset would be suitable for LGFS' balance sheet operations" it "would prevent new issues as there would be no room for holding long term assets". LGFS' ability to on-sell the Rembrandt notes to councils was thus of paramount importance to it. Indeed, one of LGFS' stated concerns was to ensure that "when [it acquired] the product for a price of $100" it was able to "present it to councils for $100 despite the reality that the market price for the product [would] be close to $98.80". LGFS noted that the "grotesquely complicated" nature of the product did "not help the selling process". Thus, rather than inform councils about its concerns and the fact that there was no secondary market for the notes, LGFS elected to focus on simplifying the information it provided to councils to "facilitate" its sale of the Rembrandt notes. LGFS' sales of the Rembrandt notes to the councils are addressed separately in Part 2 , Section 7 and Part 7 below.

91. On that same day, Mr Tischler received an email from Mr Silvester noting that S&P had "changed the vol [volatility] from 15% to 25% in their modelling assumptions" observing that this "has had just a minor effect on the table (2 differences highlighted in yellow)": [SAF196] and J[1075]. Mr Silvester also noted that "in general, small changes to fees or spreads don't affect the rating stability": [SAF196] and J[1075]. Mr Tischler had understood Mr Silvester's email to be stating that "the change to the volatility was unlikely to change the AAA rating": J [1183]. This was not true and, as the primary judge observed, LGFS had no "real idea of the events within S&P and ABN Amro relating to the volatility assumption" or any other aspect of how the CPDO was rated: J[1183]. Mr Silvester's advice was at its best a mistake and at its worst a lie. This issue is addressed in detail in Part 3 below.

92. On 31 October 2006, S&P issued the R-3 Ratings Letter (see [53] above) to Mr Lewis which stated that S&P had "assigned a public rating of 'AAA' to [Rembrandt 2006-3]": [SAF197] and J[318]. On 2 November 2006, Mr Lewis informed Mr Tischler by telephone that ABN Amro had received the R-3 Ratings Letter from S&P for Rembrandt 2006-3: [SAF200] and J [1184]. Mr Tischler requested that LGFS be sent a copy of the R-3 Ratings Letter, which Mr Lewis duly sent to Mr Tischler, who then forwarded the letter to Mr Hilder: [SAF200], J [1184] and J[1077]. Aside from expressing that Rembrandt 2006-3 had been assigned a AAA rating, the R-3 Ratings Letter also stated that (J[1077]):

- the rating did not constitute investment, financial or other advice and could not be relied upon as such;
- S&P undertook no independent verification of the information provided to it by ABN Amro;
- the rating did not constitute a recommendation to buy, hold or sell any obligations; and

• the ratings letter constituted S&P's "permission… to disseminate the above-assigned rating to interested parties".

93. In the days immediately preceding LGFS' receipt of the R-3 Ratings Letter (31 October and 1 November 2006), Mr Tischler and Mr Silvester exchanged emails about the value of the notes and settlement, including that the price of Rembrandt 2006-2 had dropped below par: [SAF198] and J[1076]. The Rembrandt 2006-3 notes, with a face value of $40 million, were issued to LGFS on 2 November 2006 and LGFS completed its purchase of those notes on the same day: [SAF201], J[325] and J[670].

94. On 16 November 2006, Mr Lewis sent Mr Tischler (with a copy to Mr Silvester) a copy of the Post-Sale Report for Rembrandt 2006-3 (see [49] and [55] above), which had been issued by S&P the previous day: [SAF204-205], J[357] and J[1091]. As with the Pre-Sale Report, ABN Amro had participated in the drafting of the Post-Sale Report, a fact that was unknown to LGFS: J[3089].

95. On 14 December 2006, Mr Tischler sent an email to Mr Silvester (with a copy to Mr Michell) which confirmed LGFS' desire to purchase an additional $5 million of Rembrandt 2006-3 provided that the price remained at par or less: [SAF211] and J[1105]. On 4 January 2007, Mr Lewis advised Mr Cian Chandler, the primary credit analyst at S&P for rating the CPDO, that ABN Amro had received an order to increase the issue of Rembrandt 2006-3 by $5 million and requested a letter from S&P confirming that the increase would not affect the rating of the existing notes as well as confirming the rating of the new notes: [SAF212] and J[362]. S&P issued that letter on 5 January 2007: [SAF213] and J[362].

96. On 9 January 2007, Mr Lewis sent an email to Mr Tischler and Mr Michell attaching the ABN Amro final term sheet for Rembrandt 2006-3 (which showed the volume of the notes as $45 million, an adjustment to include the additional issue of $5 million): [SAF214] and J[1112]. On the same day, the additional Rembrandt 2006-3 notes, with a face value of $5 million, were issued to LGFS: [SAF215] and J[1228]. Mr Hilder stated that the reason for the purchase was to have an additional amount on LGFS' books for its own use and as a "reserve for potential future sales" given the popularity of the notes amongst councils: J[1228]. Mr Hilder was not involved in the purchase of the additional notes but he understood Mr Tischler to be dealing with ABN Amro with respect to the proposed purchase: J[1228].

97. On 20 February 2007, Mr Silvester sent Mr Tischler a number of transaction documents which related to the Rembrandt 2006-3 transaction, including the Notice of Creation of Trust, the Master Trust Deed and the Supplemental Deed: [SAF216] and J[1114].

7. SALE OF NOTES TO THE COUNCILS

98. By 2003, structured financial products – particularly CDOs – had begun appearing in the local government investment market: J[990]. LGFS initially opposed investments by councils in CDOs, but by 2004 CDOs were making such substantial inroads into LGFS' traditional deposit-taking business that LGFS reconsidered its position: J[991]. In late 2004 and early 2005, LGFS began to investigate the possibilities of expanding its role as a provider of financial services to councils and expanding the range of investments options it offered to include structured financial products: J[991]. Market conditions were particularly trying for

deposit-taking institutions like LGFS and diversification to offer more "exotic" products was an attractive option: J[994].

99. LGFS set about investigating the viability of structured financial products. In December 2004, it prepared an internal report entitled "LGFS and CDOs". The report identified "issues for LGFS in purchasing or recommending CDOs", including (J[992]):

1. The questionable reliability of ratings – the report noted that "the correlation between names in a portfolio has a significant effect on the performance of tranches of a CDO" and that it was difficult to make accurate assumptions regarding default correlation;

2. The lack of a "well-established secondary market", which posed "a problem for liquidity and market valuations";

3. The impact of changing economic circumstances on movements in the price of CDOs, noting that at that time "credit spreads [were] historically low" and that "should economic conditions deteriorate the price of CDOs will decline"; and

4. That "in the absence of price movements arising from the maturing of the CDO market, the probability of price falls appears to be greater than the probability of price rises".

The report recommended that, if LGFS were "satisfied at a theoretical level that CDOs may be an appropriate investment", its next step would be to build knowledge of the issues. The report concluded that it was possible that "a single-tranche synthetic CDO" would prove to be the most appropriate form of investment for LGFS: J[993].

100. On 17 February 2005, LGFS held a board meeting. The papers for that meeting noted that "financial market conditions are probably at their worst ever for a deposit taking business such as LGFS". The papers also included "a broad overview of the draft strategic framework that [was] being explored to develop a detailed strategy for LGFS" and identified possible strategies which included adding an advisory operation and improving returns by, among other things, exploring LGFS' possible role as "a broker for specialised products (long term bonds, FRNs and CDOs) for councils". A table appended to the papers, next to the action "develop a strategy for possible use of CDO products", noted "several discussions with market players. Internal paper produced. Staff member to attend a CDO conference in February": J[994].

101. LGFS held a further board meeting on 6 July 2005, the papers for which included LGFS' 2005 /2006 Business Plan (**Business Plan**). Under the heading "2005/06 Operating Environment", the Business Plan recorded that LGFS' balance sheet had suffered an $80 million fall in deposits from a peak of just over $500 million to $420 million. Under that same heading, it was also noted that (as extracted at J[995]):

> Managed Cash Funds have not matched the earning rates on longer term Floating Rate Notes and leveraged Collateralised Deposit Obligations, and with the ready availability of those products, there has been a significant shift of council funds into the longer term

> floating rate securities … [T]here has been a similar shift away from traditional deposit products and in the absence of a crisis of confidence in such products it is likely that LGFS's Balance Sheet will continue to fall …

The Business Plan observed that a consequence of this environment was that "there [was] an opportunity to win business because councils have experienced difficulty in assessing the new products and traditional advisors to councils have been primarily focussed on funds management as the appropriate form of investment". To that end, the Business Plan opined that LGFS presented "a credible alternative approach".

102. Under the heading "Strategic Plan for 2005/2006", LGFS set out its intention to "[e]xplore product structures that could be used in a local government context that adds value or represents an alternative to CDOs for councils". It also identified that it would "*[l]everage off the rapport with the councils to encourage the resultant products as viable alternatives for them*" (emphasis added). This leveraging was important because, as the Business Plan noted, the councils were "very slow to change from existing practices".

103. The papers for the 6 July 2005 board meeting also included a research presentation entitled "Investigation of Local Government Investment Market" dated May 2005. The presentation had been created by Woolcott Research Pty Ltd at the commission of LGFS. The minutes of the board meeting disclosed that Mr David Elliot and Mr Matthew Toohey of Woolcott Research joined the meeting at 1:00 pm to present their findings. Relevantly, the presentation slides indicated that: (a) councils "tended to have a conservative approach in their investing philosophy"; (b) councils "were aware that they were investing public money, and thus had an obligation not to invest in anything too high risk"; (c) financial controllers at councils had "an accountancy background", and investment was "not their area of expertise"; (d) CDOs "were seen as a riskier investment" – nobody at the councils "felt they 'really' knew how a CDO works" and councils tended to "rely on [adviser's] for making investment decisions"; (e) the majority of councils were using an advisory service as they felt they did not have "the expertise or time to make the best investment choices": and (f) while councils retained "the final right on all investment decisions", it was "rare for them not to take the [adviser's] recommendations": J[998].

104. In September 2005, Mr Michell visited a number of the Councils, including Eurobodalla, Cooma, Corowa, Narrandera, Murray and Oberon, recording their appetite for CDOs and his perception of their approach to investments, particularly CDOs: [SAF254] and J[1006]. Mr Michell's notes record that appetite for CDOs was mixed but that most of the Councils were happy with LGFS' services: [SAF254] and J[1006]. His notes included the following:

> **Eurobodalla**
> John Murphy & Miles Craighead
> 20% CDO's
> Current policy restricts amount invested in A1 category (inc LGFS) both individually and combined. Will be expanding this category in policy. Restrictions inhibiting returns – forcing them to A1+ level.
> Miles interested in ECF – Mark to phone to discuss structure of FM.
> …
> **Cooma Monaro**
> Darryl Hagger & Kate

Very happy LGFS. Very conservative. LGFS + two others. No CDO's. No FRN's.
…
Corowa
Ian Rich
CDO's through Grange – not happy with portfolio manager. Looking to sell portfolio.
Send letter of offer on "Right Balance" – very keen.
Total about $15-18 mill.
Send info on training.
…
Narrandera
Robert Brown
Very happy with LGFS. Send info on training.
LGFS plus two others (local bank and other)
Very conservative. No CDO's
…
Murray
Nathan Quinlan
Very conservative. Grange want to portfolio manage their funds.
Not comfortable with CDO's – don't understand them.
Send letter of offer "right balance".
Send details on training.
…
Oberon
Amanda McGrath
Send letter of offer "right balance"
Reviewing investment policy in November after auditors
Buying first CDO $500k – could be "beech" – **"just dipping their toes" opportunity** f or monitoring
Send info on training

(Emphasis added.)

105. Mr Michell would make further marketing trips throughout LGFS' course of marketing the Rembrandt notes. After one of these trips, he noted in an email to Mr Tischler that "the positive image of LGFS is certainly something that comes out as providing a level of comfort for people and this acts to allay any concerns that (sic) about the ten year term or the fact that it is a new product": J[1094] and J[1377(6)]. Mr Michell's reference to "ten year term" was to the term of the Rembrandt notes, a term which he had identified was an "eyebrow raiser" for the councils: J[1094] and J[1377(6)].

106. In October 2005, Mr Hilder presented an Activity Report to the Board of LGFS prepared in the previous month. The report stated that:

> *Most if not all council holders of CDO's (sic) do not understand these products; Councils do not have the resources to monitor CDO's (sic) in an appropriate fashion*; The high credit ratings on CDO's (sic) do not truly represent the inherent risks; CDO's (sic) are constantly evolving, there is no standard structure, complexity is increasing; Should credit markets suffer a significant blow-out, there will be losses.

(Emphasis added.)

107. A further board meeting was held on 12 October 2005. The minutes of that meeting recorded that FuturePlus' CEO expressed concern that "funds under management continued to fall and that CDO's (sic) continue to have a detrimental impact on market share" and that the company (being, presumably, LGFS) "would struggle to become profitable under its current business model, given the low margins available": J[1007].

108. Between June 2005 and November 2005, LGFS' term deposits suffered a reduction of around $95 million. By November 2005 over sixty councils in New South Wales had engaged external fund managers in respect of their portfolios: [SAF139].

109. In late 2005, LGFS developed a new service it intended to provide to councils, entitled 'Right Balance' (**Right Balance Service**): J[1153]. This new service was part of LGFS' plan to strategically position itself as an investment adviser to councils as opposed to its historical role as a deposit-taking institution: J[1153]. LGFS marketed the Right Balance Service to councils through a brochure (**Right Balance Brochure**), which included the following statements (emphasis in original) (J[982]):

> Local Government Financial Services Pty Limited (LGFS) and FuturePlus Financial Services Pty Limited (FuturePlus) have joined forces to provide the foundation for a unique financial advisory service developed exclusively to assist Local Government Councils.
>
> **How can we help you?**
> Combining forces with FuturePlus places an extensive range of financial market and advisory capacities at LGFS's disposal. This means that LGFS can provide you with:
>
> - **Financial expertise** – from highly experienced market specialists.
> - **Market intelligence** – using our extensive in-house and external research capacities.
> - **Effective investment decision making** – backed by an experienced team with highly successful processes for managing active portfolios in financial markets.
> - **Major buying power** – combined with FuturePlus, having $7.5 billion in funds under management, LGFS can demand particularly competitive prices from the market.
>
> With these capabilities and resources behind us, LGFS is extremely well equipped to provide Councils with a competitive edge to maximise returns on their funds.
>
> What benefits can we bring you?
> Having LGFS on your side means you will benefit from:
>
> - An effective strategy developed by experts.
> - Current market intelligence provided by experienced professionals with impressive track records.
> - Sound product analysis drawn from successful in-house portfolio managers.
> - Sharp prices garnered from the group's buying power in financial markets.
>
> Supporting this is the superior client service offered by LGFS and FuturePlus. The core business of both LGFS and FuturePlus is to provide the best possible financial solutions

and services to Councils, whether focused on investment needs or the superannuation needs of staff.

A partnership within Local Government

The Local Government Superannuation Scheme, together with its service provider, FuturePlus, has delivered very good financial outcomes for Councils for 8 years. Further, LGFS has a 30 year track record of successfully providing a range of financial services for Councils.

By partnering with LGFS, Councils can harness the extensive skills, experience and resources of both LGFS and FuturePlus to achieve better financial outcomes for Councils' own funds.

The "Right Balance"

At LGFS we believe that successful investment management is about getting the "Right Balance".

We have the skills and experience to help you achieve the difficult task of getting a balance of risk and return, a balance of credit and concentration, a balance of funds management and direct investments, a balance of fixed and floating rate exposures and a balance of exposure to various possible outcomes.

The Right Balance can only be achieved through a disciplined and logical process, such as the one developed by LGFS specifically for Local Government Council clients. Based on key principles, this process develops a framework for setting a broad strategy to maximise a Council's investment returns and then for measuring the success of that strategy.

The process is all about getting the "Right Balance". Its key components are described over.

The "Right Balance" principles

The key principles of the LGFS Right Balance process are to:

- match the strategy to the nature of Councils' funds
- relate the Balance principles to the purpose for which Councils' funds are held
- assess and define Councils' risk tolerance and balance the strategy with this risk preference
- develop and articulate a preferred economic scenario that is directly related to financial market movements
- identify the main risks to this preferred scenario and assess the impact of a contrary outcome
- analyse the various market segments to identify "value"
- work within Councils' preferred market segments (direct investments, funds management or a combination of both)

- monitor economic and investment market developments in the context of Councils' strategy and within the assumptions that the strategy is built upon. (This is done in consultation with Councils to ensure the strategy remains relevant.)

LGFS also provides tactical advice on the products that can be used to implement each Council's strategy.

> From time to time assets can trade at a price which is well above an appropriate price for the nature of the product and its attendant risks. LGFS will monitor these prices with a view to adding value to Councils by identifying "cheap" assets that fit with their strategies.
> LGFS can also provide Councils with formal reporting on a regular basis which details the performance of the portfolio and enables a review the strategy.
>
> LGFS will monitor these prices with a view to adding value to Councils by identifying "cheap" assets that fit with their strategies.

110. The Right Balance Brochure indicated that Messrs Hilder, Tischler and Michell had been appointed as the councils' primary contacts to "ensure effective delivery of advisory services and the timely flow of information to [c]ouncils": J[983]. It also specified the following information in respect of regulatory requirements (J[984]):

> - LGFS is an Australian Financial Services Licensee (AFSL 245642).
> - FuturePlus is an Australian Financial Services Licensee (AFSL 238445).
> - LGFS holds a credit rating of "A,A1" by Standard & Poor's Ratings Agency.
> - LGFS is an authorised investment under Local Government Act 1993 – Investment Order dated 16th November 2000 section (n).
> - Local Government Financial Services Pty Limited (LGFS) is wholly owned by the Local Government Superannuation Scheme (LGSS).
>
> - FuturePlus Financial Services Limited (FuturePlus) is owned by the Local Government Superannuation Scheme and the Energy Industries Superannuation Scheme.

111. LGFS had also prepared a standard-form letter which it sent to the councils with the Right Balance Brochure. That letter (the **Right Balance letter**) said (J[985]):

> Investment markets have become extremely complicated with Brokers pushing increasingly complex and involved products that require extensive evaluation and legal due diligence. It has never been more difficult to manage financial assets.
>
> In response to this, LGFS has joined forces with the Local Government Superannuation Scheme to develop the "Right Balance", a service to help councils extract the best returns from financial markets for the risks taken.
>
> In using the "Right Balance" service council will not only benefit from the research and market resources of LGFS but will also benefit from the extensive resources and capacities of the staff managing the Local Government Superannuation Scheme. With an organisation of over $8 billion behind you, the complexities of the market can readily be mastered and the finest prices can be extracted.
>
> The "Right Balance" service is a structured and logical strategic process for councils, to assist in managing and monitoring investment portfolios and to provide input into investment choices away from a sales context.
>
> The process is structured to capture all the relevant elements important to council. The objective is to achieve the "Right Balance" between risk and return, credit

concentration, funds management and direct investment exposures for council. A detailed explanation is set out in the attached brochure.

We would like to invite you to consider engaging LGFS to provide the "Right Balance" service for your council. …

112. LGFS also prepared an agreement which it was intended would be executed as between LGFS and those councils that wished to subscribe for the Right Balance Service (**Right Balance Agreement**). The Right Balance Agreement contained the following two recitals (J[986]):

A LGFS has represented to the Council that it has the skill, facilities, capacity and staff to carry out the terms of this Agreement.

B The Council wishes to appoint LGFS to provide Services in respect of its Portfolio and LGFS has agreed to accept that appointment on the terms and conditions set out in this Agreement.

113. The Right Balance Agreement also contained the following provisions (J[987]):

2.1 Appointment
The Council appoints LGFS to provide the Services in respect of the Portfolio on the terms and conditions of this Agreement.

2.2 Acceptance
In consideration of the Service Fees, LGFS accepts its appointment as service provider on the terms and conditions of this Agreement.
…

3.1 Performance
LGFS shall provide the Services diligently, accurately and efficiently and to meet the Performance Criteria set out in Schedule 1. If the Agreement, including Schedule 1, does not expressly specify the date by which a particular Service must be provided at the latest, the Service is required to be performed by a date which will reasonably enable the Council to comply with any Relevant Law.
…

3.3 Capacity

LGFS must maintain access to sufficient Resources to ensure the provision of Services and Additional Services.
…

3.8 Accuracy
LGFS is at all times responsible for ensuring that the information delivered (such as monthly performance reports) and the processes undertaken by virtue of the Services provided are accurate and complete. This means that the information supplied has been processed correctly in accordance with Council's Investment Policy and Relevant Law.
…

4.7 Commitment as to Resources

LGFS must have, or have access to, all the Resources necessary to provide the Services in accordance with this Agreement. LGFS represents that it:

(a) will not seek to recover fees for the provision of the Services on an hourly rate basis; and

(b) will maintain adequate and appropriate staff levels to provide the Services in accordance with the Performance Criteria.

…

5.1 Liability of and Indemnity by LGFS

LGFS is liable to the Council for each claim, action, proceeding, judgment, damage, loss, expense or liability incurred or suffered by or brought or made or recovered against the Council **(Council Loss)** to the extent that it arises as a result of or in connection with any breach of this Agreement by, or negligent act or omission of, or fraud or dishonesty on the part of, LGFS (or any of its officers, employees or agents) but not if the breach, act or omission is based on the direction of or information provided by the Council. LGFS agrees to indemnify the Council for all direct Council Losses but not for any indirect, economic, consequential or special Council Losses.

5.2 Liability and Indemnity by Council

The Council is liable to LGFS for each claim, action, proceeding, judgment, damage, loss, expense or liability incurred or suffered by or brought or made or recovered against LGFS **(LGFS Loss)** to the extent that it arises as a result of or in connection with any Proper Instruction, or any breach of this Agreement by, or negligent act or omission of, or fraud or dishonesty on the part of, the Council (or any of its officers, employees or agents (other than LGFS)). The Council agrees to indemnify LGFS for all direct LGFS Losses but not for any indirect, economic, consequential or special LGFS Losses.

…

6.1 Compliance generally

LGFS will, at all times, comply with the:

(a) the Relevant Law;

(b) the provisions of this Agreement; and

(c) any compliance procedures established by the Council in respect of the Portfolio, and advised to LGFS from time to time.

…

9.1 LGFS' representations and warranties

LGFS represents and warrants to the Council, as at the date of this Agreement and for the Term and it is a condition of this Agreement, that:

(a) it has and will maintain within Australia the power, skill, capacity and resources necessary to perform its obligations under this Agreement;

(b) it will exercise all due diligence and vigilance in carrying out its obligations under this Agreement;

(c) it will ensure that sufficient competent employees will at all times have the conduct of, and will maintain close supervision of, the Services and any Additional Services and any Additional Services to be provided under this Agreement;

…

(e) it holds all licences, permits, authorisations, approvals and consents necessary to perform its obligations under this Agreement and will comply with all applicable laws in the performance of its obligations under this Agreement;

…

114. Schedule 1 to the Right Balance Agreement identified the "Service" in these terms (J[988]):

> This Service Delivery Schedule (SDS) sets out the agreed service commitment between the Council and LGFS. The SDS forms part of Schedule 1 of the Services Agreement between the parties.
>
> The purpose of the SDS is to:
>
> - Clearly outline the Services to be provided to the Council by LGFS under the Agreement;
> - Establish the responsibilities of each party in delivering these services; and
> - Formulate a system to measure the accuracy, completeness and timeliness of LGFS as a service provider.

Phase	Service	Performance Criteria
Initial Action	• Develop reference investment that reflects the underlying purpose of funds • Assessment of current portfolio • Review Council's Investment Policy • Cash flow analysis	Within 30 days after signing of agreement
Strategy	• Assess strategic orientation of portfolio • Establish trigger points that would initiate a re-consideration of strategy • Evaluation of the implications of alternative scenarios • Agree process for regular portfolio review and reporting	Within 30 days after signing of agreement
Strategy Execution	• Assess the short term influences that could	Within 5 business days of authorisation

	impact on the tactical timing of investments • Assessment of assets within the risk parameters specific to council's investment policy • Review approach to complex structured products	
Reporting	Monthly reporting • Economic and Market report • Portfolio performance report • Compliance report	Within 7 business days of end of month
	Quarterly reporting • Review against implement Strategy • Review of investment strategy	Within 7 business days of end of quarter (being three month anniversary of signing of agreement)
	Annual reporting • Annual assessment of investment strategy • Presentation of annual results to Council	Within 30 days of one year anniversary of signing of agreement

115. The Right Balance Agreement defined the Relevant Law as the *Local Government Act* , the *Corporations Act* , the *Income Tax Assessment Act 1997* (Cth), regulations and regulatory policy made under those Acts, and other Australian laws applicable to the councils as notified to them by LGFS: J[989].

116. The Right Balance Service was not successful and only had a marginal effect on LGFS' continuing loss of market share: J[1035]. Of the Councils to whom LGFS marketed the service, only Corowa and Cooma subscribed for the service and entered into the Right Balance Agreement with LGFS (the **RB Councils**): [SAF19], [SAF21] and J [1153]. The other councils will be referred to as the **NRB Councils**.

117. On 30 November 2005, Mr Hilder sent an email to Mr Peter Lambert, who was the CEO of LGSS and the CEO and Company Secretary of LGFS since 5 December 2007, attaching board papers including an "Activity Report December 2005 Quarter" which observed that:

> [T]he strongest demand [for the Right Balance Service] is from councils that have portfolios of CDO's (sic) that are being approached by brokers wishing to trade them. These councils are unsure as to the brokers' motivation and do not have the tools or knowledge to evaluate the proposed trades. *These councils have expressed a need for expert independent assistance and see LGFS as a natural fit to fill this roll (sic).*

(Emphasis added.)

118. LGFS held further board meetings on 7 December 2005 and 22 February 2006. The papers for the 7 December 2005 meeting included reports about the marketing of the Right Balance Service and the impact of CDOs on LGFS' balance sheet. Mr Hilder presented the "Business Situation Review" which proposed a number of alternatives to "address the balance sheet reduction" including developing a new deposit product, using managed fund investments as assets against short-term council deposits, and maximising opportunities associated with the Right Balance Service: [SAF140]. The minutes of the meeting on 22 February 2006 record that in response to the confirmation of the minutes of the meeting held on 7 December 2005, FuturePlus' CEO "outlined that the underlying profitability of the business would continue to be difficult given that the providers of products utilising CDOs were eroding market share of those products with higher margins": [SAF141].

119. It was also in late 2005 that Mr Tischler had commenced purchasing CDOs for LGFS' own books in a tentative step into the market: J[1163]. Nonetheless, LGFS had not found a suitable alternative product and its market share continued to decline: J[1292]. LGFS' interest, by this time, was to establish itself as a player in the financial products market in order to overcome the "substantially deleterious effect that the sale of CDOs" by its competitors had had on LGFS' profitability: J[2311]. The CPDO provided LGFS with an opportunity.

120. On 6 March 2006, Mr Cordeiro published a paper entitled "Implications for structured credit for Local Government Authorities" which was discovered by LGFS, stating:

> CDO's (sic) as an investment are probably a reasonably conservative investment for a local government investor when used in the right way, with sufficient understanding of the limitations and possible extreme (but unlikely scenarios) that can occur with this product type…*It is clear from feedback from many of these investors are (sic) not fully briefed on limitations of the product and it would probably be fair to say that many investors in these products should not be invested (sic) in the way that they are*.
>
> (Emphasis added.)

121. On the same day, Mr Tischler met with representatives of ABN Amro, including Mr Cordeiro. Mr Tischler's notes of that meeting recorded that "[s]ome CDOs held by councils may not be suitable for inclusion because of excessive risk or unusual structural elements". His notes also recorded the following (J[1011]-J[1012]):

> Meeting with ABN-Amro 6th March 2006
>
> Summary
>
> Meeting arranged to discuss ways ABN-AMRO could assist in the repackaging (sic) a disparate assortment of Council held CDOs into a securitised structure to produce a superior security(s) for resale to councils.
>
> - Recognition of potential "time bomb" investors in CDOs may face if market moves against them.
> - Significant portion of product (sic) in the market poorly structured and vulnerable

- Combining large volume of separate CDO issues held by councils into a common pool and securitising that pool to produce a superior AA rated security for resale …
- […]
- Purchase issues back from council at par, so no loss from initial purchase on issue and reissue new AA rated securitisation product at around 100 bps over bill. This may mean capital losses and gains against mark to mark values – which could present weakness to those running a counter campaign
- […]

- Some CDOs held by councils may not be suitable for inclusion because of excessive risk or unusual structural elements

122. On 5 April 2006, Mr Cordeiro emailed Mr Hilder regarding developing "[f]urther options for NSW Councils" stating:

> *Elliott [Levick] has asked me to think further about the options that may suit the requirements of NSW councils for high quality investments.*
>
> *I am conscious of the difficulty to organise each individual council as they are independently managed, however, I am also conscious of the limited level of knowledge of complex financial products such as CDOs and similar products. I have been trying to identify a strategy which would be achievable and sensible for yourselves and the NSW councils in general.*
>
> Firstly, you would we (sic) aware that CDOs themselves aren't bad products, really, it's the contrary, they are good products. The problem with many of the transactions sold to NSW councils is [that] the distribution fees that are deducted from the value of the transactions forces the originators to create structures which are less robust than can otherwise be achieved. Furthermore, there is no independent specialist reviewing the transactions making it difficult for the council to truly understand the level of risk associated with the investment.
>
> *I would like to propose a discussion with that (sic) would involve ABN AMRO working with LGFS to create a high quality CDO investment which would meet the objectives of NSW councils (i.e. return above BBSW) plus a high degree of security and rating stability of the structure.* There are a number of possible options for LGFS but some of the roles could include:
>
> - Distribution agent
> - Portfolio manager
> - Structural adviser
> - Asset consultant
>
> In addition to the roles above, subject to a sufficiently acceptable volume, we could arrange for a third party, experienced, specialist portfolio manager to manage the transaction on the investors and your behalf.

What we would be trying to achieve is a transaction that pays a satisfactory margin over BBSW, but has a credit quality that would be satisfactory to the asset consultant. We could engage the services of an independent agency to assess the credit worthiness of the structure.

Please think about this line of discussion and feel free to call or email me back with your thoughts.

(Emphasis added.)

123. The circumstances in which LGFS purchased the Rembrandt 2006-2 and Rembrandt 2006-3 notes from ABN Amro are set out at [59]- [97] above.

124. At around the time that LGFS was considering investing in the Rembrandt notes, it was also in the process of a setting up its Fixed Out-Performance Cash Fund. That fund was to operate as a managed investment scheme and LGFS required an amendment to its AFSL to operate the fund; an amendment it was in the process of obtaining: [SAF464] and J[3594]. At trial, LGFS submitted that the Rembrandt notes were a "sideshow" to its real interest in marketing its Fixed Out-Performance Cash Fund. The primary judge rejected this submission on, among other things, the basis that it was "defeated by [LGFS'] own documents": J[2166].

125. LGFS began the process of marketing Rembrandt 2006-3 to councils soon after its purchase of the notes. In early November 2006, LGFS prepared a brochure entitled "LGFS Community Income Notes Brochure" to be provided to some of the councils (**LGFS Community Income Notes Brochure**): J[48]. It included the following information on the first page (as set out by the primary judge at J[49]):

Community Income CPDO Notes

Arranged by Local Government Financial Services Pty Ltd

The Offer:

AAA Rating	CPDO is a new form of synthetic credit investment that carried a AAA rating on both the principal and the interest.
High Return	Community Income CPDO Notes have a AAA rated quarterly coupon rate of BBSW + 190 bps pa.
Diversification	This new form of synthetic credit investment offers diversification as an alternative to existing forms of structured investments such as CDOs and CPPIs.
Liquidity	LGFS will provide liquidity by repurchasing notes at market value.

Key Features:

Credit indices:	The credit portfolio is comprised of credit swaps against international credit indices. The credit indices are rolled over

represent an implicit “self cleansing” feature.	every six months into a new set of indices providing a “self-cleansing” effect, i.e. entities downgraded to below investment grade are removed and replaced by investment grade entities.
Credit indices: spread widening can potentially be beneficial.	A widening in credit spreads, with no corresponding defaults, may be beneficial to the structure increasing the value of the leveraging.
Controlled leverage.	The Community Income CPDO Notes aim to pay stated coupons by taking leveraged exposure that is governed by a fixed set of rules.
Potential early de-leveraging /cash-in.	If the Note value rises above the value of a AAA bond paying BBSW + 190 bps pa plus administration expenses, a “cash-in” event will be triggered and the credit index portfolio will be fully unwound. Investors continue to receive coupon payments for the remainder of the term without any further exposure to leveraged credit risk or can sell the CPDO, potentially for a profit.
LGFS support.	LGFS will continue to provide support to investors including next day liquidity and daily pricing as required throughout the term of the investment.

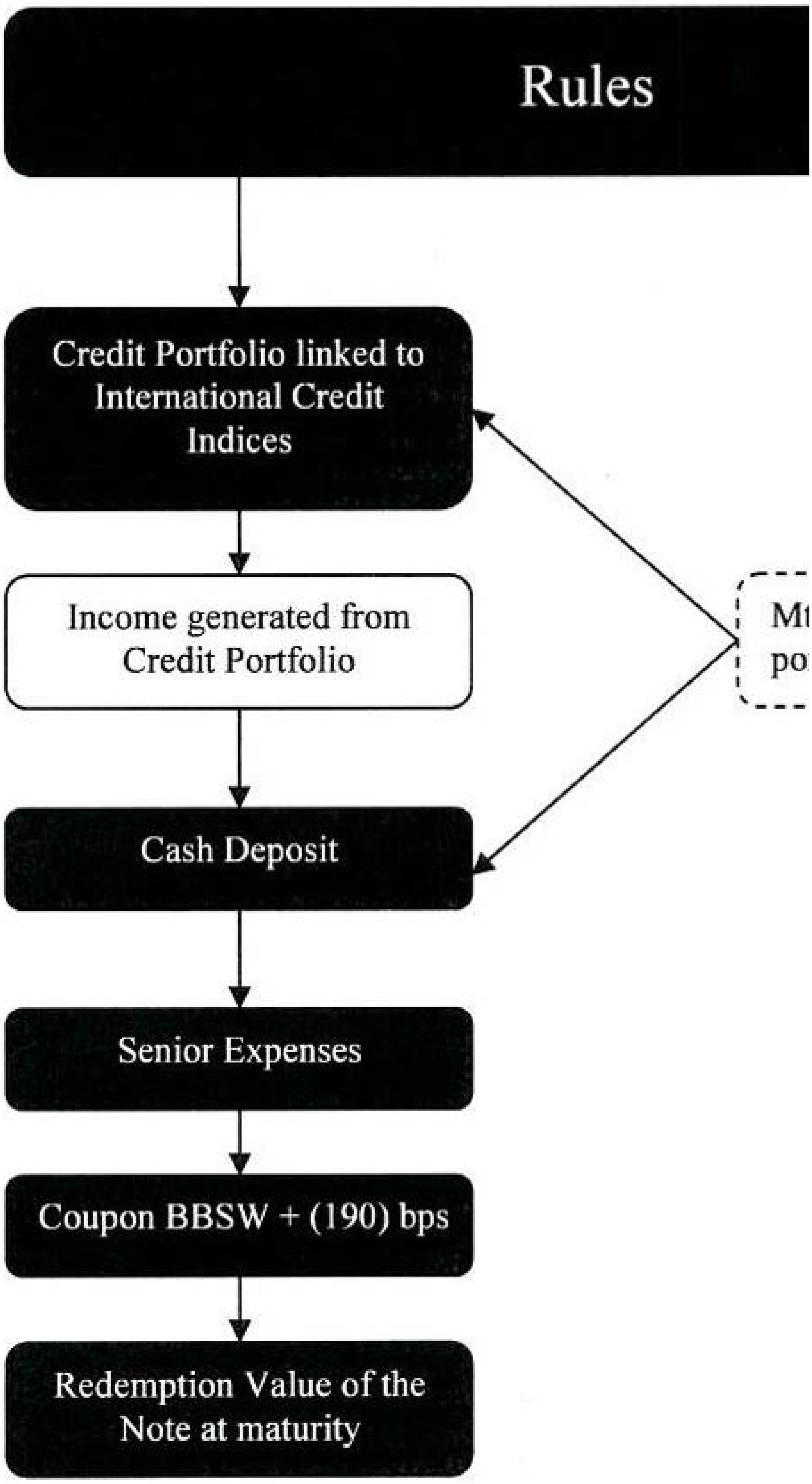
126. At the bottom of the first page appeared the following statement:

> This document and the Term Sheet are for wholesale investors only. Retail investors cannot hold the Notes. This material is for information purposes only and should not be distributed to any person or entity in any jurisdiction or country where such distribution would be contrary to local law or regulation. This document is not an offer, nor invitation to offer, nor a solicitation or advice or recommendation to buy, subscribe for, issue or sell securities. No representation, warranty or assurance of any kind, express or implied, is made as to the accuracy or completeness of the information in this document or the Term Sheet. This document is not intended to set out the final terms and conditions of the Notes and it may be amended, superseded or replaced in its entirety by the Term Sheet or other summaries of the terms and conditions. The final terms and conditions are set out in the Issue Notice. Investments such as the Notes involve a degree of leverage risk, and the value of such instruments may be highly volatile. Such risks may include the loss of a significant amount or all of your investment. This brief statement does not disclose all of the risks and other significant aspects in connection with the Notes and, before purchasing the Notes, you should ensure that you fully understand the terms of the Notes, including relevant risk factors and any legal, tax and accounting considerations applicable to the Notes. Neither Local

Government Financial Services Pty Ltd nor any of its officers or employees accepts any liability whatsoever for any loss arising from the use of this document or the Term Sheet.   This material may not be reproduced, distributed or transmitted to any other person without the prior written consent of Local Government Financial Services Pty Ltd. Please note that the information contained herein is of a general nature only. It is has not been prepared taking into account your particular investment objectives, financial situation and particular needs. This document is provided by Local Government Financial Services Pty Ltd (ABN 12 001 681 741), an Australian Financial Services Licensee (AFSL No 245642). Local Government Financial Services is owned by Local Government Superannuation Scheme (ABN 68 078 003 497).

127. The second page of the brochure contained the following diagram:

Community Income CPDO Notes



128. Mr Hilder intended the brochure to be a "plain-English explanation of the features of the Rembrandt notes" although he accepted that while it identified the advantages of the product, it did not identify any disadvantages or risks: J[1202] and J[1337]. Mr Hilder agreed that the brochure did not acknowledge that spread widening could be potentially detrimental to the

structure of the CPDO, or that leveraging could increase the magnitude of the loss: J [1202]. Mr Hilder had made a decision "only to show the key features which were positive, not those that presented risks": J[1204]. For instance, while the brochure emphasised the liquidity of Rembrandt 2006-3 in the body of its text, it only discussed volatility in the fine print contained at the bottom of the first page. Mr Hilder said that he nonetheless approved the brochure on the basis that it was a mere "agenda for discussing the product" to "entice interest" and facilitate the sale of the product by outlining the "rewards or benefits or returns of the product": J[1337]. Mr Tischler's evidence was to the contrary; he considered the brochure to be the "marketing script" for the product: J[1338].

129. LGFS' decision to highlight the liquidity of the Rembrandt 2006-3 notes while minimising their volatility was deliberate. LGFS was aware that the Rembrandt 2006-3 notes were highly volatile. The Surf Presentation (set out at [61]- [69] above) disclosed as much on page 29 under the heading "price volatility". The presentation stated that: the "NAV of the note is sensitive to credit spreads of the underlying portfolio of index swaps"; the "price of the notes may be lower than the initial purchase price"; the "traded price may be different from the NAV of the notes due to supply and demand issues; and "[l]everage may increase the magnitude of price volatility". ABN Amro had mentioned price volatility as an issue at the oral presentation attended by Mr Hilder. At trial, Mr Hilder gave evidence that he understood that "the design of the Rembrandt notes meant that the price was liable to fluctuations which depended on the value of the indices": J[1357]. Yet, despite the Surf Presentation disclosing that the "price of the notes may be lower than the initial purchase price" and both Mr Hilder and Mr Tischler being aware that the Rembrandt 2006-2 notes had experienced a decline in market value to less than the issue price (see [87]-[93] above), LGFS did not inform the Councils that the market value of the notes may not be their face value. Rather, as the next paragraph sets out, LGFS chose to focus on the liquidity of the Rembrandt 2006-3 notes in its marketing.

130. Presumably to avoid the issue of volatility hindering its ability to on-sell the notes, LGFS emphasised the liquidity of the notes. The brochure stated that LGFS would "provide liquidity by repurchasing notes at market value" and that LGFS would "continue to provide support to investors including next day liquidity and daily pricing as required throughout the term of the investment": see [125] above. The liquidity of the notes was also important in ameliorating the ten year term of the Rembrandt notes which Mr Michell had identified as an "eyebrow raiser": see [105] above. Indeed, Mr Michell's email to Mr Tischler in which this issue was raised stated that the "eyebrow raiser" became "largely irrelevant when they [saw] the written commitment from LGFS to buy back at 24 hours (sic) notice": J [1094]. But, despite knowing that the Councils were relying on the liquidity of the notes to mitigate against the length of their term, LGFS did not inform the Councils that the market value at which LGFS promised to repurchase the notes from the Councils would be whatever price ABN Amro determined having regard to supply and demand at the time: J[1363]. In the event, liquidity was an important factor in the Councils' decision to purchase the Rembrandt 2006-3 notes. The primary judge found that there was evidence to establish, or to support an inference, that the promised liquidity of the Rembrandt 2006-3 notes was a factor which the Councils (except for Ryde) relied on in deciding to invest in the notes: see J[1552] (Parkes), J[1641] (Orange), J[1730] (Oberon), J[1955] (Murray), J[2012] Cooma and J[2050] (Narromine).

131. In addition to the brochure, LGFS marketed the notes by providing a copy of either the Pre-Sale Report or the Post-Sale Report to some of the Councils, by sending a letter entitled "CPDO – The Next Generation" to two Councils (Narromine and Ryde) (**the CPDO letter**), and by holding discussions with various representatives of the Councils: [SAF260] and J [1306]. The primary judge found that the discussions LGFS held with representatives of the Councils conveyed the impression that the CPDO, marketed as "Community Income CPDO Notes", were specifically tailored or designed for local councils: J[1370]. This impression was also conveyed by the terms of the CPDO letter sent to Narromine and Ryde, which was set out by the primary judge (at J[1125]) and which stated as follows (the version sent to Ryde contained a difference in the opening paragraph which is not material):

> **AAA Rated Principal & Coupon**
>
> AAA Rated Principal & Coupon
>
> CPDO – The next generation.
>
> As you discussed recently with Simon Michell, LGFS has introduced Constant Proportion Debt Obligation (CPDO) technology. This is a new AAA rated structure type which pays a AAA rated coupon of 190 basis points above the 90 day BBSW rate.
>
> This new form of synthetic credit investment offers very high liquidity and represents a diversification alternative to existing forms of structured investments such as CDO's and CPPI's, some of which have struggled to maintain their credit rating and projected coupons.
>
> The CPDO is a rules based structure that uses two investment grade credit indices (DJ CDX.IG and (iTraxx) rather than a static portfolio of credit default spreads to earn coupon. The indices roll every six months into a new series and entities downgraded to below investment grade are removed and replaced by investment grade entities, this serves to limit the credit risk in the transaction.
>
> When compared with a static portfolio comprising identical underlying reference entities, rolling the indices acts as a defensive mechanism that limits negative credit migration and default risk. – Standard & Poor's Ratings Agency
>
> Once the notes earn enough to pay the BBSW +190 bps coupon and expenses for the remainder of the term an early cash-in occurs and the credit index portfolio will be fully unwound. Investors continue to receive coupon payments for the remainder of the term without any further exposure to leveraged credit risk. In addition the option exists to sell the CPDO, potentially for a profit.
>
> Spread widening, attended by no corresponding defaults, is beneficial to the structure. – Standard & Poor's Ratings Agency
>
> Since issuance in November 2006, the notes have paid an initial coupon of 8.22% to the 20/12/06. Then 8.31% to the 20/3/07. The current coupon rate is 8.36% with the next roll (sic) 20/6/07. The rating has remained at AAA since issuance.

LGFS is proud to be the first to tailor this robust structure to Local Government which we believe provides Councils with the opportunity to improve the liquidity, credit quality and performance profile of longer dated portfolios.

We have a limited amount of notes remaining and we would be happy to discuss the characteristics of this offering in more detail with you.

(Emphasis added.)

132. Further, seven of the Councils were provided with either a draft or final version of the ABN Amro term sheet for the Rembrandt notes (Bathurst, Moree, Deniliquin, Murray, Narrandera, Oberon and Orange): [SAF260] and J[1307].

133. Mr Tischler and Mr Michell discussed ways of selling the product to council representatives: J [1205]. They agreed to (J[1205]):

- focus on the product's AAA rating, as this meant Rembrandt fell "clearly" within the terms of the Ministerial [O]rder;
- provide [C]ouncils with the [Pre-Sale Report or Post-Sale Report] and the ABN Amro draft term sheet, as well as the LGFS [C] ommunity [I]ncome [N]otes [B]rochure; and
- strongly encourage council representatives to read those documents for themselves.

134. The marketing documents used by LGFS (i.e., the LGFS Community Income Notes Brochure and the CPDO letter) emphasised the following features of the product (J[1308]):

(a) the AAA rating assigned to the Rembrandt notes by S&P;
(b) the high return and liquidity of the Rembrandt notes;
(c) LGFS's "support" for the product (also reinforced by the renaming of the product as "community income notes"), plainly intended by LGFS to communicate a connection with the functions of councils;
(d) the likelihood of a "cash-in" event occurring through which the credit index portfolio would be unwound and investors would continue to receive coupon payments for the remainder of the term of the investment, without any further exposure to leveraged credit risk, and

(e) that the Rembrandt notes offered diversification as an alternative to existing structured credit investments such as CDOs.

135. On 16 November 2006, Grove Research and Advisory prepared a report about the Rembrandt 2006-3 notes (the **Grove Report**). A council (not involved in these proceedings) emailed the report to Mr Tischler on 30 November 2006 and Mr Hilder saw the report soon thereafter: [SAF209]. Relevant aspects of the report were set out by the primary judge at J [53]:

Features

Issuer	Rembrandt Australia Trust Series 2006-3
Books Close / Settlement	[November 17] 2006
Distributor	Local Government Financial Services (LGFS)
Arranger / Swap Counterparty	ABN Amro
Calculation Agent / Index Dealer	ABN Amro
Term	10 years
Rating	AAA (Standard & Poor's)
Structure	Credit-linked capital-protected notes
***Releverage* Triggers**	75% / 125% of target
Quarterly Contingent Coupons	BBSW + 1.9% p.a.
Leverage Limit	15x
Liquidity	ABN Amro intend to make a market (1% bid offer spread currently indicated)
Currency	$A
Early Redemption Trigger	Cash-out (deleverage) event: NAV below 10c in the dollar
Underlying Assets	Investment grade CDS swap indices

The investment, less a 1% arrangement fee, will be invested in a cash deposit. This deposit can be leveraged into (long) index positions in a "dynamic leverage" manner. Leverage is limited by a complex formula to constrain the "value-at-risk" to a level that is unlikely to trigger a cash-out event – the factors affecting permissible leverage are discussed further below. The underlying investments are:

- 50% "Dow Jones CDX.NA.IG" index – the 125 most liquid investment-grade North American CDS contracts
- 50% "iTraxx Europe" index – the 125 most liquid investment-grade European CDS contracts

These are rolled every 6 months into new investment grade contracts, minimising (but not eliminating) the risk of default. This is contrasted to a CDO, in which names downgraded to sub-investment grade are not replenished and the investor remains exposed to them.

Since 1996, 8 credits have defaulted while still in their investment-grade indices (*i .e.* within 6 months of last index rollover, at which point they were still investment-grade). Accounting frauds such as Enron and Parmalat feature prominently in this list; however, other operational shocks can also be the cause. For example, the grounding of flights, additional security costs and reduced passenger numbers that followed “September 11” tipped Swiss Air into sudden default.

The issue is not managed; selection of indices and changes in leverage are based on pre-determined formulas. The target amount of value at risk is based on the combination of:

- *Fixed interest curve* (i.e. the theoretical value of the capital guarantee at maturity, plus coupons and fees).
- The credit duration of the indices (currently around 4.5 years), applied to a spread gap of 30% widening. Where the index spread is less than 67bp, a minimum spread gap of 20bp applies.
- 1.4% of the index face value to cover default risk.

Note that a series of severe losses could result in “cash-out” and termination. This would result in a near total loss, unlike a standard CPPI credit note.

Although coupons are rated AAA, there remains a significant risk that, particularly in the later years, coupons may not be payable. The expectation is that unpaid coupons in response to a late “cash-out” event would not overly disadvantage investors, on the basis that they had been paid BBSW +190bp for a number of years. However, it is possible for adverse conditions to result in a poor overall return.

Key Features – CPDO

- Compared to previous CPPI credit notes, CPDOs are typically longer-dated. The longer term reduces the risk of “cash-out” events and enables greater leverage to be employed. It can take a “full cycle” view compared to a 5-year credit product that could capture a “bear market” only.

- However, unlike CPPI, "cash-out" of a CPDO results in early termination, and loss of at least **90%** of the investment. (By contrast, in a CPPI investment "cashing out" results in deleverage, but ultimately a return of capital at maturity).
- As a result of this leverage, and the longer term to 'ride out" market cycles, Standard and Poor's modelling suggests that target coupons are very unlikely to be missed, and therefore that **income** can be rated AAA, not just collateralised principal as in CPPI.
- Unlike conventional CPPI, the *fixed interest curve* used is the cost of collateralising <u>both</u> maturity proceeds <u>and</u> coupons. Leverage is based on the size of the *shortfall* to *fixed interest curve*, rather than *ex cess above fixed interest curve* as in a CPPI investment.
- CPDOs introduce the concept of a "cash-in" event: If sufficient profits are made, the issuer will collateralise not just the maturity proceeds but also the <u>coupons</u> (and fees). The note will therefore stop taking trading risks, and effectively become a AAA FRN.
- In contrast to CPPI, leverage is <u>increased</u> as NAV falls, on the basis that <u>more</u> leverage is required to produce the targeted return. A CPDO is therefore a somewhat "contrarian" design, as opposed to CPPI which is "momentum-following".

Conceptually, the key difference between a CPDO and a CPPI credit investment is this: In the face of losses, the CPPI "gives up" – it deleverages, and ultimately "cashes out" to fixed interest, thereby ensuring the investor at least gets capital back at maturity. The CPDO "fights to the death" to earn the targeted coupon, taking on <u>more</u> risk in the face of losses and only "cashes out" if the NAV falls to under 10% of initial investment.

Key Risks

- CPDOs are a brand new product type, and while S&P have been convinced that risks to coupon and capital are relatively low this has not been tested across a credit **market cycle**.
- This makes them prone to **re-evaluation by rating agencies** as rating methodology evolves (particularly if new, unanticipated risks emerge). Conceivably, a change of heart could see an issue previously rated "AAA" downgraded due to a new approach.
- In particular, we have seen reports of a new CPDO rating matrix circulating internally in S&P that would not be consistent with a AAA rating for a product of this yield.
- Also, falls in the NAV due to **realised losses** in the index trades could result in ratings **downgrade** (at least of interest rating). It is not clear whether the rating could split if the security of capital and income diverged substantially.

- The note is exposed to **mark-to-market risks** from the trading positions. Buyback quotes from the market maker are likely to be based primarily on the NAV which could be **substantially below par**, and therefore result in realised losses should they have to sell.
- For example, the arranger's simulations project a **1% chance of NAV falling to the low 70's**, and a **5% chance of bottoming in the low 80's**. Such scenarios may also result in target coupons not being paid in full.
- 10 years is a long time and circumstances can change – it may not be possible for investors to **reliably forecast their liquidity requirements** over that period.
- In the extreme, a **cash-out (deleverage) event** would result in **earl y redemption** – investors would receive a major **enforced realised capital loss,** and not have the opportunity to "save face" by holding to maturity to receive their capital back in full.
- **Defaults** within 6 months of inclusion or retention in rolling investment grade indices still occur from time to time, particularly during periods of economic weakness. Defaults have a **direct impact on the NAV**.
- **Credit spreads widening**, with large discontinuities, could reduce NAV substantially, and place coupons at risk. In particular, unlike conventional CDOs, CPDOs directly participate in market value risks. A CDO's pricing is locked in, and cannot be affected by changes in market spread levels.
- Purchasing a leverage position in CDS indices is less compelling in periods (such as the present) of **historically low spreads**.

Risk Mitigation and Benefits

1. The inventors of CPDOs have applied sufficient rigour to demonstrate to S&P's satisfaction that risks to capital and coupon are commensurate with a **very high credit rating**.
2. The **targeted returns** are higher than available for similarly rated synthetic CDOs of long terms, and arguably no riskier. They are somewhat lower than targeted from equity or similar growth assets over that timeframe, but with relatively low correlation to equity returns.
3. In the arranger's simulations, even the low probability outcomes with very large falls in NAV still resulted in the bulk of **coupons being paid at BBSW + 190**, and therefore a commercial return was achieved from holding the product to full-term.
4. The arranger indicates that in the event of a cash-in, the issue would likely be **discounted at roughly BBSW**. This would generate capital profits of approximately 1.9% per year of remaining term. For illustration purposes only, a cash-in event after 7 years

would result in a capital profit of around $5, for a realised return approximately BBSW+ 245bp at current interest rates.

5. The **economic environment** remains relatively benign, and **corporate balance sheets** in good shape (despite recent moves towards increasing leverage).
6. The arranger has performed back-testing on the performance of such a structure invested **through the credit cycle** of 1996-2002 and found it to be surprisingly robust. 1996 was, like the present, a period of extremely tight credit spreads. Index positions would have suffered early as spreads widened, and several defaults occurred during the recession. However, the higher reinvestment rates on index rolls ultimately exceeded the cost of the early mark-to-market losses.
7. The arranger has put in place **hedging** on the credit indices at the time of an earlier CPDO issue. This locked in a coupon / rating combination that (reportedly) would not be possible under today's market conditions. Moreover, the value of the hedging positions is such that initial NAV will be $101 (effective a <u>negative</u> arranging cost up-front).
8. The CPDO leverages more as markets fall – an intuitively more pleasing response for a "contrarian" investor than in CPPI.

Indicative Investor Profile

This product is likely to suit investors:

- Looking for **very** long-dated and high-return structured credit product;
- Needing a strong principal rating and capital guarantee, including rated income;
- Able to invest for a 10-year period – while intended liquidity arrangements through making a market appear reasonable, there is no guarantee of liquidity in all market conditions.
- Able to cope with a high level of potential volatility in NAV, especially as this will be a primary driver of secondary market pricing.

It offers potential for a higher return than available on other high-rated, high-income products such as conventional CDOs but is likely to yield less than pure equity plays over its 10-year horizon. While it is possible to achieve these sorts of returns from equity / property linked notes, it is difficult to replicate the stability of coupon in such structures.

> Investors likely to want such an investment should seriously contemplate buying this issue. At current market conditions, the yield and rating combination cannot be replicated. The investor benefits from hedging put in place by the arranger prior to issue, and to some extent would be buying investments at "last month's price". This makes it particularly good **relative** value in the long-only structured credit space for clients who have Policy that would permit investments of this term.
>
> Term sheet and issue summary are available on request. Your Grove advisor can recommend whether these notes fit into your portfolio strategy.
>
> (Emphasis in original.)

136. On 27 November 2006, Mr Michell emailed Mr Tischler a document which contained a summary of the visits he had made to local councils in New South Wales between 20 November and 24 November 2006: J[1093]. Mr Tischler forwarded the document to Mr Hilder on 29 November 2006. Mr Michell's summary contained the following notes:

> **Oberon Council**
> Committed to purchase $500k-$1mill of CPDO
>
> **Bathurst City**
> Happy with CDO – will present to his boss for approval for $1mill
>
> **Forbes Shire**
> Never previously bought CDO or CPPI products. Positive response to CPDO. Believe they will purchase CPDO largely on our recommendation.
>
> **Narromine Shire**
> Very positive response to CPDO. Short of funds at the moment. Unable to make commitment until cash flow improves…
>
> **Moree Plains Shire**
> Liked the product. Will buy $2mill of CPDO. Asked for a regular economic update.

137. It also contained the following "overview" (at J[1093]):

> Generally the response to the product has been very positive both by Councils who have a good understanding of CDO & CPPI and others who are having a structured product explained to them for the first time.

The main “eye-brow raiser” is the ten year terms but this soon becomes largely irrelevant when they see the written commitment from LGFS to buy back at 24 hours notice.

The coupon definitely works as most have a maximum of only 110 to 120 bps on any current holding.

The positive image of LGFS is certainly something that comes out as providing a level of comfort for people and this acts to allay any concerns about the ten year term or the fact that it is a new product.

138. On 1 December 2006, Mr Tischler forwarded the Grove Report to Mr Lewis who himself forwarded it to others within ABN Amro. Later on that same day, Mr Tischler emailed Mr Silvester to the effect that LGFS was happy for ABN Amro to meet with Grove Research and Advisory but wanted an LGFS staff member to be present. What happened with respect to the Grove Report after this is of no present relevance, except to note that Grove Research and Advisory subsequently contacted LGFS to arrange a sale of the Rembrandt 2006-3 notes to three of their clients: J[1113].

139. Prior to their purchase of the notes, some of the Councils sought advice from advisers other than LGFS. Moree, for example, sought advice from Grange Securities Ltd. On 27 November 2011, Mr Stewart Calderwood of Grange Securities Ltd forwarded an email to Mr Mitchell Johnson and Mr Simon Hearn of Moree which stated that “at AAA investor (sic) won’t lose money as even if the rating agency assumptions are way wrong you build in such huge margins for error at AAA that you should be alright”. The email also noted that the “current market rally has reduced spreads so it is far more likely now that the instrument will go the full term rather than being called early and there is considerable uncertainty over the instruments going forward as to a) whether they truly are going to work (sic) b) what will the rating agencies do going forward and what they will do for existing deals”.

140. Each Council invested in Rembrandt 2006-3. The following table, extracted from the trial judgment, summarises the primary judge’s findings about the amount invested by each Council in Rembrandt 2006-3, the date or dates on which each Council communicated to LGFS its decision to invest, the date each Council (excluding Bathurst) signed a transfer and acceptance form and the amount each Council received after the investment cashed out: [SAF6].

Council	**Investment in Rembrandt**	**Communication of decision to invest to LGFS**	**Date Transfer and Acceptance Form Signed**	**Redemption Amount**
Eurobodalla	$500,000	3.11.06	6.11.06	$33,387.08
Parkes	$3,000,000	3 or 4.11.06	8.11.06	$200,322.50
Corowa	$1,000,000	2.11.06	9.11.06	$66,774.17
Orange	$1,500,000	13.11.06	23.11.06	$100,161.25

Moree	$2,000,000	27.11.06	29.11.06	$133,548.33
Oberon	$1,000,000	13.11.06	5.12.06	$66,774.17
Deniliquin	$500,000	24.11.06	11.12.06	$33,387.08
Bathurst	$1,000,000	28.11.06	21.12.06 (transaction completed via Austclear)	$67,043.10
Narrandera	$2,000,000	13.02.07	3.04.07	$133,548.33
Murray	$1,000,000	17.01.07	17.04.07	$66,774.17
Cooma	$2,000,000	17.05.07	23.05.07	$133,548.33
Narromine	$500,000	24.05.07	20.06.07	$33,387.08
Ryde	$1,000,000	24.05.07	27.06.07	$66,774.17

These notes will be referred to as the **LGFS Sold Notes**.

141. LGFS retained some $26 million of the Rembrandt 2006-3 notes (the **LGFS Retained Notes**).

8. DECLINE OF THE REMBRANDT NOTES

142. On 21 March 2007, LGFS held a board meeting at which it was noted that the sale of structured financial products had slowed in financial markets and that while LGFS had sold 50% of its issue of Rembrandt 2006-3, of “the other six issues announced, four were cancelled, one was postponed and another raised only $1 million”: J[1116]. On 22 March 2007, S&P published a **CPDO Evaluator** which set out its intended approach for modelling future CPDO structures: see [366] and [368] below. Mr Hilder considered that the CPDO Evaluator, although ostensibly applying to only future CPDO structures (a matter which was stressed by ABN Amro), would impact on perceptions of the Rembrandt notes: J [1369]. Nonetheless, LGFS did not bring the CPDO Evaluator to the attention of the relevant Councils, including Narromine and Ryde who were yet to subscribe for the notes: J [1369]. Between 2 April and 29 May 2007, Rembrandt 2006-3 was priced at between 99.34 (98.44 in ABN Amro’s ledger) and 101.99 (101.33 in ABN Amro’s ledger) cents in the dollar: [SAF290] and J[2210]. By June 2007, the Rembrandt 2006-3 notes held by LGFS had reduced in price by $500,000: [SAF291] and J[1361]. On 20 December 2007, S&P placed the Rembrandt notes on “CreditWatch Negative” status, meaning that it was possible that the rating of the notes would be downgraded in the next three months: [SAF218] and J [1131]. On 20 February 2008, S&P announced that it had downgraded the rating of the Rembrandt notes to BBB+ status, at which point the notes had a value of about 35% of par: [SAF219] and J[1132].

143. On 7 March 2008, LGFS circulated a letter to each of the Councils, suggesting options that might avoid the Councils having to incur a realised loss on the notes. Four of the five proposed options required the Councils to invest further funds. The remaining option was to continue holding the notes. None of the options which required the investment of further funds were acceptable to any of the Councils: [SAF294] and J[1132].

144. LGFS sold the LGFS Retained Notes to LGSS on 20 March 2008. On 9 October 2008, LGFS sent a letter to each of the Councils stating that they could no longer advise them about what

to do about the Rembrandt notes: [SAF295] and J[1133]. It was also in October 2008 that the Rembrandt notes cashed out: J[2275].

PART 3: S&P'S RATING AND ABN AMRO'S KNOWLEDGE THAT THE RATING LACKED REASONABLE GROUNDS AND WAS MISLEADING: ABN AMRO aPPEAL GROUNDS MATRIX ROWS 61 AND 62

1. CHRONOLOGY OF EVENTS RELATING TO THE VOLATILITY ISSUE

1.1 Introduction

145. ABN Amro challenges the finding made by the primary judge that it knew that S&P's rating of the Rembrandt notes lacked reasonable grounds and was misleading.

146. An essential part of this challenge is that ABN Amro claims that it had reasonable grounds to believe that S&P rated the Rembrandt notes using an assumed 25% volatility (together with S&P's other base case parameters) and that the notes could be rated AAA using 25% volatility.

147. The primary judge's findings contrary to ABN Amro's claims are stated at J[3143], J[3148]-J[3149] and J[3162(3)]. A critical part of her Honour's findings, which is challenged by ABN Amro, is that when each series of the Rembrandt notes was issued, ABN Amro knew that S&P was using a 15% volatility assumption which it knew from at least early October 2006 to be flawed. This issue is referred to as the "volatility" issue.

148. As part of its challenge to her Honour's finding that ABN Amro knew or ought to have known that the notes could not be rated AAA using 25% volatility, ABN Amro submits that the modelling of the notes, then described as the Surf CPDO, in the period from May to June 2006 was not applicable to Rembrandt 2006-2 or Rembrandt 2006-3 because the structure of those notes had been adjusted in about late July 2006 to include "rebalancing on the rolls".

149. ABN Amro accepts that it did not put this submission at the trial but it submits that, for reasons to which we will refer later, it should be permitted to put the submission on appeal.

150. The PA Councils, whose submissions on this question were adopted by Bathurst and LGFS, submitted that it was not open to ABN Amro to put this argument, which was described as the "rebalancing" issue for the first time on appeal.

151. ABN Amro's contentions on the "volatility" issue and the "rebalancing" issue rely, in large measure, upon an examination of the documentary evidence.

152. Much of the documentary evidence comprised emails, some of which passed between ABN Amro and S&P, but many of the emails were internal to either ABN Amro or S&P.

153. Since the issue sought to be raised by ABN Amro depends upon whether it had reasonable grounds to believe that the AAA rating was justified, it is important to distinguish between the communications which were internal to S&P and those which were sent to ABN Amro or were internal to it.

154. Nevertheless, the parties accepted that a consideration of ABN Amro's contentions should be determined in light of the documentary material, considered in its full context.

155. The context is voluminous and consists of documents, some of which are referred to in the trial judgment, although not always in their full terms or in chronological order, and others which are found in various places in the appeal books.

156. In order to assist us in considering this issue we asked the parties to produce what was in effect an agreed chronology, prepared by counsel for the PA Councils and annotated by ABN Amro. We have drawn the chronological narrative set out below substantially from that document.

1.2 Background to the development of the CPDO

157. The background to the development of the CPDO can be traced to the period commencing in late 2005 and early 2006: see Part 2 , Section 3 above and J[79].

158. At that time two groups of employees within ABN Amro were working on the development of structured credit products which would be designed to obtain high credit ratings from S&P notwithstanding changes which were then emerging in market conditions for such products: J [79]-J[81].

159. One of the employee groups was the London-based Exotic Credit Derivatives Group or **ECD Group**. It was responsible within ABN Amro for structuring, trading and marketing structured credit products: J[79].

160. The members of the ECD Group included Mr Richard Whittle, Mr Jamie Cole, Mr Paul Silcox, Mr Dave Poet and Ms Caroline Bosch. The positions they held in the ECD Group are described by the primary judge at J[72].

161. The other relevant employee group within ABN Amro was the Structured Credit Marketing Group or **SCM Group**: J[79].

162. The relevant members of the SCM Group were Mr Michael Drexler, Mr Juan-Carlos Martorell and Mr Chris Hodgeman. Mr Drexler and Mr Martorell were based in ABN Amro's New York office. Both were former employees of S&P. Mr Hodgeman was based in Hong Kong. The positions they held within ABN Amro are described by the primary judge at J[72].

163. One of the products on which ABN Amro's ECD Group and SCM Group were working was a new Dynamic Participation Note or DPN. ABN Amro had been working with S&P on the model for the DPN to ascertain the credit default risk, and hence the indicative rating for that product: J[80].

164. At about the same time, ABN Amro was working on another product which adopted the general framework of the DPN but with a number of alterations. A major alteration was the way in which leverage was employed. The alteration was to invert the way in which leverage was used so that leverage was increased when the product performed poorly and decreased when it performed well. For that reason the product was called the anti-DPN. Later, the anti-DPN model became the CPDO: J[81].

165. Another major alteration to the DPN which was made in the anti-DPN was a capping feature. It capped the return on the product by providing a cash in mechanism so that the risk associated with trading in the underlying indices to which the product was linked, ceased when the product earned enough to pay the coupon throughout the term and the principal on maturity: J[81].

166. On 11 March 2006 Mr Poet circulated an email within ABN Amro to a number of senior personnel including Mr Whittle, Mr Drexler, Mr Cole and Mr Silcox. The email attached some notes which outlined ratings achievable with S&P for DPNs. It also set out some parameters for modelling anti-DPNs and their rating implications. The anti-DPN section of the paper was followed by a note stating that (see also J [782]):

> S&P have indicated that they would accept the use of [volatility] of 20% in the spread process…

167. On 12 March 2006 Mr Poet sent a further email to the same ABN Amro employees attaching a paper explaining the anti-DPN structure: J[83]-J[84]. The email observed that S&P held a presentation on rated CPPIs (a form of structured product which preceded the CPDO, and included the DPN) with 20 banks. This suggested some urgency for ABN Amro if it was to compete with the other banks.

168. Mr Poet's paper attached to the email considered the results of the anti-DPN using volatility parameters of 35% and 20% (noting that lower volatility should be helpful to the anti-DPN's performance): J[84].

169. Mr Poet's paper also explained the use of leveraging in the anti-DPN. He illustrated this by comparing it with a "casino strategy" involving the doubling and re-doubling of losing bets. The paper included the following remarks (J[84]):

> … the value between the beginning and the end of the game is volatile, if you hit a losing streak your net worth can become very low, however most of the time you will be able to "bet yourself out of the hole".
>
> …
>
> … given the volatility of the product we should ensure that investors know that it will likely trade way below par, however if they are willing to "stick it out" to maturity they may receive a good return.
>
> …
>
> The spread process is crucial to the anti DPN's performance.

170. On 4 April 2006 Mr Drexler sent an email to a number of S&P employees in New York including Mr Derek Ding and Mr Sriram Rajan. Mr Ding and Mr Rajan were employed as quantitative analysts in S&P's New York office. They were responsible for the modelling of the DPN and anti-DPN (and later the CPDO) for rating by S&P: J[85] and J[74].

171. Mr Drexler's email attached an explanation of the problems and "our fixes" to the DPN model. He proposed a "spread vol", that is to say volatility, of "from 35% to 25%". He said both were justifiable given the historical data. He went on to say (J[85]):

> Also, the spread vol of 25% seems to be reasonable in against the data which shows vol to be more in the sub 20% range.

172. Mr Norbert Jobst of S&P, who was one of the addresses of Mr Drexler's email of 4 April 2006 sent it on to other S&P employees including Mr Chandler. Mr Chandler was based in S&P's London office and was responsible for liaising with ABN Amro as well as certain employees of S&P, including S&P's quantitative analysts: J[86] and J[74].

173. Mr Chandler then emailed Mr Drexler on 6 April 2006 (with copies to S&P employees including Mr Jobst, Mr Ding and Mr Rajan) addressing, inter alia, Mr Drexler's arguments for reducing some of the parameters for the model, including the volatility and stating (J[86]):

> … can you provide some evidence for coming away from these inputs?

174. Mr Drexler replied on 6 April 2006, attaching data from the relevant United States and European credit default swap indices (namely CDX and iTraxx). Mr Drexler stated that the observed LT mean (presumably a reference to long term spreads) and volatility were considerably below current assumptions: J[87].

175. Mr Chandler then sent a further email to Mr Drexler on 6 April 2006 (with copies to inter alia Mr Ding and Mr Rajan). The email was to the effect that S&P wanted evidence "over and above" the two year period of the indices: J[89].

176. Mr Drexler replied on 7 April 2006. His email included an observation on the volatility issue. As to that issue, Mr Drexler stated that the volatility on both the CDX and iTraxx indices was below 20% and that this was confirmed by an analysis of bond spreads: J[89].

177. On 26 April 2006 Mr Silcox sent to Mr Cole his analysis of the rating stability of the anti-DPN. Mr Silcox's modelling showed that the anti-DPN should be capable of achieving better ratings than the DPN, using the same parameters for the anti-DPN as had been used for the DPN: J[91].

178. However, Mr Silcox's modelling also showed that the rating which could be achieved was sensitive to various inputs including initial spread and assumed long term spread. As the primary judge observed at J[91], if the assumed initial spread was reduced from 36 bps to 26 bps the rating fell from AAA to A+, and if the assumed long term spread decreased below the assumed rate of between 80 and 100 bps, the rating fell to levels as low as BB+.

1.3 The anti-DPN (or CPDO) is introduced to S&P

179. The primary judge said (at J[95]) that the first written communication between ABN Amro and S&P about the anti-DPN appears to be an email from Mr Drexler to Mr Rajan and Mr Ding on 2 May 2006. Mr Drexler's follow up email to Mr Ding stated that the "corporate traditional DPNs" did not work anymore and that 5 year spreads had fallen: J[95].

180. On 9 May 2006 ABN Amro provided S&P with a sensitivity analysis on anti-DPN stability for a 10 year note at LIBOR + 200. The parameters included a volatility rate of 25%.

181. On 16 May 2006 there was a telephone conference between S&P and ABN Amro. Mr Chandler made a file note of it. One of the issues that was recorded in the file note was volatility. Mr Chandler noted that ABN Amro wanted volatility to be assumed to be 25% for the purposes of modelling the CPDO: J[112].

182. Very shortly after the telephone conference Mr Drexler and Mr Ding had an email exchange: J [147]. As the primary judge explained at J[115], the effect of what took place was that S&P's assumed volatility for the product was 35% whereas ABN Amro sought 25%.

183. ABN Amro continued to press for the 25% volatility assumption in an email from Mr Drexler to Mr Chandler and others from S&P (including Mr Ding and Mr Rajan). Mr Drexler's email stated that a 25% volatility assumption was justified because (J[116]):

> … historically the credit indexes have shown 15% vol …

184. Mr Drexler also said that "we always roll into the 5 yr index" which limits the volatility and that the structure should have a lower volatility than an LSS (a structured financial product developed by ABN Amro and rated by S&P prior to the CPDO): see J[116] and definition J [23].

185. On 22 May 2006 Mr Silcox informed Mr Ding that in its modelling ABN Amro had assumed 25% volatility, a long term average spread of 100 and a mean reversion speed of 40%: J [120].

186. On 25 May 2006 Mr Drexler and Mr Martorell of ABN Amro had a conference call with Mr Chandler and others from S&P including Mr Ding and Mr Rajan. Mr Chandler's notes of the call record that (J[134]):

> when we use 35% vol. and S&P defaults we still get BBB?

187. On 26 May 2006 Mr Chandler sent an email to Mr Martorell requesting further modelling from ABN Amro. The email requested the results of modelling based on a number of scenarios including (J[138]):

> (1) Scenarios by Volatility; 15%, 25%, 30%, 35%

188. On the same day, 26 May 2006, Mr Cole (rather than Mr Martorell) responded to Mr Chandler's request. Mr Cole said (J[140]):

> We had (I understand) agreed to use 25% vols – using 35% is overkill…

189. Later in the day on 26 May 2006 Mr Cole sent an email to Mr Chandler (and to the other main members of the S&P and ABN Amro "teams") attaching a matrix of modelling results which is reproduced in the trial judgment: J[145] and J[146].

190. The matrix was based upon a coupon of around 2% above LIBOR and included a range of inputs for a specified number of defaults, evenly distributed over the 10 year period as requested by S&P: J[145]. It comprised a range of assumptions including four different

assumptions for volatility, namely 15%, 25%, 30% and 35% and LTAS ranging from 40 bps to 80 bps: J[146].

191. As the primary judge observed at J[3118], from the results of this modelling, Mr Cole knew that based on the number of defaults assumed by S&P, the CPDO could not achieve a rating of AAA if LTAS was assumed to be 80 bps or less at a volatility of 25%.

192. However, Mr Cole's matrix did show that upon those assumptions, but with a volatility of 15%, the model produced a AAA rating: J[146].

193. ABN Amro contends in the appeal that the modelling which was conducted on 26 May 2006 was an early version of the Surf CPDO which did not take into account "rebalancing on the rolls". Senior Counsel for ABN Amro points in this regard to the primary judge's observations at J[244] in which she referred to an amendment to the Australian CPDO made in August 2006 to rebalance on the rolls of the indices.

194. Later in the evening on 26 May 2006, Mr Martorell sent an email to Mr Chandler (with a copy to Mr Drexler) stating that (J[148]):

> Our quants have been working with your quantitative team for this last 3 months on the basis that the base case scenario assumes 25% spread vol.

195. Mr Martorell's email of 26 May 2006 included a statement that the historical volatility of the portfolio was less than 15% for its 2½ year history: J[148(c)].

1.4 ABN Amro communicates with S&P's rating committee

196. S&P's rating committee was due to meet on 31 May 2006. Mr Chandler was a voting member of the committee. Mr Ding and Mr Rajan were not voting members but they attended the meeting by telephone: J[157].

197. Shortly before the meeting of S&P's rating committee Mr Chandler sent to the members a rating analysis meeting paper or **RAMP**: J[157]. Under the heading "Results", the RAMP set out the results and different sensitivities of the results to the inputs chosen for the model: J [157].

198. The model for the base case scenario referred to in the RAMP was volatility 25%, LTAS 100 bps and MR of 40%. This produced a rating of AAA for a coupon of 2% above LIBOR. However, the RAMP went on to say that this was not the full story and the results varied for different sensitivities: J[157].

199. One of the sensitivities to which the RAMP then referred was volatility. The author stated that over the previous two years, the iTraxx and CDX indices had a volatility of 15%. A table was then set out based on volatility assumptions ranging from 15% to 35% and an LTAS ranging from 40 to 80: J[157].

200. The table showed that at a volatility of 25% with an LTAS of 80 or less the model did not produce a AAA rating but it did produce AAA at an LTAS of 80 with an assumed volatility of 15%: J[157].

201. The author of the RAMP went on to say that volatility was not the main dependent variable and that the rating was heavily dependent on the LTAS. The author then said (J[157]):

> Maybe the most valid result here is the 15% volatility table …

202. After the S&P rating committee meeting Mr Chandler sent an email to Mr Martorell, with a copy to Mr Drexler, and copies to S&P employees including Mr Ding and Mr Rajan. The email stated that the S&P committee could not ignore a scenario where low spreads continued into the future. This was a reference to LTAS below 80 bps at a volatility of 15%. The effect of the email was to ask ABN Amro whether the CPDO could justify a coupon of LIBOR + 2% at a AAA rating. Mr Chandler stated that (J[159]):

> The current view is that L + 200 bps is not giving a AAA rating.

203. Mr Cole sent an email to the ABN Amro team on 31 May 2006 about Mr Chandler's approach. He said that ABN Amro "are completely screwed" if they took this approach" and it was completely unrealistic if they (S&P) were assuming their AAA default vector because, if so, spreads would not remain "at these levels": J[166].

1.5 ABN Amro provide S&P with more analysis

204. On 1 June 2006 Mr Martorell sent an email to Mr Perry Inglis and Mr Chandler of S&P (copying the ABN Amro "team"). The email set out details of the sensitivity analysis that had been requested by S&P. It concluded by requesting that S&P review the additional analyses (J [172]):

> … with a view to confirm that the base case of 25% vol LTM = 100 is sensible. We want to launch this product asap …

205. The primary judge observed at J[175] that the modelling results contained in the attachments to Mr Martorell's email on 1 June 2006 showed that if S&P default rates were assumed (which ABN Amro did not consider they should be):

> … the CPDO did not achieve a rating of AAA other than at an assumed volatility of 15% and an assumed LTAS of 80 bps.

206. ABN Amro contends that, in view of the subsequent amendment to the model to take account of rebalancing on the rolls (J[244]), the analysis dated 1 June 2006 was an early version of the CPDO which did not take account of that factor.

1.6 S&P conducts further analysis

207. On 2 June 2006 Mr Ding distributed to the members of S&P's credit committee the results of further modelling which he had conducted: J[183]-J[184].

208. As the primary judge observed at J[185], it was apparent from the modelling results prepared by Mr Ding that they involved an assumed volatility of 15%. Moreover, as her Honour went on to say at J[185], the modelling contained assumptions as to LTAS and:

> … if the spread of 40 bps remained for one year only before rising to 90 bps the indicative rating was AAA but if the spread of 40 bps lasted for two years before rising to 90 bps [for the remaining 8 years] the indicative rating was only A.

209. Her Honour also found at J[186] that Mr Chandler emailed the results of the modelling to the ABN Amro team.

210. Several days later, on 5 June 2006, Mr Chandler emailed Mr Ding and Mr Rajan requesting that Mr Ding run the model for one year with an LTAS of 40 bps and the next nine years at a spread of 80 bps: J[190] and J[192].

211. On the same day, 5 June 2006 Mr Chandler sent an email to the S&P credit committee members (including Mr Ding and Mr Rajan). The email stated that the committee wished to be comfortable with a structure that reflected the current sentiment where spread levels remained relatively flat for the start of the transaction with some mean reversion to historic levels thereafter: J[191].

212. Mr Chandler's second email of 5 June 2006 continued by stating (J[191]):

> The run that we feel replicates this is a scenario where 1st year Long Term Mean = 40, 1-10 year, LTM = 80, spread vol = 15% …

213. Also on 5 June 2006, Mr Martorell sent an email to the main members of the ABN Amro "team". The email stated that Mr Martorell had just spoken to Mr Chandler who was trying to arrange a meeting of the S&P committee and that "it should be OK". Mr Martorell's email stated that S&P were most concerned with the scenario involving an LTAS of 40 bps for the first year and 80 bps for the following nine years: J[194].

214. Mr Martorell's email and Mr Cole's reply as set out in the trial judgment at J[194] do not make reference to the assumed volatility ratio.

215. Mr Ding conducted further model runs and distributed the results to the S&P committee using an adjusted model. A note attached to the results refers to a volatility of 15%: J[197].

216. The primary judge observed at J[199] that Mr Ding's results were based on an assumed volatility of 15%. Her Honour also observed that Mr Ding's results at an assumed LTAS of 40 bps for one year and 80 bps for nine years produced an indicative rating of AAA. But her Honour also noted that the indicative rating was adversely affected by assuming 40 bps for any period longer than one year: J[199].

217. On 6 June 2006 Mr Chandler informed Mr Martorell that S&P was comfortable that the structure could be rated AAA and he said that S&P were still considering the base case for surveillance of the rating: J[200].

218. On 7 June 2006 Mr Chandler sent an email to Mr Martorell and Mr Drexler about the relevant scenarios for surveillance of the rating. He set out the main scenarios, the first of which was for a volatility of 15%, mean reversion speed of 40%, LTAS of 40 bps for one year and 80 bps for the remaining term: J[203].

219. Her Honour made the following critical finding at J[204] about the communications referred to above:

> From the ABN Amro internal communication it is apparent that ABN Amro understood that S&P was comfortable to rate the CPDO AAA on the basis of modelling assumptions as set out in para (1) of Mr Chandler's email about ongoing surveillance – that is, starting at the current spread levels at that time, applying S&P default levels, volatility = 15%, mean reversion speed = 40%, LTM 1 = 40 bps for 1 year, LTM 2 = 80 bps for remaining term.

1.7 The launch of the CPDO

220. On 9 June 2006 ABN Amro prepared an announcement to its marketing team about the launch of the CPDO, which was called, at that time, the "Surf": J[206].

221. The primary judge observed at J[207] that the announcement attached the current version of the Surf Presentation which contained modelling assumptions consistent with ABN Amro internal communications about the details received from S&P: see [61]ff above. In particular, the assumptions included an initial portfolio spread of 36 bps, a volatility of 15%, and a spread of 40 bps for one year with 80 bps for the remaining term: J[207].

1.8 Some issues raised within ABN Amro about roll costs

222. On 19 June 2006, an ABN Amro employee who had been involved in the presentation of the CPDO to clients raised a number of questions with the ABN Amro team that had been raised by clients. One question was the cost of index rolls: J[210].

223. On, or shortly before, 3 July 2006 Mr Silcox carried out some modelling on the effect of roll costs. He then sent an email to other members of the ABN Amro team (and to others including Mr Hodgeman in Hong Kong) stating that "S&P do not model roll costs but do stress the number of defaults": J[216].

224. On the same day, 3 July 2006, Mr Silcox sent an email addressed only to members of the ABN Amro team. He said that they needed to think about the best approach to the subject of roll costs and how to raise it with S&P without S&P becoming "hung up on the roll cost and the modelling of it": J[217].

225. Mr Cole responded to Mr Silcox's email suggesting that ABN Amro should "get" S&P to emphasise the "highly stressed" default vector and not to get them [S&P] "thinking too much about it": J[218].

226. Mr Martorell replied on 4 July 2006 (J[219]) stating:

> We should avoid S&P to overthink [the roll costs question] and open a can of worms.

1.9 The CPDO in AUD

227. The primary judge said at J[227] that the first mention to S&P of the CPDO in Australia occurred on 21 July 2006 in an internal S&P email referring to ABN Amro's marketing of the product in Australia with a coupon of 190 bps and a rating of AAA.

228. On 25 July 2006 Mr Silcox sent an email to Mr Ding and Mr Rajan on which ABN Amro relies. The email does not address the rating of CPDOs denominated in Australian dollars but refers instead to ratings for notes denominated in Canadian dollars: J[227].

229. Mr Silcox's email of 25 July 2006 is set out at J[227]. It states, relevantly, that "we are thinking about making a tweak to the leverage rules" which involves unwinding the trade on the roll dates instead of, as previously, rolling over the "full notional" on those dates.

230. Mr Ding referred to this email in his affidavit, in the part which is reproduced at J[526] of the trial judgment. Mr Ding said in his affidavit that he communicated with Mr Silcox or Mr Drexler in late July 2006 about modelling a structure for a proposed new transaction that was similar to the Canadian dollar CPDO which was referred to in Mr Silcox's email of 25 July 2006: J[526].

231. Mr Ding went on to say in his affidavit that he recalled that one of the proposed transactions was similar to the Chess CPDO except that it was to be issued in Australian dollars with a coupon of "Australian LIBOR" plus 190 bps. He also said in his affidavit that he understood that the new transaction was to have re-balancing on the roll dates. Mr Ding said that the Australian dollar transaction subsequently became known as Rembrandt 2006-2: J[526].

232. In addition, Mr Ding said in the portion of his affidavit reproduced by the primary judge at J [526]:

> I used a base case volatility of 25%, a base case MR of 40% and a base case LTAS of 40 (for the first year) and 80 (for the remaining 9 years of the transactions).
>
> …
>
> I ran 100,000 simulations on the version of the Internal Model that provided for re-balancing on the roll date.
>
> The indicative rating yielded by the Internal Model for those runs was 'AAA'.

233. However, importantly, the primary judge said at J[527] that she did not "accept aspects of this evidence", that is to say, in particular, Mr Ding's statement that he used a 25% volatility base case.

234. The primary judge went on to say at J[528] that Mr Ding's evidence was that he had sent the results of the modelling to Mr Silcox on 2 August 2006, but that after this, Mr Silcox queried the rebalancing on the roll dates assumption and Mr Ding then re-ran the model without rebalances on the roll dates: J[528].

235. The primary judge completed her narrative on this exercise by stating that the results (apparently without rebalancing) yielded an indicative rating of AAA and that Mr Ding sent the results to Mr Silcox on 3 August 2006 as well as reporting the results to Mr Chandler: J [528].

236. There are two other paragraphs of Mr Ding's affidavit to which the primary judge did not refer but which are important in understanding the evidence of the rebalancing issue. The first is paragraph [55] in which Mr Ding explained that when he became aware of the Chess CPDO in about May 2006, he commenced work on a model to analyse the transaction. He described this model as the "Internal Model".

237. The second was paragraph [56] which we reproduce in part as follows:

> Initially I created one version of the Internal Model. That version did not automatically provide for rebalancing of the leverage notional on the roll date because this was not a feature of the CHESS CPDO as proposed at that time. …
>
> After rating the CHESS CPDO I created a second version of the Internal Model which provided for automatic rebalancing on the roll date. The reason for two models was that not all transactions were structured by the arranger to automatically rebalance at the roll date. …
>
> I used the rebalancing model for transactions that were structured to automatically rebalance on the roll date. By contrast, I used a model that did not provide for rebalancing for transactions that only rebalanced on the roll date upon the occurrence of pre-specified conditions (usually identified in the termsheet). Each version of the Internal Model was coded, and ran, in exactly the same way except for the rebalancing feature described above. In this affidavit I have generally not distinguished between each version of the model and I refer to them together, and separately, as the "Internal Model".

238. On 8 August 2006 S&P published a presale report for the "first CPDO structure" rated by S&P. The product was described as "Chess II Ltd" and the denominations were said to be in Euros, US dollars and Japanese yen, for a series of floating rate notes due in 2016. The presale report contained an explanation of the mechanics of the structure but it did not address assumptions in the model such as the volatility rate of the notional credit index portfolio. It contained an indicative preliminary rating of AAA.

239. On 11 August 2006 S&P published the Pre-Sale Report for Rembrandt 2006-2 rated by S&P: see [49]ff above. It also contained an explanation of the mechanics of the structure and contained an indicative preliminary rating of AAA: see [49]ff above. It did not address assumptions in the model such as the volatility rate of the notional credit risk portfolio.

1.10 Tightening spreads

240. On 14 August 2006 Mr Cole sent an email to the ABN Amro team, and to Mr Hodgeman in Hong Kong. The email stated (J[238]):

> Gulp … see average spreads have tightened in again and today average (cdx/itrax now 35 bps … This is now below the cushion level of 36 bps we did all our runs/sims on.
>
> Caroline [Bosch] – can you please check to see that ratings are still OK for all currencies based on current spreads. I imagine that we are still OK for deals with new rebalancing, but we need to definitely check the AUD/NZD ones based on this as they don't use new rebalancing method …

241. Also on 14 August 2006 Mr Cole sent an email to Mr Silcox to ask whether he had run ABN Amro's model for the AUD and NZD transactions. Mr Cole said he knew S&P had confirmed the ratings but wanted to know if ABN Amro had done so as Ms Bosch "was having trouble getting the correct results". Mr Silcox said he had not done so using S&P's parameters: J[239].

242. On 14 August 2006 Mr Cole sent a further email to the ABN Amro team, and to Mr Hodgeman in Hong Kong about the tightening of spreads. The email included the following (J[240]):

> Further to this, the EUR/USD/JPY are still comfortable (with rebalancing on rolls). The AUD and NZD deals were both OK for 36 bps. However, on 35 bps they are really borderline (AUD passes, NZD fails) … Both should pass comfortably if you used rebalancing on the rolls.
>
> …
>
> Something to seriously consider for AUD/NZD deals is still whether to switch …

243. A further email on 14 August 2006 addressed the volatility issue. It was from Mr Hodgeman to Mr Cole and the ABN Amro team. The email asked how S&P had come up with the assumption of 15% for their base case assumption: J[241].

244. Mr Martorell replied on 15 August 2006 (J[241]) stating that:

> Although in LSS S&P used 25%, LSS is very sensitive to spread process.
>
> …
>
> Remember that the "AAA" rating of CPDO was not really sensitive to the vol parameter. I think rating levels were almost identical with 15%, 25% and 35% … Since the CPDO rating is more sensitive to defaults than spread process S&P was fine to use their internal estimate of 15% for this product.

245. The primary judge observed at J[242] that, notwithstanding Mr Martorell's email, ABN Amro's own modelling showed that different volatilities had a material effect on the ratings. Her Honour went on to reiterate the finding she had made at J[175] (which we have referred to above at [205]) that, if S&P default rates were assumed, at an assumed volatility of 25%, with an assumed LTAS of less than 80 bps, the CPDO did not rate AAA: J[242].

1.11 The ABN Amro Surf Presentation

246. The content of the Surf Presentation has been referred to at [61]- [69] above. The document is dated August 2006 but it appears to have been made on 15 August 2006.

247. Importantly, as the primary judge said at J[38], the S&P base case is identified in the Surf Presentation as including an initial portfolio spread of 36 bps with a volatility of 15% and an LTAS of 40 bps for the first year with 80 bps for the balance of the term.

1.12 Further correspondence on tightening spreads

248. On 15 August 2006 Ms Bosch sent a further email to Mr Cole following up on his "Gulp" email of 14 August 2006 (see [240] above) and his reference in the later email of 14 August 2006 to the failure of the NZD transaction to attain a AAA rating: see [242] above. Ms Bosch appears to have re-run the simulation with a larger number of runs (50,000) but her email stated that the NZD transaction rated AA+ at an initial spread of 35 bps "without rebalancings on roll".

249. On the same date, 15 August 2006 Mr Hodgeman informed Mr Cole that the Australian CPDO would be amended to rebalance on the rolls of the indices: J[244]. The primary judge made that finding at J[244] but she did not refer to the evidence on which it is based. Her Honour went on to find at J[244] that the transaction documents for the Rembrandt transactions were amended to reflect this change.

250. The finding as to Mr Hodgeman's communication to Mr Cole on 15 August 2006 about rebalancing on the rolls appears to be supported by Mr Cole's next email in the "Gulp" email chain on 15 August 2006 in which he said:

> glad you did change –NZD still didn't pass with more sims.

1.13 Further emails about the rating

251. Later that day on 15 August 2006 Ms Bosch sent an email to Mr Ding following up on several points relating to the CPDO. She informed Mr Ding that she had obtained default probabilities for the AUD/NZ CPDOs of 0.44% and 0.54% respectively (that is to say, results giving a AAA rating) based on 15,000 simulations with no rebalances.

252. That number of runs appears to be small when compared with the 50,000 referred to in her earlier email and full details of the parameters which she used were not set out.

253. On 25 August 2006 Mr Rajan sent a lengthy email responding to questions raised by a client of ABN Amro. The email is lengthy and is set out in full in the trial judgment at J[253]. The email stated relevantly that:

> Our parameterisation for volatility (25%) is higher than has been historically realized
> …

254. Mr Rajan's email of 25 August 2006 also stated that S&P did not estimate historical parameters for the specific portfolio referenced in the CPDO. He said that theoretically, all parameters could be referenced via Merrill Lynch but the most useful reference was the JP Morgan index. He also said that S&P used that index, rather than the historical one because of its short history: J[253].

255. Mr Rajan's email concluded with a statement that S&P did not yet have a model for the CPDO (J[253]) and:

> For this trade, we had access to ABN Amro's source code.

256. On 28 August 2006, Mr Hodgeman forwarded Mr Rajan's email on to members of the ABN Amro team including Mr Cole, Mr Martorell and Mr Silcox. The message merely stated "FYI".

257. On 29 August 2006, Mr Cole forwarded Mr Rajan's email on to Mr Silcox, Mr Whittle, Mr Drexler and Ms Bosch (but not Mr Martorell). Mr Cole's email included an observation that S&P seemed to be saying that they were now using 25% volatility rather than 15%: J [256].

258. On 2 September 2006, Mr Lewis of ABN Amro in Australia asked whether his office could be given the rating model used for the CPDO as, without the model, they would be "flying blind": J[265]. There was no evidence that the model was ever provided.

1.14 S&P issues rating letter

259. On 5 September 2006, S&P issued the R-2 Ratings Letter to Mr Lewis. The R-2 Ratings Letter rated the Rembrandt 2006-2 notes AAA. On the same day Mr Ding sent an email to ABN Amro in London confirming that the AAA rating had been issued: J[267]-J[268].

260. Mr Ding was cross-examined about his email of 5 September 2006 confirming the rating. The transcript of the relevant part of the cross-examination is set out in the trial judgment at J [575]. The transcript amply supports the finding made by her Honour at J[576] that there was no document recording the results of any modelling runs of the Rembrandt 2006-2 notes as at 5 September 2006 when the R-2 Ratings Letter was issued.

261. The primary judge went on to say at J[576] that she was satisfied that there was no such modelling of the Rembrandt 2006-2 notes and that Mr Ding did not run any model for the CPDO using actual starting spreads until 10 October 2006. Her Honour said at J[576] that until 10 October 2006:

> I consider that Mr Ding used an assumed average starting spread of about 36 bps just as ABN Amro had done before spreads started to tighten …

1.15 Mr Martorell's comparative table

262. It appears that by September 2006 another well-established ratings agency, Moody's, was also involved in rating other ABN Amro CPDO transactions. On 28 September 2006 Moody's confirmed to ABN Amro that it had assigned a rating of Aaa (the equivalent of S&P's AAA rating) to an ABN Amro CPDO known as "**Castle**": J[279].

263. On 2 October 2006 Mr Martorell provided a client of ABN Amro with a table comparing the assumptions used by S&P and Moody's to rate the CPDO. The table which Mr Martorell provided is of some significance because it stated that S&P's assumption for "spreads" was mean reversion speed of 40%, volatility of 15% and LTAS (described as LMR in the table) of

40 bps for the first year with 80 bps for the remaining nine years. The table is reproduced in full in the trial judgment at J[281].

264. Mr Martorell's table also shows that S&P's AAA rating of the CPDO assumed default rates in accordance with its internal evaluator: J[281].

1.16 S&P realises 15% volatility not justifiable

265. The primary judge found that by 3 October 2006 S&P had decided that 15% volatility could no longer be justified for use in rating the CPDO and that 25% volatility had to be used. Her Honour also found that by 3 October 2006 ABN Amro was aware that S&P no longer considered 15% volatility to be an appropriate assumption and that 25% would be used for new CPDOs. Her Honour's findings are stated at J[2615], J[2655] and J[3139].

266. In making that finding the primary judge referred to an email from Mr Martorell dated 10 November 2006 to which we will refer later: see [356] below.

267. The primary judge also relied upon the fact that ABN Amro had been advocating a 25% volatility assumption to S&P based upon what was said to be an actual historical figure of 15%: J[3139]. She considered it was unlikely that S&P "botched" such a basic calculation by employing a 15% figure. Instead, her Honour reasoned that the more likely explanation was that S&P accepted the representations made by ABN Amro that the historical volatility of the indices was 15% and made no calculation itself: J[2615].

268. The evidence given by Mr Chandler at T2215.40 to T2216.3 that throughout 2006 he believed the historical volatility of the iTraxx/CDX indices to have been 15% does not detract from the primary judge's finding.

1.17 Mr Ding detects starting spread problem

269. On 10 October 2006 Mr Ding sent an email to a number of people in S&P including Mr Rajan and Mr Chandler stating that there was a potential problem with the initial spread used in S&P's calculations. The email is set out in the trial judgment at J[284].

270. Mr Ding's email went on to say that for most of the CPDOs, deal arrangers were using starting spreads of 35 or 36 bps. However, he stated that spreads had tightened in the past week and were then at 31 bps. He then said (J[284]):

> The note's performance is sensitive to the initial spread to an extent that if initial S = 32, it will not pass AAA test.

271. Mr Ding was cross-examined about his email of 10 October 2006. The relevant part of the transcript is reproduced in the trial judgment at J[581]. Mr Ding accepted in cross-examination that he had been modelling the CPDO for the two months preceding the email at a starting spread of 35 or 36 bps.

272. The primary judge found at J[582] that, based upon Mr Ding's concession in cross-examination, Rembrandt 2006-2 was never modelled at actual starting spreads. She made the same finding about Rembrandt 2006-3 at J[582].

1.18 Further discussion of the parameters

273. On 11 October 2006 Mr Cole sent an email to the ABN Amro team requesting them to ignore his earlier suggestion about additional fees which made the deal "very cuspy AAA /AA+". Mr Cole's email went on to say that:

> … the effect of the extra fee combined with the tightening of spreads since we last looked at this last week was more than our gut feeling, plus we have re-run with the new revised S&P spread vol.

274. This email was not referred to in the trial judgment, or in ABN Amro's written or oral submissions but it was inserted in the agreed chronology at ABN Amro's request.

275. By 12 October 2006 Mr Rajan said that S&P were receiving daily calls on quantitative issues relating to the criteria used in the CPDO. He said that, as a result, the quantitative analysts at S&P were considering quantitative issues about modelling CPDOs: J[285]. Mr Rajan made that statement in an email response to a request from Mr Stephen McCabe, a senior quantitative analyst at S&P's London office, (J[285]) that the S&P team:

> … put together a document with all of the parameters we needed to model a CPDO.

276. The primary judge referred to Mr Rajan's email of 12 October 2006 in finding (at J[2565]) that Mr Rajan held serious concerns about the validity of S&P's modelling of the CPDO from no later than August 2006.

277. On 12 October 2006 Ms Bosch sent an email to Mr Cole and Mr Martorell about some modelling requests. She said in the email that she had carried out some analysis of iTraxx and CDX data which showed an average volatility of 29%. However, she said that this figure was "not that much different" from the 25% volatility used by S&P: J[286].

278. The primary judge seems to have explained the reference to 25% in this email at J[2629]. She found that by 12 October 2006 ABN Amro knew that S&P had discovered the error it had made about volatility and had let ABN Amro know that it would be using an assumed 25% volatility for future CPDOs: J[2629]. Her Honour's findings at J[3135] and J[3136] are to similar effect.

279. The primary judge found at J[646] that ABN Amro knew that S&P realised "by early to mid-October 2006" that the 15% volatility assumption was not justifiable and was intending to use 25% volatility for future deals.

280. The early to mid-October date to which the primary judge referred at J[646] is to be contrasted with her finding at J[2639], J[2655] and J[3139] that ABN Amro was aware of that information by 3 October 2006.

281. The "early to mid-October date" is also referred to in an important finding made by the primary judge at J[649]. She found that S&P proved itself willing not to correct the 15% volatility error for existing CPDO deals "in the pipeline" as at early to mid-October 2006. Her Honour found at J[649] that:

> Those existing deals included Rembrandt 2006-3, as S&P was willing to treat that as a carbon copy of Rembrandt 2006-2 despite recognising that 15% volatility was unjustifiable.

282. This finding is not inconsistent with the finding made by the primary judge at J[320], based upon an S&P document published in October 2006 to which she referred at J[319], that S&P expected prospective arrangers of CPDOs to model their products on the basis of an LTAS of 40 bps for one year and 80 bps for the balance, a mean reversion speed of 40% and an assumed volatility of 25%.

1.19 Rembrandt 2006-3

283. On 16 October 2006 Mr Lewis notified Mr Chandler of S&P, and the ABN Amro team in London that ABN Amro's lawyers were drafting documents for the Rembrandt 2006-3 transaction involving the sale of $40 million of notes "to a bespoke investor": J[290].

284. Mr Lewis described the Rembrandt 2006-3 transaction as a carbon copy of Rembrandt 2006-2, except for an increase in expense fees to allow for a fee ABN Amro would be paying to the bespoke investor: J[290].

285. Initially, Mr Lewis indicated that ABN Amro wished to settle Rembrandt 2006-3 on 27 October 2006 but S&P was later informed that the transaction date had been deferred until 2 November 2006: J[290].

286. On 17 October 2006 Mr Lewis sent Mr Chandler the Rembrandt 2006-3 draft documents and a swap confirmation seeking his response on the same day, as Rembrandt 2006-3 was "a simple mark-up" from Rembrandt 2006-2: J[290].

287. The swap confirmation that Mr Lewis sent to Mr Chandler seems to have been the subject of an email communication the previous day, 16 October 2006, between Mr Silvester of ABN Amro's Sydney office and Mr Tischler of LGFS. Mr Silvester said in the email (J[1060]):

> We can lock in the terms of the deal as soon as you give us the go ahead. This will mean that ABN Amro will execute the hedge and protect LGFS from further spread tightening.

288. Rembrandt 2006-3 was hedged at 32.05 bps on 18 October 2006: J[316] and J[3143].

1.20 The stability analysis

289. On 24 October 2006 Ms Bosch sent an email to Mr Hodgeman setting out a rating stability analysis for the CPDO based on an initial spread of 32 bps, but not using S&P's assumed defaults. Ms Bosch's email stated:

> … this one is still run with 15% vol for the spread process. SP (sic) changed in the meantime to 25% vol.

290. Ms Bosch's email of 24 October 2006 went on to note that the trade with LGFS was hedged at 31.8 bps, and:

> [i]n general, such small changes to fees or spreads don't affect the rating stability.

291. In his oral submissions, Mr Jackman SC submitted on behalf of ABN Amro, that the effect of Ms Bosch's email was that small changes in fees or spreads did not affect the rating stability which was the subject matter of the tables contained in the email.

292. ABN Amro also submitted that the purpose of the stability analysis was to show what effect different scenarios would have on the AAA rating.

293. However, Mr Hutley SC, for the PA Councils, submitted that this email should not be taken to be cogent evidence that S&P (to ABN Amro's knowledge) was modelling the product at 25% volatility. This is because the email was merely a stability analysis conducted by Ms Bosch, who did not give evidence, so that the reason for her comment about S&P's change to the volatility was not explained. In particular, there was no suggestion that Ms Bosch was involved in the direct dealings between S&P and ABN Amro about deals in the "pipeline".

294. On 25 October 2006 Mr Hodgeman extracted the content of Ms Bosch's email of the previous day and emailed it to Mr Silvester in Australia, without acknowledging Ms Bosch as the source of the information.

295. Mr Hodgeman's email of 25 October 2006 contains the statement originally made in Ms Bosch's email that "SP (sic) changed in the meantime to 25% vol".

296. Mr Hodgeman's email to Mr Silvester of 25 October 2006 appears to be the source of statements made by Mr Silvester in an email sent by him to LGFS on 25 October 2006. The relevant part of the email is extracted in the trial judgment at J[294] as follows:

> S&P have changed the vol from 15% to 25% in their modelling assumptions. This has had just a minor effect on the table …

297. The primary judge made two relevant observations about the email at J[296]-J[297]. First, she said that none of the results in the table were based on S&P's assumed defaults. Second, she said that Mr Silvester's statement about the change in the volatility assumption must have been wrong. This was because, as she said at J[297]:

> If S&P had changed the volatility assumption from 15% to 25% for the modelling of the Rembrandt CPDO all of the earlier modelling indicates that, without changes to S&P's other assumptions, the Rembrandt CPDO would not rate AAA.

298. The primary judge went on to say at J[298] that this finding was not to suggest that Mr Silvester knew the information to be wrong. Rather, ABN Amro in Australia did not have access to the model and thus was "flying blind": see [258] above. The Sydney office was dependent upon Mr Cole and Mr Martorell, in particular, to provide accurate information about issues raised by LGFS as to the stability of the rating: J[298].

299. The primary judge also said at J[3141] that, if Mr Silvester had the modelling results which Mr Cole and Mr Martorell had in London (which it appears he did not) he would have known that S&P did not change its assumption about volatility from 15% to 25%.

300. One other email on 25 October 2006 referred to the topic of rating stability. It was from Mr Cole to Ms Bosch with copies to a number of other ABN Amro employees including Mr Martorell and Mr Silcox: J[240].

301. Mr Cole's email of 25 October 2006 noted that spreads had tightened again to around 30 bps. He said that, at a minimum, ABN Amro should circulate an update to all sales persons who had live deals to give them "some colour" on where the market was and how it was affecting pending trades, saying "we can still get AAA but stability getting hit and will get worse if spreads tighten". Mr Cole also said that ABN Amro would have to consider "chopping coupons": J[293].

302. As the primary judge went on to say at J[293], Mr Martorell agreed that this would have to be considered (that is, cutting coupons) if spreads stayed where they were.

303. It is not clear whether the discussion about this topic between Mr Cole and Mr Martorell is relevant to the issue of volatility of the Rembrandt notes because the discussion within ABN Amro in this email chain focusses upon a product with a coupon of 100.

304. So much can be seen from the primary judge's remarks at J[299] and J[351] that by 26 October 2006 ABN Amro had at least six CPDO transactions which were required to be rated shortly by S&P, some of which were "carbon copies" of earlier deals that had already been rated. One such transaction was Rembrandt 2006-3, whilst others were not carbon copies because they were at different coupons.

1.21 "A crisis in CPDO land"

305. In late October 2006 there were a number of internal emails within S&P expressing concern about the accuracy of the ratings given by S&P to CPDOs: J[302]ff.

306. The catalyst for these communications may well have been newspaper articles which, by no later than 27 October 2006, had called into question the rating of CPDOs: J[2630].

307. The emails commence on 26 October 2006 with an internal S&P communication in which Mr Inglis referred to the need for discussion within S&P about "a crisis in CPDO land": J [302].

308. The primary judge's discussion of this topic commences at J[302]. She went on in the following paragraph to refer to communications dated 27 October 2006 between Mr Chandler, Mr Wong and Mr Ding which culminated in a question from Mr Inglis, set out at J[303]:

> … Are our ratings under pressure?

309. Another S&P employee, Ms Andrea Bryan responded: "I would say yes": J[304]. Mr Inglis then said (J[305]):

> And I would disagree. This is analytical bs at its worst. I know how those ratings came about and they had nothing to do with the model!

310. On the same day, 27 October 2006, Mr Inglis sent an email to Mr Wong asking for his comments to which Mr Wong replied, stating amongst other things (J[306]):

> Drexler is a smart and charming man. Cian [Chandler] and Sriram [Rajan] were, I think, sandbagged a little. The model was a work in progress … and Drexler simply bulldozed it through.

311. Mr Wong's email went on to say that the product which was issued at LIBOR + 200 with a AAA rating gained huge attention at a time when the spread on the underlying credit indices was 34 bps: J[306]. He continued as follows:

> There are two approaches to this:
>
> (1) stick with all current assumptions and emphasise that we stress other factors …
>
> (2) Further limit the existing parameters to the 3 or 4 deals. Change the parameters for all other deals.

312. These two options, identified in Mr Wong's email, were referred to by the primary judge (together with certain other matters) as giving rise to the inference that S&P rated the Rembrandt 2006-3 notes using the same criteria as it used for the Rembrandt 2006-2 notes because it was a "repeat deal", or "carbon copy" which was therefore rated on the basis of, inter alia, an assumed volatility of 15%: see J[344], J[649], J[2642], J[2643] and J[3148].

313. A further internal S&P email sent during this period and addressing concerns about the rating was an email from Mr McCabe, of S&P's London office, to a number of other persons located at that office including Mr Chandler and Mr Inglis. The email was dated 29 October 2006. It is set out in the trial judgment at J[308] and includes the statement that "[t]his CPDO issue is a real mess".

314. On 30 October 2006 Mr Chandler communicated his concerns about the rating to ABN Amro in an email to Mr Cole and Mr Martorell, with a copy to Mr Inglis. The email is set out in the trial judgment at J[309]. It includes the following statement:

> We are of the opinion that the current level of spreads are at a level that would no longer make the probability of receiving a coupon of +200 basis points consistent with a AAA rating.

315. At about the same time, on 30 October 2006, Mr Inglis sent an email to Mr Wong (J[313]) stating:

> I don't think anyone is suggesting that 200 bps is now sustainable for new deals and ABN [Amro] have been told that too.

316. Also on 30 October 2006, Mr Martorell sent an email to Mr Cole and others in ABN Amro noting that ABN Amro had not yet got hold of S&P's "grid of initial spreads and coupons" but that he was setting up a call with S&P to "discuss CPDO deals going forward". Mr Martorell's email (J[314]) also stated:

> [a]s we know current deals that are in the execution process should not be part of the discussion.

317. Other emails dated 30 October 2006 and 31 October 2006 from ABN Amro, referred to in the trial judgment at J[315] and J[316] mention the hedging of the Rembrandt 2006-3 transaction which occurred several weeks earlier, and which was said to justify the preservation of the AAA rating.

1.22 The ratings letter for Rembrandt 2006-3

318. On 31 October 2006 S&P issued the R-3 Ratings Letter for Rembrandt 2006-3 to Mr Lewis at ABN Amro's Australian office. The letter was set out in full by the primary judge at J [318]. We refer to it at [51] and [53] above.

319. The primary judge found that no modelling was conducted by S&P for the rating of Rembrandt 2006-3 and that S&P rated it using the same criteria as were used for the rating of Rembrandt 2006-2, including, as we have said, an assumed volatility of 15%: see J[649], J [2642], J[2643], J[2708], J[3148] and J[3260].

1.23 More discussion about tightening spreads

320. On 1 November 2006 Mr Cole replied to the email dated 30 October 2006 from Mr Chandler about the effect of the tightening of spreads and its impact upon the AAA rating. He copied his email to other members of the ABN Amro team including Mr Martorell: J[321].

321. It is evident from the opening line of Mr Cole's email that Mr Chandler's email resulted in a discussion between ABN Amro and S&P. This was followed up by a grid that was set out in Mr Cole's email with different underlying spreads and different coupon figures which were said to produce a default probability of around 0.5% and hence a AAA rating.

322. Relevantly, the grid for the coupon of LIBOR+200 showed a five year spread of 30 bps, an index spread of 31 bps and a default probability of 0.49% with a rating of AAA.

323. Mr Cole's email went on to say that given current index spreads of around 28.5 bps, ABN Amro would be looking to market and close the CPDOs with a coupon of below 175 bps. He also said:

> I would suggest around 150 bps (to give some room for a bit more tightening of index spreads). Perhaps suggest 150-175 bps for index spreads 27-29, 175 bps for index spreads 29-31, and 200 bps for index spreads above 31.

324. Counsel for ABN Amro submitted that there was no reason to believe that the exercise described in Mr Cole's email was done at a volatility of other than 25%. He also submitted that the grid demonstrated that with very low starting spreads, and a volatility of 25%, a AAA rating could be achieved.

325. It is not clear whether that submission was put to the primary judge but, in any event, a subsequent email from Mr Chandler, which was not referred to in the trial judgment, shows that the submission must be rejected. The email was dated 3 November 2006 and stated that Mr Chandler and Mr Inglis told Mr Cole and Mr Martorell, apparently in the conversation

referred to in Mr Cole's email (or a conversation dated 2 November 2006 referred to at J[326] of the trial judgment) that:

> … the levels that they are getting are higher than we expect (but this is an ABN [Amro] model issue).

326. On 2 November 2006 Mr Martorell requested that Mr Chandler and Mr Inglis make themselves available for a telephone conference to discuss the "new spread environment and ratings": J[326]. The primary judge referred to this at J[326] and went on to refer to an email that Mr Cole circulated within ABN Amro following the conference.

327. The email from Mr Cole was dated 2 November 2006 and stated that he and Mr Martorell had been advised in a telephone call with S&P that S&P was not reviewing its rating methodology or assumptions for CPDO deals, whether existing or in the pipeline, but was looking to see what coupons had a "comfortable rating" for different underlying spreads given the recent significant tightening: J[326].

328. On 2 November 2006 LGFS acquired $40 million of the Rembrandt 2006-3 notes at a starting spread of 32.05 bps, the deal having been hedged at this initial spread on 18 October 2006: J [316] and J[3143].

1.24 Some further problems emerge

329. On 4 November 2006 Mr Rajan sent an email to Mr Sebastian Venus, another quantitative analyst with S&P, stating that he had been concerned since July 2006 about assumptions made by S&P in respect of the credit curve used in the model for the CPDO. He had first raised this concern in an email dated 6 July 2006. He had stated in the earlier email that the model simulations changed from AAA to less than BBB "if one moves from a fixed to a constant credit curve": J[221] and J[329].

330. The primary judge set out the relevant parts of Mr Rajan's email exchange of 4 November 2006 with Mr Venus and other persons within S&P at J[329]. Mr Rajan's comment (J[329]) included the statement that:

> When we first looked at this ABN [Amro] trade, we said that there might be a better way to model things … but we would do it later. Now the trade caught on and we are locked in.
> So I can accept the responsibility for not modelling things in a more systematic way

331. The primary judge observed at J[2564] that Mr Rajan's remarks in his 4 November 2006 email were made at a time when work on S&P's own model was also raising issues about the validity of the initial modelling and rating by S&P.

332. On 6 November 2006 Mr Venus distributed within S&P a matrix showing that the indicative modelling ratings were very sensitive to any assumed benefit of the roll of the indices: J [331]. Mr Venus informed Mr McCabe, of S&P's London office, that he was not comfortable with the roll-down benefit used by S&P. Mr Venus also said (J[331]):

> The important thing to highlight from this exercise is that the whole deal is extremely sensitive to an assumption that we do not know much about, and neglecting it entirely gives us results that go from AAA to sub investment grade.

333. ABN Amro submitted that this viewpoint was not passed on to it. We were not taken to any evidence to suggest that Mr Venus' matrix, or his comments, were passed on directly to ABN Amro but in our opinion nothing turns on this.

1.25 Further consideration of the rating

334. On 6 November 2006 Mr Cole asked Ms Bosch whether notes rated AA or AA+ by S&P for 10 years, at 15 times leverage, would be capable of carrying a coupon of $US LIBOR+200 bps: J[333]. Ms Bosch replied that it depended on how far S&P wanted to "haircut" the rating but (J[333]):

> @ 28 bps + 200/15 lev gives PD of 0.0065 which is strictly speaking still below AAA cutoff point.

See also J[3162(3)].

335. On 7 November 2006 Mr Chandler sent ABN Amro a document entitled S&P's CPDO ratings matrix. The primary judge set out the details which appeared under the heading "LMR Spread Process Parameters" at J[334]. The parameters were said to comprise a mean reversion of 40%, volatility of 25%, long term mean of 40 bps for one year and 80 bps for the remaining nine years. Assumed credit defaults were said to be an average of seven per year over the ten year period.

336. The matrix then set out a table which is reproduced in the trial judgment at J[334]. The table shows the ratings that would be produced for different coupons, ranging from LIBOR+200 to LIBOR+100, at different opening spreads, varying from 28 bps to 40 bps, and at leverages of 15, 12 and 9.

337. As the primary judge observed at J[335], the table showed the importance of the starting spread to the rating. Her Honour also noted at J[335] that the table showed that, with an assumed starting spread of 35 bps (rather than the earlier assumption of 36 bps which was not referred to in the table) the base case CPDO (paying LIBOR+200 bps) did not rate AAA, but only AA+.

338. Counsel for ABN Amro submitted that this did not contradict his basic hypothesis, that is to say, that at the 25% volatility rate said to have been assumed by ABN Amro, the notes were capable of producing a AAA rating. This was because, he submitted, the grid was a generic one which did not specifically address the Rembrandt 2006-3 notes.

339. There may be some force in the submission that the grid was a generic one as can be seen from the email sent by Mr Chandler to Mr Martorell on 7 November 2006 attaching the matrix. However, as Mr Hutley SC for the PA Councils submitted, emails are not proof of the

facts stated in them, and the real point of the exchanges between ABN Amro and S&P on this topic was that ABN Amro was concerned that the grid was directed at it, in the sense that it revealed deficiencies in ABN Amro's CPDO, thereby exposing its position in the market.

340. Mr Hutley's submission is borne out by an email response dated 7 November 2006 from Mr Whittle of ABN Amro to Mr Chandler and others about the matrix: J[336]. Mr Whittle stated that he was very concerned about the matrix because it implied that the AAA rating S&P had given to recent deals would not be replicated for similar deals at similar spreads in the future: J[336].

341. The primary judge went on at J[336] to highlight Mr Whittle's comment that:

> I think this would be extremely damaging for S&P's credibility in the eyes of both investors and banks.

342. Her Honour also observed, at J[338], that Mr Martorell was equally concerned, telling S&P that it should be made clear that the matrix did not apply to ABN Amro's CPDO structure.

343. Mr Inglis' email of the same date, 7 November 2006, to ABN Amro accepted that:

> No one is suggesting that the numbers in the grid are directly comparable with your deals but we do understand your sensitivity.

344. On 7 November 2006 Mr McCabe sent an email to Mr Inglis and Mr Chandler and other members of the S&P team (J[339]) suggesting that:

> … we tell ABN [Amro] we messed up in the first deal and will NOT be repeating this on any future trades. They therefore need to adjust the spread volatility of 15% to 25% in their model.

345. On 8 November 2006 Mr Rajan replied to the S&P team (J[240]):

> I am not clear how they used 15% to start with.

346. It was not suggested that the internal S&P emails of 7 November and 8 November 2006 were communicated to ABN Amro.

347. On 8 November 2006 Mr Martorell circulated an email to a number of ABN Amro employees including Mr Drexler, Mr Whittle, Mr Cole, Mr Silcox, Ms Bosch and Mr Hodgeman about S&P's new rating matrix: J[343]. The primary judge reproduced the email at J[343].

348. The relevant parts of Mr Martorell's email of 8 November 2006 are:

> Last night, S&P distributed a new "coupon/spread" ratings matrix based on a Generic CPDO structure, to us and a number of other banks …
> …
> However, what is particularly unhelpful is that the coupon/ratings grid based on different underlying spreads seems to indicate lower ratings would be assigned for a given coupon/spread than have actually been assigned to ABN [Amro] deals already printed …
> Following our call with S&P last Thursday [2 November 2006], S&P confirmed that

> they are not reviewing their rating methodology or assumptions for CPDO deals, either for existing deals or deals in the pipeline (which appears to have changed). …
> …
> S&P did last night verbally confirm the AAA rating on all the current deals and said they are not looking to downgrade.
> …
> The general message has to be the grid sent by S&P is for a Generic CPDO Structure and not tailored to our SURF structure.

349. An email from Mr Andrew Feachem of ABN Amro to sales staff dated 8 November 2006, reproduced in the trial judgment at J[345] followed up on Mr Martorell's "general message". The email included the statement (J[345]):

> It is important that you continue to push SURF with your accounts.

350. On 9 November 2006 Mr Martorell sent an email to Messrs Chandler, Ding and Inglis, with copies to Mr Cole and Mr Silcox. The email included tables with default probabilities for different coupons, different spread levels and different leverage "based on [Surf] parameters".

351. The coupons shown in the table were LIBOR+200 and LIBOR+150. The spread levels ranged from 26 to 32 and the leverage multiples were 15, 9 and 5.

352. Mr Martorell's email requested that S&P "get back to us to make sure that we get (sic) same results". He asked S&P to focus urgently on the 9 and 5 leverage multiples.

353. ABN Amro relies upon the entry in the table for the LIBOR+200 coupon at an initial spread of 28 bps with a leverage multiple of 15. In particular, ABN Amro points to the relevant line on the table for that product which shows a default probability of 0.64%, that is to say, a probability of less than S&P's cut-off point of 0.728%.

354. As Mr Hutley SC pointed out on behalf of the PA Councils, the table does not refer to 25% volatility. However, Mr Inglis replied to Mr Martorell's email on 10 November 2006 (J[350]) asking:

> Could you please confirm that you have run the vol at 25% – that is what we used to get to sign off your last two trades.

355. Mr Silcox replied, almost immediately to Mr Inglis confirming that the simulations were run with 25% volatility.

356. Mr Martorell also informed Mr Inglis in an email dated 10 November 2006 (J[353]) that:

> All Pds [default probabilities] are based on 25% vol. Since 3rd October we have been using a 25% vol as indicated at that time by Derek [Ding] and Sriam (sic) [Rajan] as new S&P vol assumptions for the CPDOs.

357. S&P issued its Post-Sale Report for the Rembrandt 2006-3 notes on 15 November 2006: see [55] above and J[357].

358. On the same day, 15 November 2006, Mr Martorell sent an email to Mr Ding confirming that by the next day Mr Ding was to get back to ABN Amro on the "scenarios that we highlighted in the spreadsheet".

359. Mr Ding responded the following day, 16 November 2006, stating:

> JC [Mr Cole]
>
> I ran all 5 scenarios you pointed yesterday.
>
> (1) Leverage *15, init S 30, L+200
>
> (2) Leverage *15, init S 28 , L+150
> (3) Leverage *9, init S 28 , L+100
> (4) Leverage *5, init S 30, L+50
> (5) Leverage *5, init S 28 , L+40
>
> They all passed AAA, and our results tied out with yours …"\

360. Later that day, Mr Cole replied to Mr Ding thanking him for confirming the ratings and "tie-out" of default probabilities for the grid. Mr Cole's email continued:

> I assume that as all these PDs tie out, we can assume our respective models tie out. We therefore have one major outstanding question … what PD should we use for AAA cut-off points … going forwards?
>
> As an example (and per our email of 1 November), L+200 gives AAA at an initial spread of 28 pbs in our model, though we have agreed not to go for this.

361. On 20 November 2006 Mr Chandler replied to Mr Martorell's earlier email of 10 November 2006 concerning the volatility rate sent to S&P on 9 November 2006. Mr Chandler said:

> We've discussed the cushion needed going forward and feel comfortable if you are using a cut off point of 50 bps, one question we have though on the matrix is which currency does this represent? Obviously, there are going to be differences by currency …

362. Mr Martorell replied stating that the matrix referred to US dollar LIBOR and he promised to send the default probabilities for Euros and Japanese yen.

1.26 Further development of S&P's model

363. The primary judge said at J[364] that by 22 January 2007 S&P's development of its model for CPDOs remained a work in progress. Her Honour (at J[364]) set out an email from Mr Inglis to others within S&P which included the following:

> In November last year our quant group were unable to tie out arrangers' models for static index trades and so the decision was made to move to create our own model that would incorporate all types of transactions …

364. The primary judge went on to say (at J[365]) that by 26 January 2007 Mr Inglis informed ABN Amro that S&P's CPDO model was working but her Honour referred to subsequent internal communications within S&P which indicated that further work was required.

365. The primary judge said at J[366] that at the time of Mr Rajan's resignation from S&P, on or about 16 March 2007, the S&P CPDO model remained a work in progress.

366. The primary judge then referred (at J[367]) to S&P's announcement on 22 March 2007 about the launch of its CPDO Evaluator, which was a tool for modelling CPDOs: see [142] above.

367. Elsewhere in the primary judge's judgment (in particular when addressing the claim of the Councils against LGFS) she found that in about March 2007, S&P announced publicly that it was changing the way in which it approached the rating of CPDOs: see J[1196], J[2061], J [2140 (13)] and J[2207].

368. Although the primary judge did not make a finding in those paragraphs that S&P's announcement about its change of approach was reflected in its CPDO Evaluator, the chronological narrative which we have set out suggests that the CPDO Evaluator to which her Honour referred at J[367] took into account S&P's revised approach to the rating of CPDOs.

369. The primary judge concluded her narrative of the development of S&P's model at J[376] by referring to an S&P document which showed that, using S&P's original modelling, the "first wave of CPDOs" had a default probability consistent with a AAA rating but using the new model the same CPDOs had a default probability corresponding to a rating of A-.

370. In the previous paragraph of her judgment, J[375], the primary judge set out an email sent by Mr Rajan on 5 June 2007 (after his resignation) to another S&P quantitative analyst stating:

> Aside from explaining to you how we got 40/80 LTM, 30/25 vol and the history of that … I admit and accept responsibility for allowing that to start …

1.27 ABN Amro's "additional insertions" to the chronology

371. At the conclusion of what we consider to be the agreed chronology, ABN Amro made a number of "additional insertions".

372. These insertions consist, for the most part, of references to evidence which do not fit conveniently within the chronology which we have set out above. Some of the references are to evidence given by Mr Cole and Mr Ding, which the primary judge did not accept.

373. The matters to which ABN Amro refer in their "additional insertions" are addressed in our consideration of the submissions put to us by ABN Amro and the PA Councils on the volatility issue.

2. CONSIDERATION OF THE VOLATILITY ISSUE

2.1 The rebalancing issue

2.1.1 Entitlement to raise rebalancing issue

374. ABN Amro submits that it is entitled to raise the rebalancing issue on appeal because it responds to a finding made by the primary judge which did not correspond with the way in which the PA Councils ran their case at trial: ABN Amro Appeal Grounds Matrix Row 62A.

375. The critical finding to which ABN Amro points appears at J[3143]. There, the primary judge found that Mr Cole must have known that if S&P assessed the Rembrandt 2006-3 notes on an assumed volatility of 25%, it could not be rated AAA. Her Honour also found that Mr Cole must have known this from the results of "earlier modelling" by ABN Amro and S&P.

376. The "earlier modelling" to which the primary judge referred was submitted to be the modelling of the Chess CPDO that was conducted on 26 May 2006: see [187]-[195] above.

377. ABN Amro submits that this was at the heart of the primary judge's reasoning in the finding which she made about Mr Cole's knowledge and, since this was not part of the case run below, it is entitled to meet it by raising the rebalancing issue. The importance of it to ABN Amro's case on appeal is that the finding of knowledge is said to be flawed because it is linked to a state of mind about a model which was altered in about the middle of August 2006 to include rebalancing on the rolls.

378. The case which ABN Amro wishes to run on appeal is limited to a challenge to the primary judge's findings at J[3143] and J[3151], the error being said to be disclosed in a number of emails that were referred to in argument before us, and which are included in the chronology of events set out above.

379. ABN Amro submits that it is not precluded from raising the rebalancing issue on appeal by the principles stated in *Suttor v Gundowda Pty Ltd* (1950) 81 CLR 418 and *Coulton v Holcombe* (1986) 162 CLR 1 at 7-8 . It submits that the issue is not one on which evidence could have been adduced below which could have prevented it from succeeding and that the issue could have been raised, for the first time, in closing submissions at the trial.

380. The emails on which ABN Amro relies commence with Mr Silcox's "tweak" email to Mr Ding and Mr Rajan dated 25 July 2006 to which we referred at [229] above.

381. Four further emails are then relied upon. The first is Mr Cole's "Gulp" email of 14 August 2006 to the ABN Amro team and Mr Hodgeman set out at [240] above in which Mr Cole said he imagined that "we are still OK for deals with new rebalancing".

382. The second is Mr Cole's email of 14 August 2006 to the ABN Amro team and Mr Hodgeman set out at [242] above in which he said that both the Australian and New Zealand deals "should pass comfortably if you used rebalancing on the rolls".

383. The third is the communication from Mr Hodgeman to Mr Cole on 15 August 2006 that the Australian CPDO would be amended to rebalance on the rolls of the indices. We refer to this at [249] above.

384. The fourth is Mr Cole's email to Mr Hodgeman dated 15 August 2006 in which he said "glad you did change". We refer to this at [250] above.

385. Also of importance to ABN Amro's submission is the finding made by the primary judge at J [244] that the transaction documents for the Rembrandt transactions were amended to reflect the change, that is to say, rebalancing on the rolls.

386. However, even if we were to accept that these emails demonstrate that Mr Cole believed from about mid-August 2006 that the Rembrandt transaction documents had been "tweaked" to incorporate rebalancing on the rolls, there are a number of fundamental reasons why it is not open to ABN Amro to raise this argument on appeal.

2.1.2 Reasons why ABN Amro is not entitled to raise rebalancing issue

387. There are four principal reasons why ABN Amro should not be permitted to raise the rebalancing issue on appeal.

388. First, the rebalancing issue is not an abstract issue as to Mr Cole's state of mind. Rather, the rebalancing issue is an essential part of ABN Amro's contention that it believed the AAA rating given by S&P to both sets of Rembrandt notes was not flawed.

389. Thus, the effect of ABN Amro's contention on the rebalancing issue is that it believed that S&P used a 25% volatility assumption and that, with that assumption and S&P's other parameters, the AAA rating could be produced because of rebalancing on the rolls.

390. It was therefore incumbent upon ABN Amro to point to evidence that it believed that S&P had introduced a "tweak" into its CPDO model, namely rebalancing on the rolls, which enabled S&P to conclude that the notes could be rated AAA.

391. The emails upon which ABN Amro relies fall well short of this. Even if Mr Cole was the relevant mind for the purpose of establishing ABN Amro's knowledge, the emails say nothing about what he knew of the effect of the rebalancing exercise on S&P's model.

392. At most, the emails are concerned with Mr Cole's state of mind as to the modelling undertaken by ABN Amro itself using rebalancing on the rolls. This is incapable of supporting a finding as to ABN Amro's belief about S&P's rating process.

393. The rebalancing issue therefore fails at the threshold. The evidence upon which ABN Amro relies is not capable of supporting a finding that it believed that S&P's AAA rating was reasonably based and not inappropriate having regard to the "tweak" comprised in the rebalancing on the rolls.

394. Second, the evidence of Mr Cole and Mr Ding is inconsistent with the proposition for which ABN Amro now contends.

395. Mr Cole's affidavit evidence dealt with his knowledge and recollection of the base case assumptions adopted by S&P in the rating process. But he did not say that the assumptions included rebalancing on the rolls.

396. Indeed, the effect of Mr Cole's evidence was that the base case assumptions for both series of Rembrandt notes did not include rebalancing on the rolls, or at least that he had no recollection of rebalancing as a factor that influenced the AAA rating.

397. This conclusion follows from what Mr Cole said about the base case assumptions and the rating of the Surf CPDO and the Rembrandt notes.

398. Mr Cole set out his knowledge of the base case assumptions adopted by S&P in rating the Surf CPDO at paragraph 53 of his affidavit. The assumptions do not include rebalancing on the rolls. This may well be explained by the fact that rebalancing on the rolls was not an assumption adopted by S&P for the Surf CPDO. That would be consistent with ABN Amro's contention that the "tweak" did not emerge until late July 2006 but it does not support ABN Amro's contention on the rebalancing issue.

399. This conclusion is also consistent with Mr Cole's evidence in paragraph 72 of his affidavit that he became aware in late August 2006 that S&P "appeared" to be using 25% volatility as its base case assumption. This is because his belief, such as it was, did not include any reference to an assumption that S&P had adopted the rebalancing assumption.

400. The difficulty for ABN Amro which arises from Mr Cole's affidavit is that he said at paragraphs 109 and 114 that Rembrandt 2006-2 was essentially a carbon copy of the Surf CPDO (then described as the Chess CPDO) and that Rembrandt 2006-3 was the same as Rembrandt 2006-2 in all material respects.

401. The effect of Mr Cole's affidavit evidence is therefore that both series of Rembrandt notes adopted the same base case assumptions as the Surf CPDO, which did not include the assumption of rebalancing on the rolls, or at least that Mr Cole could not recollect rebalancing as a relevant assumption.

402. This conclusion is reinforced by the cross-examination of Mr Cole at T3285-T3286. He said in cross-examination by Senior Counsel for LGFS that he believed that Mr Chandler used the same model as had been used to rate earlier Surf products.

403. The only qualification in that evidence was that when he was asked whether, in rating the Australian notes (this is to say, Rembrandt), Mr Chandler used the same model as he had used in June 2006, Mr Cole said:

> I'm not 100% certain. They may have changed things in the interim.

404. Ultimately, Mr Cole conceded that, as far as he was concerned, there was no difference in substance in the structure since the initial rating was given in June 2006.

405. It is no answer to this evidence to say that, in light of the emails referred to above, Mr Cole must have had a lapse of memory. This is merely one of the many vicissitudes of litigation.

406. Mr Cole was the only witness called by ABN Amro. He gave evidence on behalf of the London "team". The other critical persons who could have given evidence for ABN Amro, including Mr Drexler and Mr Martorell, were either unable or unwilling to give evidence. But again, that is no answer. The only witness called by ABN Amro gave evidence on the topic. His evidence, taken at its highest, does not support the proposition for which ABN Amro contends, and indeed, is inconsistent with it.

407. The same conclusion applies to the evidence given on this topic on behalf of S&P by Mr Ding.

408. The effect of Mr Ding's affidavit evidence referred to above is that he created two versions of the model used for determination of the rating of CPDOs. One version of the model provided for rebalancing of the leverage notional exposure to the indices on the roll dates. The other did not.

409. Mr Ding's evidence therefore drew attention to the fact that rebalancing on the rolls was one of the integers applied by S&P in rating CPDOs by arrangers whose structures incorporated that parameter.

410. Importantly, Mr Ding's evidence did not suggest that rebalancing on the rolls would have any different effect on the rating compared with the rating which was produced by the model that did not apply rebalancing. Thus, it was for ABN Amro to raise this issue in cross-examination of Mr Ding if indeed it relied upon rebalancing as a component in the justification of the reasonableness of the AAA rating, and its belief in it.

411. Third, the question of the reasonableness of S&P's AAA rating of the Rembrandt notes, and the primary judge's finding that the ratings were fundamentally flawed, turned largely upon the expert evidence.

412. But the question of whether rebalancing on the rolls made any difference to the opinions expressed by the experts was not raised with them.

413. As the primary judge was at pains to emphasise, the Rembrandt notes were grotesquely complex instruments. The risks involved in them, and hence the reasonableness of their rating, "could not be gleaned by intuition but required mathematical modelling": J[1776].

414. No such modelling or investigation was undertaken by the experts because ABN Amro did not raise the rebalancing issue which it now seeks to agitate on appeal.

415. Fourth, the emails upon which ABN Amro seeks to rely to make good its proposition on the rebalancing issue are a very small number of the documents that were potentially relevant to this issue.

416. We were told that ABN Amro discovered a total of 9,341 documents in the proceeding, of which 1,248 were included in the tender bundle. We were also told that S&P discovered 5,508 documents, of which 852 were in the tender bundle. Thus, 14,849 documents were discovered of which 2,100 were in the tender bundle.

417. Mr Hutley SC on behalf of the PA Councils stated, correctly in our view, that if Mr Cole had given evidence as to his belief on the rebalancing issue, the PA Councils would have cross-examined him about it, and they would have wished to consider a large number of documents in order to do so. Those documents would not necessarily have been confined to the documents that were included in the tender bundle. The documents in issue would have potentially extended to the large number of discovered documents that were not included in the bundle.

418. It follows from the four matters to which we have referred that leave to raise the rebalancing issue must be refused both at a factual level and upon the well-established principles stated by the High Court in the authorities to which we have referred: see [379] above.

2.1.3 The primary judge's finding was within the case at trial

419. We reject the submission made by Senior Counsel for ABN Amro that the finding made by the primary judge at J[3143] did not adopt a submission that had been put to her Honour at trial by Mr Hutley for the PA Councils. This proposition was central to Mr Jackman's claim to be entitled to raise the rebalancing issue on appeal by way of response to a finding which he said did not correspond with the way in which the case was put against ABN Amro.

420. It is true that a substantial part of the PA Councils' claim against ABN Amro was a claim in fraud to which the finding at J[3143] did not respond.

421. The fraud claim was that ABN Amro provided S&P with a 15% historical volatility figure, knowing it to be false, in order to persuade S&P to adopt a 25% volatility parameter instead of the 35% figure for which it was pressing.

422. However, it is apparent from the PA Councils' closing submissions at trial, to which we were taken at length, that the factual issues were not limited to the knowing use of false historical figures in proving the 25% volatility assumption.

423. In particular, as can be seen from, for example, para 757 of the PA Councils' closing submissions, they contended that ABN Amro knew that, in rating the Rembrandt notes, S&P relied upon its earlier conclusion, reached in late May or early June 2006, that the CPDO was entitled to a AAA rating. The submissions went on to say:

> It [ABN Amro] therefore knew that the rating for those issuances of the CPDO was just as unreliable as the first AAA rating S&P gave to the CPDO.

424. The primary judge's finding at J[3143] is directly responsive to that submission. Moreover, ABN Amro did not seek to meet that proposition in its submissions (or in evidence) at the trial by pointing to the rebalancing issue. It cannot now be permitted to raise that issue.

2.2 The 25% volatility argument

425. As we endeavoured to explain in the introduction to Part 3 (see [145]-[156] above), ABN Amro's submission on the 25% volatility parameter lies at the heart of its challenge to the primary judge's finding that it knew the AAA rating was flawed.

426. ABN Amro's essential submission is that it believed from about late August 2006 that S&P had applied a 25% volatility parameter in forming the opinion that the Rembrandt notes warranted a AAA rating.

427. Senior Counsel for ABN Amro submits that ABN Amro should succeed on this issue regardless of whether we accept ABN Amro's contentions on the rebalancing issue (which we do not).

428. However, there are substantial difficulties in the proposition that the volatility issue is not dependent upon the arguments which underlie ABN Amro's contention with respect to rebalancing on the rolls.

429. One of the difficulties is that it was implicit in ABN Amro's submissions on the rebalancing issue that rebalancing on the rolls was a necessary integer in S&P's modelling process which justified ABN Amro's belief that, with the 25% volatility parameter, the Rembrandt notes warranted a AAA rating.

430. It would therefore follow from our rejection of ABN Amro's submissions on the rebalancing issue that there is no utility in considering, in isolation from that issue, the question of whether ABN Amro believed (or had reasonable grounds to believe) that the Rembrandt notes were rated AAA at 25% volatility.

431. In any event there are a number of reasons why ABN Amro's submissions on the volatility issue must be rejected. These reasons follow from the primary judge's detailed factual findings and the reasoning process which underlie her conclusion that S&P, to ABN Amro's knowledge, applied a 15% volatility parameter to the Rembrandt notes.

2.2.1 *The primary judge's findings on the volatility parameter*

432. The primary judge's critical findings on the volatility parameter are dealt with in the trial judgment in section 12.4.8 commencing at page 1081. She began her discussion of this topic by stating that what occurred in relation to this input within both S&P and ABN Amro was extraordinary. Her Honour went on to say at J[2611]:

> ... S&P made an *egregious error* induced by ABN Amro, corrected it after it had rated the Rembrandt 2006-2 CPDO (and many other CPDOs), and then decided not to apply the correction to the rating of the Rembrandt 2006-3 CPDO but instead to treat the Rembrandt 2006-3 CPDO as a carbon copy of the Rembrandt 2006-2 CPDO and thus deserving of the same AAA rating (which the Rembrandt 2006-3 CPDO could not have achieved if the error had been corrected for the rating of it, let alone if other basic issues, such as actual starting spreads, had been taken into account).
>
> (Emphasis added.)

433. The *egregious error* to which the primary judge referred was the 15% volatility parameter. She accepted at J[2614] that there is more than one way of calculating and modelling volatility but:

> ... when it came to calculating the volatility of these indices over the relevant period of their existence every one of the independent experts came to the conclusion that the average volatility was about 28%.

434. As we mentioned earlier and as the primary judge observed at J[2615], the notion that S&P botched such a basic calculation is difficult to accept. She considered that the more likely explanation, which was supported by Mr Chandler's evidence, is that S&P accepted ABN Amro's representations that the historical volatility of the indices was about 15%, and made no independent calculation.

435. The primary judge said at J[2619] that S&P's insistence at trial that it adopted a base case assumption of 25% volatility "is difficult to understand". She went on to refer to the base case parameters that Mr Chandler recommended to the S&P rating committee meeting of 31 May 2006 which included a volatility parameter of 25% but, as her Honour pointed out,

the RAMP which Mr Chandler prepared for the meeting stated that the most valid volatility rate may be the historical figure, which he wrongly assumed to be 15%.

436. We have set out at [196]- [203] above under the subheading "ABN Amro communicates with S&P's rating committee" the relevant communications between S&P and ABN Amro which the primary judge took into account in the conclusions which she reached at J[2619].

437. The primary judge observed at J[2619] that the S&P rating committee decided that further work was required because it was concerned about low spreads. This was a reference to Mr Chandler's email to Mr Martorell and Mr Drexler, sent after the S&P rating committee meeting, which incorporated a request for ABN Amro to consider the effect of modelling which contained a volatility parameter of 15%: see [202] above.

438. The primary judge concluded by stating at J[2619]:

> After this [i.e. the rating committee meeting], all modelling for rating purposes within S&P before the rating of AAA was issued for the first CPDO assumed volatility of 15%.

439. The first CPDO was the Surf. The primary judge found at J[2621] that it was apparent from ABN Amro's draft Surf marketing presentations as amended from 9 June 2006 onwards, that ABN Amro understood S&P to have adopted base case parameters which included a volatility assumption of 15%. She went on to observe that it was unlikely that ABN Amro got this figure wrong in the information it was intending to give to clients.

440. Importantly, the primary judge concluded at J[2621]:

> ABN Amro in fact changed the assumed volatility in its description of S&P's base case from 25% to 15% in the 9 June 2006 version of the draft Surf marketing presentation, no doubt because ABN Amro knew this to be true.

441. The primary judge's conclusion at J[2621] is fully supported by the evidence to which she referred elsewhere in her judgment. Her Honour set out at J[37]-J[38] the relevant parts of the Surf marketing presentation which bore the date August 2006. This document included the statement recorded at J[38] that the S&P base case assumptions referred to by ABN Amro included a volatility figure of 15%: see also [63]-[66] above.

442. For completeness, we were taken to a copy of the Surf Presentation that was in evidence at the time. The document was found at Vol 6 Tab 193 of the Appeal Book. The relevant statement of S&P's base case assumptions, including the 15% volatility parameter, appears at page 31 of the Surf Presentation.

443. The evidence on which the primary judge relied also included ABN Amro's announcement to its marketing team dated 9 June 2006 which attached the current version of ABN Amro's draft Surf presentation: see J[206]-J[207]. That version of the Surf presentation identified S&P's main modelling assumptions. The assumptions included a volatility parameter of 15%.

444. Having identified at J[2621] the importance of the 15% volatility assumption stated in the Surf Presentation, the primary judge then turned at J[2622] to an email dated 25 August 2006

from Mr Rajan of S&P which stated that S&P's parameterisation for volatility was 25%. We have set out the relevant paragraphs of the email at [253]- [254] above, and at [256] to the email forwarding Mr Rajan's message to various members of the ABN Amro team.

445. Whilst this email chain might possibly be thought to support the proposition that in late August 2006 ABN Amro believed the volatility parameter to be 25%, the primary judge rejected that proposition at J[2623]. Her Honour said:

> The explanation that must be accepted is that Mr Rajan's reference in his 25 August 2006 email is simply wrong. ABN Amro obviously thought it was wrong at the time and it was. ABN Amro did not change its Surf marketing presentation back to reflect 25% volatility at that or any other time.

446. The primary judge then moved somewhat ahead in the chronology of events to refer at J [2624] to Ms Bosch's calculation of the actual average volatility of the indices at 29%. This was apparently a reference to Ms Bosch's email dated 12 October 2006 to which we have referred at [277] above. Her Honour was highly critical of this, stating at J[2624], that when Ms Bosch made her calculation:

> ... ABN Amro as a whole appears to have suffered a significant lapse of corporate memory about its dealings with S&P about the volatility input.

447. This criticism was directed at the communications from Mr Drexler and Mr Martorell to S&P to persuade the relevant S&P analysts that the historical volatility figure was 15%. The primary judge observed at J[2624] that, although Mr Drexler and Mr Martorell were not quantitative analysts, they were not mere marketers. They were both former employees of S&P who put detailed arguments to S&P about quantitative inputs in S&P's modelling. Her Honour said at J[2624] that both Mr Drexler and Mr Martorell pressed for S&P to adopt a 15% volatility parameter on the basis that this was the historical figure of the relevant indices.

448. The primary judge then turned back at J[2626] to a slightly earlier dated document, Mr Martorell's comparative table dated 2 October 2006 to which we have referred above at [263]-[264]. Her Honour placed some importance on this document, pointing out at J[2628] that ABN Amro was still informing clients on 2 October 2006 that S&P had used a volatility parameter of 15%.

449. Although later in her judgment the primary judge found that by 3 October 2006 S&P discovered the error in the volatility rate, her Honour said at J[2628]-J[2629] that ABN Amro knew by 12 October 2006 that S&P had become aware of the error.

450. The primary judge pointed out (at J[2629]) that ABN Amro's internal documents did not disclose any serious concerns about the discovery of the error. She went on to find that the most likely explanation for the absence of any concern was that S&P had told ABN Amro that the 25% volatility figure would only apply to future deals other than those which ABN Amro already had in the "pipeline". Her Honour said at J[2629] that this explanation was supported by contemporaneous documents.

451. The contemporaneous documents which the primary judge apparently relied upon for this finding seem to be dated a little later in October 2006. The first is Mr Wong's email of 27

October 2006, the relevant part of which we have reproduced above at [310]-[311]. The second is Mr Martorell's email of 30 October 2006, the relevant part of which we have set out above at [316].

452. The explanation given by the primary judge at J[2629], namely that S&P's application of the 15% volatility parameter to deals "in the pipeline", was a "compromise" which ABN Amro was willing to accept, is consistent with a finding which she made earlier in her reasons at J [649]. Her Honour there found that S&P was willing "not to correct" the 15% volatility error for existing CPDO deals in the pipeline. Her Honour found that those deals included Rembrandt 2006-3. We have set out her Honour's findings on that issue at [281] above.

453. The primary judge considered that communications dated after 12 October 2006 dealing with how S&P had come up with the 15% volatility parameter should be viewed with care: J [2630]. She found at J[2630] that there was no apparent explanation for S&P's decision in October 2006 to change the volatility assumption from 15% to 25% other than that S&P had discovered its error.

454. The primary judge observed at J[2630] that by 27 October 2006 there were press articles calling into question the AAA rating. We refer to this topic above at [305]ff under the sub-heading "A crisis in CPDO land".

455. The primary judge continued her discussion of this topic at J[2632]. She referred to S&P's rating matrix which included a volatility parameter of 25%. We refer to the matrix, which was sent by Mr Chandler to ABN Amro on 7 November 2006 at [335] above. Her Honour went on to say at J[2630] that the matrix caused consternation within ABN Amro because it made public that previous CPDOs could not be rated AAA. This is borne out by ABN Amro's email to Mr Chandler dated 7 November 2006 to which we refer at [340] above.

456. The primary judge reiterated at J[2632] that S&P addressed ABN Amro's concerns by assuring it that the matrix only applied to future trades. However, as we pointed out at [339] above, when referring to ABN Amro's email of 7 November 2006 and the PA Councils' submissions on the matrix, ABN Amro's real concern was that the matrix was directed at it. This email of 7 November 2006 and Mr Inglis' email in reply make no reference to any assurance by S&P that the matrix was applicable only to future trades.

457. The primary judge went on to refer at J[2633] to Mr Martorell's email to Mr Inglis of 10 November 2006, the relevant part of which we have reproduced above at [356]. The email stated that since 3 October 2006 ABN Amro had been using 25% volatility as indicated at that time (that is, 3 October 2006) by Mr Ding and Mr Rajan.

458. The statement by Mr Martorell is not proof of the fact. Nor is it proof of ABN Amro's state of mind as at 3 October 2006. The primary judge did not state this in express terms. Rather, as mentioned above, she was satisfied that communications after 12 October 2006 such as Mr Martorell's email of 10 November 2006 (J[2630]):

> ... about how S&P had come up with the volatility of 15% need to be considered with great care.

459. The primary judge concluded her review of the email communications about the volatility assumption at J[2635]. She found that S&P's proposition that it adopted a base case for the

purposes of rating the CPDOs which included a 25% parameter for volatility "[was] without foundation".

460. The primary judge then turned to consider Mr Ding's evidence about the modelling of the CPDOs. She referred at J[2637] to Mr Ding's evidence that at all relevant times he had used a base case volatility assumption of 25% and that he had used 15% for "some sensitivity analyses". She found at J[2638] that Mr Ding's evidence about the volatility assumption had "serious problems".

461. The reasons which the primary judge gave for that finding appear at J[2638] and J[2639]. She placed considerable emphasis upon the events which followed S&P's rating committee meeting of 31 May 2006 and the statement in ABN Amro's Surf marketing presentation that S&P's base case parameter for volatility was 15%.

462. The primary judge's reasons for the finding also included the statements made in Mr Martorell's email of 10 November 2006 that ABN Amro had used the 25% volatility parameter since 3 October 2006. She said at J[2639] that the email was a contemporaneous record which was entitled to substantial weight. There is some tension between this observation and her Honour's statement at J[2630] that emails dated after 12 October 2006 need to be considered with care.

463. Ultimately, the primary judge also appears to have relied, in her reasons for rejecting Mr Ding's evidence, upon Mr Inglis' email of 10 November 2006. She refers to this at J[2639]. We set out the relevant part of the email above at [354]. Her Honour concluded at J[2639] that Mr Inglis' statement that S&P had used 25% volatility to "sign off your last two trades" was a strong indicator that:

> ... before those last two trades S&P had been using another volatility assumption, being 15%.

2.2.2 *The primary judge's three key findings on volatility*

464. The primary judge went on to make three important points on the volatility parameter commencing at J[2641]:

1. First, she observed at J[2641] that the Rembrandt 2006-2 notes were rated by S&P on 5 September 2006 which was before the change to the "new" volatility assumption of 25%. This appears to be a reference to 3 October 2006 which was the date referred to in Mr Martorell's email of 10 November 2006: see [356] above. Her Honour went on to say at J[2641] that it followed that the Rembrandt 2006-2 notes were rated on a base case assumption of 15% volatility. In fact S&P published the Pre-Sale Report for the Rembrandt 2006-2 notes, assigning a preliminary rating of AAA on 11 August 2006: see [49] above and J [45]. However, nothing turns on this because on any view the Rembrandt 2006-2 notes were rated AAA before 3 October 2006 which was the date upon which, on her Honour's finding, S&P adopted a new volatility assumption (to ABN Amro's knowledge) of 25%.

2. Second, her Honour found at J[2642] that although the Rembrandt 2006-3 notes were rated on 31 October 2006, that is to say after the critical date of 3

October 2006, it was treated as a repeat deal by S&P and thus rateable as AAA on the same basis as Rembrandt 2006-2, with an assumed volatility of 15%. Her Honour relied at J[2642] on "numerous references" to S&P treating Rembrandt 2006-3 as a repeat deal to support her finding. The references which her Honour appears to have had in mind include the statements made in Mr Lewis' emails of 16 and 17 October 2006 to which we have referred at [283]- [286] above. Moreover, paragraphs 109 and 114 of Mr Cole's affidavit and his evidence in cross-examination, was to the same effect: see [400] above.

3. Third, her Honour reiterated the finding that S&P treated the rating of Rembrandt 2006-3 as a repeat deal of Rembrandt 2006-2, "and thus was rated on the basis of an assumed volatility of 15%": J[2643]. Her Honour referred to Mr Wong's email of 27 October 2006 to support her finding: see [310]-[311] above. That email identified the options available to S&P in order to avoid the reputational issues that would otherwise have followed from an acknowledgment that S&P had "messed up" the rating. The options were "stick with all current assumptions" or "limit the existing parameters to the 3 or 4 deals".

465. Although the primary judge's second and third points appear to be virtually identical, the "numerous references" in the second point include, as we have said, Mr Lewis' emails. This may suggest that her Honour's "repeat deal" finding extends both to S&P and to ABN Amro's knowledge of it.

2.2.3 *The primary judge's rejection of Mr Ding's evidence*

466. The primary judge did not accept Mr Ding's evidence that he used a 25% volatility assumption in rating the Rembrandt 2006-2 notes. Her Honour's finding, and her reasons for it, are stated at J[2644]-J[2645].

467. The primary judge's essential reasoning is based upon her finding that, apart from some minor changes, S&P treated the Rembrandt 2006-2 transaction as a copy of the earlier ABN Amro CPDO, that is to say, the Surf CPDO. Her Honour pointed out that the modelling for that CPDO showed that it could not achieve a AAA rating with a 25% volatility assumption and the other base case assumptions which were incorporated into the modelling for the CPDO: J [2644].

468. The primary judge went on to say at J[2645]:

> Mr Ding's evidence is thus inconsistent with the contemporaneous documents bar one and all of the available modelling results. I do not accept that he modelled the Rembrandt 2006-2 CPDO using a volatility of 25% and found the Rembrandt 2006-2 CPDO to achieve a rating of AAA. I am satisfied that he modelled it using a volatility of 15% and found the Rembrandt 2006-2 CPDO to achieve a rating of AAA. I am also satisfied that had he used 25% volatility he could not have found that the Rembrandt 2006-2 CPDO achieved a rating of AAA. The same conclusion may be reached for the other extracts from modelling runs in and around this period.

469. Importantly, the primary judge said at J[2646] that she did not accept that there was any unfairness in the PA Councils' submission that the modelling results after the S&P ratings committee meeting of 31 May 2006 (see [194]-[203] above) were based on an assumed volatility of 15%. She said (at J[2646]):

> ... The dispute about S&P's base case involving 25% volatility or 15% volatility was a matter on which the [PA C]ouncils opened. It was obviously in issue.

2.2.4 *The primary judge's rejection of Mr Chandler's evidence*

470. The primary judge accepted Mr Chandler's evidence that he initially believed the appropriate volatility parameter to be 35%. Her Honour did not accept his evidence that he was ultimately persuaded to adopt a lower base case assumption of 25%. Her Honour found at J[2650] that Mr Chandler's evidence was affected by hindsight and that S&P used a 15% volatility parameter as a basis for assigning a AAA rating to the "CPDOs in question", that is to say, the Rembrandt notes.

471. The primary judge gave ample reasons for this at J[2650]ff. It is unnecessary to set out the details of her reasons in support of this finding since it is not challenged by S&P on appeal.

2.2.5 *The primary judge's rejection of ABN Amro's "reasonable grounds" submission*

472. The primary judge deals with the question of ABN Amro's knowledge of the volatility parameter in section 13.4.2 of her judgment under the heading "ABN Amro representations misleading?"

473. ABN Amro's submission at trial was, relevantly, that even if S&P's ratings lacked reasonable grounds, the representation made by ABN Amro (namely that S&P's opinion could be safely relied upon) was not misleading. This was because it was said to be an opinion genuinely held by ABN Amro for which ABN Amro had reasonable grounds: see J[3106].

474. ABN Amro submitted, in support of that finding, that Mr Cole's evidence established that ABN Amro genuinely believed that S&P had reasonable grounds for rating the Rembrandt notes as AAA, and that the ratings were the product of the exercise of reasonable care and skill on S&P's part: see J[3106].

475. The primary judge rejected that submission for reasons which included her observations of Mr Cole and her consideration of contemporaneous documents which revealed knowledge by Mr Cole that was inconsistent with his oral evidence, and which also revealed the involvement of other ABN Amro personnel in procuring the rating from S&P: see J[3108]ff.

476. The primary judge's consideration of Mr Cole's evidence included a lengthy analysis of what he, and other ABN Amro employees, knew about S&P's adoption of the relevant volatility parameter: see, for example, J[3113].

477. The primary judge's approach to Mr Cole's evidence is encapsulated in what she said at J [3108]:

> The idea that Mr Cole's evidence was unchallenged in any way is without foundation. It was apparent from the course of the hearing that both LGFS and the councils challenged the veracity of much of Mr Cole's evidence including his evidence about his state of mind at various times throughout the ratings process and his belief about the reasonableness of the rating. One noticeable matter is that much of Mr Cole's evidence about his state of mind at various times is difficult, indeed impossible, to reconcile with Mr Cole's own email correspondence contemporaneous with the events he was trying to recollect. I have already commented on the dangers of hindsight in respect of many of the witnesses in this case. Mr Cole, a person intimately involved with the development of this product which as the evidence discloses attracted such attention in the markets at the time because of its AAA rating and high returns and then failed causing no doubt substantial losses to many investors within two years, had as much if not more reason that others to give evidence affected by hindsight and self-interest. Inferences from the objective facts and the contemporaneous records are far more likely to be reliable indicators of Mr Cole's states of mind, and that of ABN Amro, than attempts at reconstruction some five or more years after the events in question.

478. The primary judge did not expressly reject ABN Amro's submission that Mr Cole was a witness of truth but she said, at J[3110], that the submission failed "to grapple with the reality of the situation". She went on to say at J[3111]:

> The fact is that Mr Cole's evidence that S&P appeared to him to be undertaking a thorough and independent review of the CPDO simply cannot be reconciled with the facts that Mr Cole knew or must have known at the time.

479. The facts which the primary judge found that Mr Cole knew or must have known included Mr Drexler and Mr Martorell's dealings with S&P about the volatility rate. Her Honour found at J[3113] and J[3115] that Mr Cole knew that Mr Drexler and Mr Martorell were liaising with Mr Ding and others at S&P and that they were pressing for a quick rating of the Surf CPDO, as well as pressing their statements that the underlying indices showed an average historical volatility of 15%.

480. The primary judge's reasons for finding that ABN Amro knew that S&P adopted the 15% volatility parameter include the finding at J[3118] to which we referred above at [191]. This was, that from the results of Mr Cole's modelling of 26 May 2006, he knew that the CPDO could not achieve a rating of AAA with a volatility assumption of 25%.

481. The primary judge found at J[3120] that ABN Amro knew that after the meeting of S&P's ratings committee on 31 May 2006 that S&P had moved away from the 35% volatility parameter which S&P initially favoured, not to the 25% volatility figure that ABN Amro advocated but to 15% volatility.

482. In coming to the conclusion that ABN Amro knew that S&P had adopted the 15% volatility parameter, the primary judge relied upon the dealings between Mr Drexler (whose "ingenuity was up to the task") and S&P, as well as the support provided by Mr Martorell in those dealings: see J[3121] and J[3122].

483. The dealings and discussions between ABN Amro and S&P about this issue did not proceed in isolation. They included other parameters such as the LTAS. The primary judge referred,

at J[3122], to Mr Cole's email of 31 May 2006 (see [203] above) that ABN Amro were "completely screwed" if S&P adopted the various parameters which S&P advocated.

484. But the primary judge went on to say at J[3123]:

> ABN Amro ought not to have worried. ABN Amro called in Mr Cole's boss, Mr Whittle, and went over Mr Chandler's head to Mr Inglis at S&P. Whatever occurred in the call between ABN Amro and S&P, the upshot was that ABN Amro did more modelling with the "low" LTASs but using 15% volatility and fewer defaults than S&P defaults. Mr Martorell provided this to S&P on 1 June 2006 and explained the justification for this as one of consistency – using low spreads as historically indicated but also with low defaults and low volatility as historically indicated (the latter, of course, being wrong). In other words, if low spreads were assumed by reason of history so also should low volatility and defaults be assumed.

485. The primary judge also found at J[3125] that ABN Amro knew by reason of Mr Chandler's email of 2 June 2006 (see [209] above) that S&P was using 15% volatility in its modelling and was considering this with the effect of a split LTAS, that is to say 40 bps for one year and 80 bps for the remaining nine years.

2.2.6 *The primary judge's findings about the effect of tightening spreads and its relationship to volatility*

486. The primary judge dealt at some length, commencing at J[3130], with email communications, internal to ABN Amro, about the effect of tightening spreads on the AAA rating, as well as the sensitivity of the ratings model to the volatility assumption.

487. The primary judge referred at J[3131] to Mr Hodgeman's email of 14 August 2006 querying the 15% volatility assumption and to Mr Martorell's reply of 15 August 2006 to which we have referred at [243]- [244] above. Mr Martorell's email stated, inter alia, that the AAA rating was not sensitive to the volatility parameter and "I think rating levels were almost identical with 15%, 25% and 35%".

488. The primary judge was very critical of the statements made in these emails. She said at J [3131] that they showed "an extraordinary lapse of corporate memory". She also pointed out at J[3131] that there were important mistakes in Mr Martorell's email which he and Mr Cole must have recognised to be "wrong and misleading".

489. One of the errors in Mr Martorell's email was the statement that the rating levels were almost identical at each of the stated volatility parameters. The primary judge said at J[3131]:

> ... Mr Cole was involved in these communications and keen to get an answer to Mr Hodgeman. It is unlikely that Mr Cole would not have read Mr Martorell's email closely. It is even more unlikely that Mr Cole, given his intimate involvement with and knowledge of dealings related to the CPDO, would not have appreciated that the true position was that the CPDO was highly sensitive to the volatility assumption and that all of the available modelling showed that the CPDO could not achieve a rating of AAA at anything other than 15% volatility if LTAS was below 80 bps.

490. The primary judge went on to say at J[3132] that she did not accept that Mr Cole did not realise that what Mr Martorell was telling Mr Hodgeman about the relevance of the volatility assumption was seriously wrong. She continued:

> Yet Mr Cole took no step to correct Mr Martorell's errors even though they were errors communicated to ABN Amro's own staff responsible for marketing the CPDO to potential investors in Australia. This too is consistent with the approach of ABN Amro in London to the LTAS assumption, the volatility assumption itself, the lack of modelling of roll costs and the potential impact of tightened spreads which ABN Amro had not chosen to share with S&P despite ongoing dealings with Mr Ding about the rating of various versions of the CPDO including Rembrandt 2006-2. ABN Amro London seems to have treated ABN Amro Sydney no differently from how it treated S&P.

491. Importantly, the primary judge stated at J[3137] that she did not accept Mr Cole's evidence that he did not appreciate that ABN Amro had given S&P incorrect information about the volatility assumption which S&P had then used to rate the Rembrandt 2006-2 notes.

2.2.7 *The primary judge's finding about the "new" volatility assumption*

492. The primary judge found at J[3135] that as at 2 October 2006 ABN Amro believed that S&P's base case involved an assumed volatility of 15%. Her Honour went on to say at J[3135] that she was satisfied that by about 3 October 2006 S&P had told ABN Amro that for future CPDOs S&P would use 25% as the new volatility assumption.

493. The primary judge went on to say at J[3139] that:

> ... the relevant point for present purposes is that despite Mr Cole's evidence to the contrary, it is impossible to accept that ABN Amro did not actually know as at 12 October 2006 that ratings of the CPDO based on an assumed volatility of 15% were unjustifiable, unreasonable and unreliable.

494. The primary judge gave reasons at J[3139] for this critical finding. The reasons include the proposition that the 15% volatility parameter was less than the parameter for which ABN Amro itself was contending and that by 3 October 2006, ABN Amro had been informed of S&P's erroneous 15% assumption.

495. The primary judge also made the following critical findings at J[3140]:

> Given the close supervision of all aspects of the rating and rating process of the CPDOs in which the ABN Amro London team engaged, actual knowledge of these facts leads inexorably to the inference of actual knowledge that ratings of the CPDO based on an assumed volatility of 15% were unjustifiable, unreasonable and unreliable. ABN Amro thereafter continued to deal with LGFS about the Rembrandt 2006-3 CPDO on the basis that as a repeat deal it too should obtain a rating of AAA from S&P (that is, when ABN Amro knew that the Rembrandt 2006-2 CPDO had been rated AAA using the unjustifiable, unreasonable and unreliable 15% volatility assumption).

496. Her Honour went on at J[3141] to refer to Mr Cole's attitude to tightening spreads, in particular from 25 October 2006. This appears to be a reference to Mr Cole's email of that date to which we referred at [301] above.

497. The primary judge's reasons at J[3141] and the two following paragraphs, J[3142] and J[3143], should be read together. The effect of what she said appears to be that Mr Cole took the same flawed approach at the end of October 2006 to volatility and tightening spreads. This finding appears to have been influenced by the critical step in her reasoning process, referred to earlier, namely, that ABN Amro (and Mr Cole) treated Rembrandt 2006-3 as a rerun of Rembrandt 2006-2. This is implicit in her finding at J[3142] that:

> Mr Cole took the course of reinforcing to S&P that Mr Ding had indicated already that Rembrandt 2006-3 should be fine to be rated AAA and tightened spreads should not matter as Rembrandt 2006-3 had been hedged some time back when spreads were higher.

498. The primary judge then addressed (at J[3143]) the issues of volatility and tightening spreads. She found that Mr Cole must have known that, if S&P rated Rembrandt 2006-3 on an assumed volatility of 25%, it could not rate AAA even if the assumed starting spread was 36 bps, which was higher than the actual starting spread.

499. ABN Amro challenged this finding on the basis that the primary judge was said, wrongly, to have supported it by reference to Mr Cole's modelling conducted on 26 May 2006. We dealt with this challenge above at [419]ff and rejected it.

500. The primary judge then made the following important finding at J[3143]:

> Mr Cole knew that at 35 bps the Rembrandt CPDOs were borderline in terms of the AAA rating even at 15% volatility. Hence, he must have known that the AAA rating of the Rembrandt 2006-3 CPDO was unjustifiable and unreasonable on at least two bases – use of 15% volatility and the failure to use the actual starting spread.

2.2.8 *ABN Amro's "unexplained error" influences the primary judge's finding*

501. The primary judge took into account as an essential part of her reasons, the fact that ABN Amro made "a fundamental error" about the historical volatility level which it communicated to S&P. Her Honour stated, as part of her reasoning process, that ABN Amro did not explain why that error was made. She explained at J[3148] how, in her view, this error affected S&P's rating of the Rembrandt 2006-3 notes.

502. The primary judge said at J[3148]:

> ABN Amro undoubtedly made a fundamental error about a very important issue which has not been explained and repeated that error to S&P on a number of occasions, no doubt hoping and intending that it would have the desired effect of convincing S&P to reduce its volatility assumption from 35% to 25%. In fact, ABN Amro's assertions, as noted, in one sense worked too well because S&P in fact rated the CPDO AAA on the basis of that belief, using an assumed 15% volatility to satisfy itself that the CPDO

> could be rated AAA. By 12 October 2006 at the latest ABN Amro knew 15% to be wrong and seriously so and ABN Amro also knew, if the error was corrected, it would mean that on S&P's other assumptions the CPDO should not have been rated AAA. Fortunately for ABN Amro S&P was willing not to correct the volatility assumption for ABN Amro CPDO deals in the pipeline of which Rembrandt 2006-3 was one, so it could still be rated AAA. S&P was willing to rate only new CPDOs on the basis of an assumed volatility of 25% as the email exchange between Mr Martorell and Mr Inglis of 10 November 2006, read with Mr Wong's views as communicated to Mr Inglis, discloses.

503. It followed, as the primary judge made clear at J[3149], that ABN Amro knew that S&P's rating could not be safely relied upon because it knew that S&P did not have reasonable grounds for the rating which was not the product of reasonable care and skill on the part of S&P.

2.2.9 *Other reasons why ABN Amro did not have reasonable grounds*

504. Importantly, the primary judge emphasised at J[3150] that there were other facts, apart from the volatility error, which lead to the same conclusion (that is, that there was an absence of reasonable grounds for the AAA rating) for both tranches of the Rembrandt notes. She said at J[3150]:

> [t]hose facts are more diffuse than the simple proposition that S&P rated the CPDO on the basis of an erroneous belief that the average historical volatility of the ... indices was 15% but are nevertheless persuasive of the cases against ABN Amro.

505. The primary judge summarised those additional matters at J[3151]. It is unnecessary to set out that paragraph. It contains findings by the primary judge that ABN Amro knew that S&P had adopted unduly favourable assumptions on critical parameters such as starting spreads and roll-down benefit and that it had not factored in roll costs which were a necessary integer of a proper modelling process.

506. Her Honour went on to say at J[3152]:

> All of these matters of which ABN Amro was or must have been aware it also knew benefited the performance and thus the rating of the CPDO. In these circumstances I do not accept Mr Cole's evidence that ABN Amro only accepted the AAA ratings because it believed there was a reasonable basis for them. That evidence cannot be reconciled with the contemporaneous documents and objective circumstances. I also do not accept Mr Cole's evidence that he considered S&P's base case to involve a stressed but realistic outlook for the CPDO. That too is impossible to reconcile with the contemporaneous documents and objective circumstances. In other words, ABN Amro must have known that S&P's base case was unreasonably and unjustifiably weighted in favour of a positive (that is, AAA) outcome for the CPDO. ABN Amro must have known that the AAA rating (and 0.728% default probability) produced by that case was itself unreasonable and unjustifiable.

507. The primary judge referred at J[3162] to certain other submissions or propositions put by ABN Amro which she said did not affect her conclusion that ABN Amro knew that the AAA rating was flawed. Her Honour's analysis on those submissions included consideration of

emails dated 6 November 2006 from Ms Bosch, referred to at [334] above, and 16 November 2006 from Mr Ding, referred to at [359] above. Her Honour concluded by saying (at J[3162 (3)]):

> Suffice to say that read as a whole these documents tend to support the conclusion that ABN Amro well knew that the Rembrandt CPDOs did not achieve the AAA rating if S&P had used the actual starting spreads as at 5 September 2006, 31 October 2006 or even 18 October 2006 (the latter being the actual date on which Rembrandt 2006-3 was hedged according to ABN Amro).

3. CONSIDERATION OF THE PRIMARY JUDGE'S FINDINGS ON VOLATILITY

508. As can be seen from the above, the primary judge made detailed findings after a long and complex trial. Demonstration of error is not straight-forward in a case such as this: *Branir Pty Ltd v Owston Nominees (No 2) Pty Ltd* (2001) 117 FCR 424 at 435-436 [24] per Allsop J (as his Honour then was) (Drummond and Mansfield JJ agreeing).

509. Here, there are a number of reasons why, in our view, ABN Amro has failed to demonstrate error in the primary judge's findings.

510. First, ABN Amro's attack on the primary judge's detailed findings fails to grapple with the multi-faceted nature of those findings. Those findings were based upon her consideration, not only of the lengthy (but often cryptic) documentary material, but also upon her assessment of the evidence of those witnesses who were called.

511. The essential defect in ABN Amro's attack on the volatility finding is that it is based, almost entirely, upon what was said to be the proper construction of certain emails. The authors and recipients of many of the emails were not called and the primary judge did not accept critical parts of the evidence given by Mr Cole.

512. It is true that the primary judge did not expressly reject Mr Cole as a witness of truth. However, she considered his evidence to be based upon "attempts at reconstruction": J [3110]. Her Honour was critical of certain aspects of Mr Cole's evidence: see, for example, J [3115] and J[3132]. Ultimately, she did not accept Mr Cole's evidence on his essential hypothesis, namely that he did not know that S&P had rated the Rembrandt notes upon an assumed volatility of 15%: J[3137], J[3139] and J[3143].

513. Moreover, an important aspect of her Honour's reasoning was that other ABN Amro personnel, who were involved in critical discussions and communications with S&P about the volatility issue were not called, including in particular, Mr Drexler, Mr Martorell and Mr Whittle: see J[2624], J[3113], J[3115], J[3123] and J[3148].

514. The primary judge did not treat the failure of ABN Amro to call those witnesses as an application of the "rule" in *Jones v Dunkel* (1959) 101 CLR 298. Rather, their absence from the witness box was one of the vicissitudes of litigation which left a gap in ABN Amro's evidence.

515. The gap was an important one because ABN Amro contended that it believed that S&P had applied a 25% volatility parameter. ABN Amro bore the onus of proof but it did not call critical witnesses whose dealings with S&P were central to the question of ABN Amro's state of mind on this issue.

516. The second reason why ABN Amro's attack on the primary judge's findings fails is that her Honour's extensive review of the documentary evidence shows that her findings were supported by contemporaneous documentary records.

517. There are a number of essential steps in her Honour's reasoning process. The starting point is that the Surf CPDO was rated upon an assumption that the volatility parameter was 15%. This was done following the S&P ratings committee meeting of 31 May 2006 as explained by her Honour at J[2638] and J[2639].

518. This finding was amply supported, not merely by emails from ABN Amro employees containing facts asserted by them but by contemporaneous drafts of ABN Amro's written Surf Presentation commencing on 9 June 2006: see J[207]. That document made express reference to S&P's volatility assumption of 15%.

519. Indeed, as the primary judge pointed out at J[2621], ABN Amro changed its description of S&P's base case from 25% volatility to 15% volatility in the 9 June 2006 version of the Surf Presentation.

520. A further draft of the Surf Presentation dated August 2006 continued to refer to S&P's base case assumptions including a volatility parameter of 15%: see J[37] and J[38].

521. Moreover, the primary judge went on to observe at J[2623] that ABN Amro did not change its description of the volatility parameter in the Surf Presentation from 15% to 25% following receipt of Mr Rajan's email of 25 August 2006 "at that or any other time".

522. The next essential step in her Honour's reasons is her observation at J[2641] that Rembrandt 2006-2 was rated on 5 September 2006, that is to say, before the change to the "new" volatility assumption of 25%.

523. The date on which Rembrandt 2006-2 was rated was a matter of documentary record. The primary judge referred to it at J[267]-J[268] and to the email from Mr Ding to ABN Amro dated 5 September 2006 confirming the AAA rating.

524. This amply supported the inference drawn by the primary judge at J[2641] that Rembrandt 2006-2 was rated on a base case assumption of 15% volatility, that is to say, on the same assumption as was made in the Surf CPDO.

525. The primary judge's finding is reinforced by the finding she made at J[576] based upon her assessment of Mr Ding's evidence, and the documentary record, that there was no document recording the results of any modelling runs of the Rembrandt 2006-2 notes when the R-2 Ratings Letter was issued.

526. The final step in the primary judge's reasoning is the finding at J[2642]-J[2643] that Rembrandt 2006-3 was a repeat deal of Rembrandt 2006-2 and, as such, was rated on the basis of an assumed volatility of 15%.

527. There was thus, on her Honour's findings, an erroneous adoption of the 15% volatility parameter, brought about by ABN Amro's intervention in S&P's modelling process. The error was then perpetuated for each of the relevant CPDOs, Surf, Rembrandt 2006-2 and Rembrandt 2006-3.

528. The finding that Rembrandt 2006-3 was a carbon copy of the earlier CPDO, and that it was treated in that way by ABN Amro is supported by the statements made in Mr Lewis' emails of 16 and 17 October 2006 referred to above at [283]-[286]. Indeed, it is reinforced by Mr Cole's evidence: see [400] and [402] above.

529. Although the primary judge found at J[3135] that S&P had informed ABN Amro by 3 October 2006 that it was adopting a "new" volatility assumption of 25%, she explained this quandary at J[2629] by finding that ABN Amro and S&P agreed to a compromise under which the new volatility assumption did not apply to deals in the "pipeline" such as Rembrandt 2006-3.

530. That finding was supported by Mr Wong's email of 27 October 2006 and Mr Martorell's email of 30 October 2006 referred to at [310] and [316] above.

531. The third reason why the attack on the primary judge's finding fails is related to what we have already said about her reliance on contemporaneous records. In particular, not only did her Honour rely on contemporaneous records that supported her findings, but she also dealt with contemporaneous records which may have pointed against them.

532. It was central to ABN Amro's argument on appeal that it believed S&P to be using the 25% volatility parameter from late August 2006.

533. ABN Amro's submission relied in particular on Mr Cole's evidence of his belief and upon Mr Rajan's email of 25 August 2006, referred to at [254] above, a copy of which was sent to Mr Cole, Mr Martorell and Mr Silcox on 28 August 2006: see [256] above.

534. However, the primary judge rejected Mr Cole's evidence as reconstruction: see J [3108]. There is no appealable error in this. Nor is there any error in her Honour's approach to Mr Rajan's email. Her Honour found at J[2623] that the email was wrong and that ABN Amro thought it was wrong at the time because it did not change its marketing presentation to reflect the 25% volatility assumption for which it contends.

535. The primary judge was entitled to treat this as an answer to Mr Cole's "hindsight" evidence as the other recipients of the email were not called.

536. Fourth, a further document upon which the primary judge placed some reliance, as she was entitled to, was Mr Martorell's comparative table dated 2 October 2006. Her Honour observed at J[2628] that this document indicated that as at 2 October 2006 ABN Amro was still informing its clients that S&P had used a volatility parameter of 15%.

537. Fifth, ABN Amro partly accepted the primary judge's finding at J[3135] that S&P told ABN Amro by about 3 October 2006 that it would use 25% as the "new" volatility assumption for future deals. ABN Amro's attack on the finding was limited to its submission that S&P had communicated that information in late August 2006. However, that submission fails for reasons explained above.

538. The primary judge relied upon Mr Martorell's email of 10 November 2006 to support the finding that S&P told ABN Amro on or about 3 October 2006 of the new volatility assumption. ABN Amro did not attack her Honour's use of that email, no doubt because it considered that the email supported, at least in part, its own hypothesis.

539. But it should be noted that the admissibility of this email (and many of the other emails which occupy much of the trial judgment) may have been challenged upon the basis that the maker of the statement did not, and may not reasonably be supposed to have had, knowledge of the asserted fact: see *Evidence Act 1995* (Cth), s 69(2)(a) . However, the admissibility of the email was not put in issue. Rather, the primary judge appears to have determined, as she was entitled to, the weight which should be given to statements made in particular emails.

540. This approach is reflected in the primary judge's consideration of Mr Inglis' statement in his email dated 10 November 2006 that, before "your last two trades" S&P used the 25% volatility parameter. Her Honour relied on this statement at J[2639].

541. There may be some force in ABN Amro's submissions as to the proper inference to be drawn from Mr Inglis' email. However, the short answer to this is that, whatever may be made of the email, it does not negate the primary judge's fundamental hypothesis which is based upon the perpetuation of the "egregious error" in the adoption of the 15% parameter.

542. Sixth, the primary judge addressed the question of the objective probabilities of the case in a way that is immune from attack on appeal.

543. It is true that on one view the objective probabilities suggest that ABN Amro believed that S&P had adopted a 25% volatility parameter. That conclusion might be thought to follow from a central part of the Councils' case, namely that ABN Amro put forward the flawed 15% volatility parameter to persuade S&P to adopt a 25% figure instead of the 35% figure favoured by S&P: see J[2650(1)-(4)], J[3113] and J[3115].

544. But the primary judge recognised the conundrum that the finding that ABN Amro knew that S&P had adopted a 15% volatility assumption meant that its representations had "in one sense worked too well": see J[3148]. She explained her resolution of that issue at J[2615], J[2629] and J[3148].

545. The primary judge's explanation was that S&P made the egregious error of accepting ABN Amro's representations about the historical volatility indices and, when it ultimately discovered the error, S&P was willing to apply the flawed parameter to deals that were in the "pipeline".

546. We are mindful of our obligation to conduct a real review of the trial but, bearing in mind the constraints on the appellate process stated in *Fox v Percy* (2003) 214 CLR 118 at 125-127 [22]-[25] , we do not consider that appealable error is disclosed in her Honour's reasoning on this issue.

547. Seventh, there is a tension between ABN Amro's submission on appeal and the position taken by S&P which does not appeal her Honour's finding that it adopted the 15% parameter.

548. It is true that, at an abstract level, the question of whether ABN Amro knew, or ought to have known, that S&P's opinion was lacking in reasonable grounds, or not the product of due care and skill, is not determined by the finding that S&P's rating was flawed.

549. But the difficulty which arises is that the primary judge found at J[3140] that ABN Amro had closely supervised all aspects of the rating and the rating process by S&P. Counsel for ABN Amro cavilled with the generality of that finding. However, it is sufficient to say that, at least on the volatility assumption, her Honour's conclusion is supported by her findings about the roles of Mr Drexler, Mr Martorell and Mr Whittle in the adoption of the 15% volatility parameter.

550. Two final points should be made in relation to the volatility issue. Both go to the question of the utility of canvassing the morass of evidence that was raised on the issue of whether ABN Amro knew that S&P had adopted the 15% volatility assumption.

551. First, the primary judge found at J[2614] that every one of the independent experts came to the conclusion that the average volatility of the indices was about 28%.

552. Thus, even if we were to find that her Honour erred in failing to accept ABN Amro's submission that it believed S&P to have adopted a 25% volatility assumption, no appealable error is disclosed.

553. ABN Amro sought to overcome this difficulty by contending that the relevant assumption was 25% coupled with rebalancing on the rolls but we have rejected its contention on the rebalancing issue.

554. Senior Counsel for ABN Amro also submitted that the historical volatility of the indices was not a relevant factor because the indices were of short duration. But this overlooks the fact that no real attempt was made to support the 25% figure (even if we were to accept it) as a rational assumption supported by objective evidence.

555. The highest ABN Amro's submission rose on the question of such evidence was Mr Rajan's assertion in his email of 25 August 2006 that S&P did not estimate historical parameters for volatility and that the most useful reference was the JP Morgan index: see J[253].

556. The email cannot be said to prove the validity of a 25% volatility assumption. We were not taken to any evidence to establish the assumptions adopted by JP Morgan or the validity of such assumptions.

557. Second, the inutility of considering the primary judge's finding on the volatility issue is made plain by the fact that her Honour pointed to other reasons why ABN Amro did not have reasonable grounds for its belief that the Rembrandt notes warranted a AAA rating: see J [3150], J[3151], J[3152] and J[3162(3)].

558. As we said above, the primary judge found in the abovementioned paragraphs of her judgment that ABN Amro knew that S&P had adopted unduly favourable assumptions on critical factors in the rating process such as starting spreads and roll-down benefit.

559. Plainly, the issue of the proper assumption for the volatility parameter was not one which was to be considered in isolation. The numerous documents to which the primary judge referred showed that different ratings flowed from different combinations of the relevant parameters.

560. But the primary judge's finding that ABN Amro knew that S&P had adopted unwarranted assumptions about critical parameters such as starting spreads demonstrates that, in the absence of error in her Honour's findings on the other deficiencies, nothing turns upon the correctness of ABN Amro's submission about volatility.

561. ABN Amro pointed to Ms Bosch's email of 6 November 2006 which stated that at 28 bps with a coupon of 200 bps and a leverage multiple of 15, the CPDO was strictly speaking "below the AAA cutoff": see J[333].

562. However, without evidence from Ms Bosch to prove all the relevant parameters of any modelling carried out by her, the email cannot go anywhere towards demonstrating error in the primary judge's finding about the incorrectness of starting spreads.

4. CONCLUSION

563. As the preceding analysis demonstrates, S&P's rating of the Rembrandt notes was unreasonable, unjustified and misleading (and ABN Amro knew that to be so) for reasons which included:

1. The rating adopted a flawed base case volatility parameter of 15%: see [425]-[503] and [508] above; and

2. The rating adopted overly favourable assumptions including in relation to roll-down benefits and starting spreads: see [504]-[507] above.

PART 4 : LGFS' PURCHASE OF REMBRANDT 2006-3 NOTES: S&P

564. LGFS made two groups of claims against S&P. First, a claim in tort that S&P owed LGFS a duty to exercise reasonable care in forming, and to have reasonable grounds for, the opinion expressed by the rating. Next, a series of claims that S&P had engaged in misleading or deceptive conduct in contravention of ss 1041E and 1041H of the *Corporations Act* and s 12DA of the *Australian Securities and Investments Commission Act 2001* (Cth) (the ***ASIC Act***). Each was held by the primary judge to have been established. S&P appealed against each finding.

565. This section of the judgment will consider the claim in tort and then the statutory claims.

1. TORT CLAIMS

1.1. Duty of care owed by S&P to LGFS?: S&P Appeal Grounds Matrix Rows 1A, 1B, 10A, 10B and 12A-12I

566. S&P was found to owe LGFS a duty to exercise reasonable care in forming, and to have reasonable grounds for, the opinion expressed by the rating: J[2993], J[2741]-J[2825] and J[2925]-J[2955], especially at J[2819] and J[2956]. There was no suggestion, and it was not held, that S&P had a duty to be right about the opinion it expressed. The identified duty was

that S&P exercise reasonable care in forming and expressing the relevant opinion about the credit risk of the Rembrandt notes. It failed to do so.

567. S&P appealed against that finding: S&P Appeal Grounds Matrix Rows 1A and 1B. S&P contended (at trial and again on appeal) (S&P Appeal Grounds Matrix Rows 1A, 1B, 10A, 10B, 12F and 12G) that it owed no duty of care to LGFS because:

1. It was not reasonably foreseeable that S&P's conduct would cause loss and damage to LGFS (or the Councils) and the risk of harm was insignificant;

2. The salient features of a duty of care were not present, or not sufficiently present;

3. The special prerequisites for the imposition of a duty of care for negligent misstatement were not satisfied; and

4. It would be incongruous for a duty to exist when it was unlawful for LGFS to deal with, and advise in relation to, the Rembrandt notes: S&P Appeal Grounds Matrix Rows 12A-12I.

568. This section of the judgment will consider the relevant findings of fact, the applicable legal principles and then turn to consider S&P's Appeal Grounds.

1.1.1 Facts

569. The relevant factual findings in respect of S&P are set out at [40]- [58] above.

570. What facts sat on the other side of the ledger? S&P submitted that the following facts were significant. First, S&P had a contractual relationship with ABN Amro to rate the notes. S&P had no relevant relationship (contractual or otherwise) with the claimants (LGFS or the Councils). Second, S&P did not create, market or sell the Rembrandt notes. Third, S&P performed none of the analysis or work in Australia: J[74], J[378] and J [2899]. Fourth, LGFS, a party that did have direct dealings with, and responsibilities to, the Councils, acted unlawfully in contravention of the *Corporations Act* in selling the Rembrandt notes to them: J[2384] and J[2930]-J[2949].

571. Fifth, the nature of S&P's underlying conduct – its publication of credit rating opinions – amounts to a predictive opinion about the future likelihood of repayment by an issuer: J[381], J[2402], J[2503] and J[2531]. S&P emphasised the fact that it has been publishing credit rating opinions for approximately 100 years and currently publishes tens of thousands opinions each year. It offers these opinions to the world by publishing them on its website and through other means: J[383]. So, as S&P submitted, anyone, anywhere, can access S&P's opinion concerning virtually any issuer or security. This formed the basis of S&P's argument that no duty should be imposed upon it because its liability would be too indeterminate.

572. Contrary to the submissions of S&P, this appeal does not raise significant issues of law and policy. In particular, we reject S&P's submission that:

> The effect of the finding at trial, if universally accepted, could be to suggest that in issuing these opinions S&P owes a legally enforceable duty to anyone who might stumble across its ratings on any security and decide to take some action as a result, irrespective of that person's relationship with S&P or his or her awareness of, or adherence to, the limitation inherent in predictive opinions about the future, and irrespective of S&P's awareness of their identity or their vulnerability. In other words, the effect of this would be to turn predictions about the future into guarantees.

That submission ignores established legal principles. This appeal concerns the application of established legal principles to facts which ultimately were not disputed. It is to those principles we now turn.

1.1.2 Applicable legal principles

573. **Following paragraph cited by:**

Davis v Wilson (21 February 2025) (Shariff J)

1575. The Davis Applicants submitted that EY owed a duty of care to the Davis Applicants and to Davis Group Members (including group members who had not already bought shares in Quintis). It was submitted that this proposition was supported by authority in *Esanda Finance* and *ABN AMRO* at [573] ff.

Self Care Corporation Pty Ltd v Green Forest International Pty Ltd (No 2) (12 May 2021) (Baird J)

31. A second category of amendment sought arises by reason of the Applicants' calculation of damages carried out in the Ross Report, relevantly, Mr Ross' calculations of the quantum of the Applicants claim for damages consequent upon the alleged misrepresentation that the Freezeframe products were going to be sold in China, when instead, on the Applicants' case, they were resold into Australia. On Mr Ross' calculations that damages claim greatly exceeds the jurisdictional limits imposed on this Court in respect of recoverability of damages sought under ss 82 and 236 of the *Australian Consumer Law* (**ACL**), Schedule 2 to the *Competition and Consumer Act 2010* (Cth) (**CCAct**), for misleading and deceptive conduct: see ss 86AA and 138A of the CCAct . Whilst the ACL claim is maintained, and the nonpecuniary relief sought pursuant to that claim is important to them, the Applicants say that the claim is essentially a misrepresentation claim, and they propose to plead an action at common law of negligent misrepresentation: as espoused by the Full Federal Court of Australia in *ABN AMRO Bank NV v Bathurst Regional Council* [2014] FCAFC 65, incl. at [573] -[578, [597]-[598], [1106], and see the High Court in *Clayton v Bant* (2020) 385 ALR 41; [2020] HCA 44, [34], [76] .

For the purposes of this appeal, the applicable principles *may* be summarised as follows. First, for there to be a duty to exercise reasonable care in making a statement or giving advice:

1. The speaker must realise, or the circumstances must be such that the speaker ought to have realised, that the recipient of the information or advice intends to act on that information or advice in connexion with some matter of business or serious consequence; and

2. The circumstances must be such that it is reasonable in all the circumstances for the recipient to seek, or to accept, and to rely upon the utterance of the speaker: *Tepko Pty Limited v Water Board* (2001) 206 CLR 1 at 16-17 [47] (Gleeson CJ, Gummow and Hayne JJ) and at 23 [75] (Gaudron J), each adopting in substance Barwick CJ's statement of the principle in *Mutual Life & Citizens' Assurance Co Limited v Evatt* (1968) 122 CLR 556 at 571. See also *San Sebastian Pty Limited v The Minister* (1986) 162 CLR 340 at 372 ; *Esanda Finance Corporation Limited v Peat Marwick Hungerfords* (1997) 188 CLR 241 at 249-250 , 252 (Brennan CJ), 255 (Dawson J), 261, 264 (Toohey and Gaudron JJ) and 272 (McHugh J); *Henderson v Merrett Syndicates Limited* [1995] 2 AC 145 at 180 and the cases referred to by Gummow J in *Esanda Finance* at 301 and 302.

574. In respect of the second limb, the nature of the subject matter, the occasion of the interchange, and the identity and relative position of the parties as regards knowledge (actual or potential) and relevant capacity to form or exercise judgment will all be *included* in the factors which will determine the reasonableness of the acceptance of, and of the reliance by the recipient upon, the words of the speaker: *Tepko* at 16-17 [47] . It is important to recognise that the list is not exhaustive.

575. Second, proof of the criteria at [573] and [574] above establishes an assumption of responsibility or known reliance (or the converse, vulnerability) (*Woolcock Street Investments Pty Limited v CDG Pty Limited* (2004) 216 CLR 515 at 530-531 [23]-[24] (Gleeson CJ, Gummow, Hayne and Heydon JJ), sufficient for a duty to be imposed.

576. Additional, but related, points about the criteria at [573] and [574] should be noted. A duty of care is imposed whether the information or advice is given in response to a request or volunteered: *San Sebastian* at 356-7 ; *Esanda Finance* at 255-6 (Dawson J), 262 and 265 (Toohey and Gaudron JJ) and 309 (Gummow J).

577. Further, a duty is also imposed where the information and advice is communicated to an *identif iable* class of people if the criteria identified in *Tepko* are established: *Esanda Finance* at 252 (Brennan CJ) and 302 (Gummow J) approving *Al Saudi Banque v Clark Pixley* [1990] Ch 313 at 330. It is not necessary that the person making the statement know the identity of the persons who may rely on it and suffer loss: *Kestrel Holdings Pty Limited v APF Properties Pty Limited* (2009) 260 ALR 418 at 435-436 [94] ; *BT Australia Limited v Raine & Horne Pty Limited* [1983] 3 NSWLR 221 at 232 approving *Derring Lane Pty Limited v Fitzgibbon* (2007) 16 VR 563 at 571-572 [41]-[48] ; *Caparo Industries Plc v Dickman* [1990] 2 AC 605 at 638 an d *Hedley Byrne & Co Limited v Heller & Partners Limited* [1964] AC 465 where Lord Oliver noted that the identity of the person to whom the information was to be conveyed was not known by the defendant bank. Next, the fact that the person making the statement or giving

the advice has some special expertise is consistent with (although not always necessary for) the imposition of the duty: *Esanda Finance* at 265 ; *San Sebastian* at 357 and *Henderson* at 180.

578. As LGFS submitted, central to the analysis required by the identified criteria is the purpose for which the statement is made or the advice is given. A recipient of information or advice is owed a duty by the speaker if (a) that recipient is part of a class to whom the statement or advice is directed and (b) reliance on the statement or advice by a member of the class is consistent with the substance of the purpose for which the statement is made or advice given. It was for those reasons that an auditor was held to owe a duty to the company and possibly to its shareholders, but not to a lender: *Esanda Finance* at 257-8 (Dawson J explaining the result in *Caparo* at 638) and at 281, *Shaddock & Associates Pty Limited v Parramatta City Council [No 1]* (1981) 150 CLR 225 at 251 (Mason J) and *San Sebastian* at 357-8 .

1.1.3 Application of principles to facts

579. How then were those principles to be applied to S&P in the circumstances of this appeal? The primary judge held that S&P owed a duty of care to LGFS (and to the Councils): J [2819]. That duty was the duty earlier described – a duty to *exercise reasonable care* in forming, and to have *reasonable grounds for*, the opinion expressed by the rating.

580. Applying the criteria identified (see [573] above), the primary judge held that S&P *knew* that potential investors in the Rembrandt notes would rely on S&P's opinion as to the creditworthiness of the notes in deciding whether to invest in the notes: J[2480] and J[2781]. That finding was not surprising. The factual findings supporting that conclusion include those at [40]- [57] above. Counsel for the PA Councils submitted that the primary judge's findings relevant to the issue of duty could be put in the form of 38 separate paragraphs, which we have distilled into 19 propositions. Whether the PA Councils' summary was in part repetitive or open to criticism in its particular expression may be put to one side. It was established at trial that:

1. S&P published a system of stand-alone ratings where the relevant information for an investor was contained in the rating itself and the accompanying definition S&P assigned to the rating: J[1465(1)] and J[1463(1)];

2. S&P was paid money to assign a rating, "knowing that the only purpose of its rating is to facilitate the marketability of the product": J[2787];

3. S&P knew and expected that potential investors would rely on an S&P rating as the best independent evidence of the risk of loss on an investment, as its business model depended on investors holding that belief: J[2524], J[2529] and J [2777];

4. S&P's business model for rating structured financial products depended on potential investors requiring banks and financial institutions to obtain ratings from internationally recognised credit rating agencies such as S&P: J[2524];

5. Structured finance is its own specialised field of knowledge: J[1414]. S&P held itself out as competent to analyse and rate the CPDO: J[2659];

6. At the time of the rating of the CPDO, S&P had published the meaning of a rating of AAA as indicating S&P's opinion that the "obligor's capacity to meet its financial commitment on the obligation is extremely strong": J[62];

7. ABN Amro paid S&P for rating Rembrandt 2006-3 in circumstances where the sole purpose of the rating was for ABN Amro to communicate the rating to potential investors so that they could take the rating into account in deciding whether or not to, or whether they could, invest. The purpose of ABN Amro obtaining the rating was for dissemination to potential investors so that they could rely on the rating as S&P's expert opinion with respect to the creditworthiness of the CPDO as issued (J[2816]) and / or to take into account the rating in deciding whether to invest: J[2759];

8. S&P knew that the rating would be used by ABN Amro as a marketing tool and that ABN Amro would invite potential investors to rely on the rating as the expert opinion of S&P, a credit ratings agency, of the creditworthiness of the CPDO: J[2793]. S&P knew that its rating was intended to be used for these purposes and it was paid for the assignment of the rating so that ABN Amro could carry out this purpose: J[2759], J[2793] and J[2816];

9. S&P knew the Rembrandt notes were to be issued in tranches of $40 million and $5 million respectively and that investors could only purchase the notes in minimum amounts of $500,000: J[2754];

10. S&P knew the Rembrandt notes were intended to be marketed by ABN Amro in Australia and that ABN Amro intended to communicate the rating of AAA to potential investors: J[222], J[233]-J[235], J[253]-J[254] and J[2754];

11. The AAA rating was assigned three weeks before the Post-Sale Report was issued, and the report merely records the rating and explains why it was assigned. The relevant fact was the rating itself: J[2781];

12. S&P knew that the rating would be highly material to the decision of potential investors in Rembrandt 2006-3 to invest and that is why, in its Ratings Letters (J [2480]), S&P expressly and unconditionally authorised the dissemination of the AAA rating to interested parties. S&P must have known that ABN Amro intended to communicate the rating to potential investors: J[2499], J[2743], J[2793] ("[i] nterested parties", as S&P knew, were potential investors in the CPDO). Indeed, the existence of such potential investors was the reason for S&P being able to earn money by providing ratings services: J[2798];

13. S&P knew that ABN Amro could only communicate the AAA rating to potential investors for as long as S&P chose to maintain the rating. S&P had made it clear to ABN Amro in its R-3 Ratings Letter that it could change or withdraw its rating at any time or withdraw it altogether: J[2754] and J[2787];

14. The terms of the Ratings Letters: see [51], [53] and [54] above;

15. The R-3 Ratings Letter was issued three weeks before the Post-Sale Report. Accordingly, "S&P must have considered it acceptable for interested parties to be informed of its rating, and to use the rating as appropriate as part of the investment decision-making process, on the basis of the 'assigned rating' of AAA alone": J[2523];

16. S&P did not require ABN Amro to provide any particular information to investors when disclosing the rating to investors. It permitted the dissemination of the rating without restriction or limitation: J[2499], J[2523], J[2541] and J[2793];

17. S&P took no step to ensure that a person relying on its rating did so only in the context of whatever report S&P might have published at the same time: J[1465(2)]. S&P had no system in place to ensure that it did not assign a rating unless it had also published an accompanying report: J[1465(3)]. S&P did not refer to its reports in its formal letters assigning ratings: J[1465(4)]. S&P did not take any step to ensure that the person who had obtained the rating ensured that they gave to any prospective investor any S&P report which explained how S&P had reached the rating: J[1465(5)];

18. S&P never expected that investors would all obtain, read and understand its reports and did not believe it was necessary for investors to do so in order to understand S&P's rating: J[1466]-J[1467];

19. S&P must have known that many potential investors, although meeting the definition of wholesale investors, would not have had the in-house expertise to enable them to "second-guess" the rating: J[2773].

581. Second, the primary judge addressed whether it was reasonable for the recipient of S&P's rating to rely upon it. In this context, the relevant recipient was LGFS. The primary judge held that it was reasonable for LGFS (and the Councils) to rely on the rating as S&P's expert opinion on the basis that S&P had reasonable grounds for its opinion and the opinion was the product of reasonable care and skill: J[2481] and J[2517]. Each of the factual findings addressed at [580] is relevant. As LGFS submitted, S&P's business was (and is) to provide independent expert opinions on creditworthiness and it held itself out as doing so, amongst other things, by publicly explaining its ratings: J[34]-J[35]. Indeed, the only available information as to the creditworthiness of the notes was S&P's rating.

582. Third, the primary judge addressed the question of whether the loss was reasonably foreseeable: J[2786]-J[2787] and J[2817]. The primary judge concluded that it was. The factual findings relied upon by her Honour included that:

1. The ratings were of a complex financial product, the issue price of which was $50 million (Rembrandt 2006-2) and $45 million (Rembrandt 2006-3);

2. The product required complex modelling to evaluate the risk of default;

3. S&P knew that ABN Amro intended to communicate the rating to potential investors (S&P authorised that communication) as part of ABN Amro's marketing;

4. The class of potential investors included persons who would or were likely to rely on the rating to assess the creditworthiness of the Rembrandt notes: see [40] -[57] above;

5. All or some members of the class of potential investors could not otherwise assess the creditworthiness of the notes; and

6. Investors who bought the notes would be exposed to loss if the notes were not as creditworthy as S&P represented.

As the primary judge stated, foreseeable loss was the immediate consequence of S&P carelessly rating the notes as the risk of default, and loss on default, was the risk to which the rating was directed: J[2816]. The risk was not insignificant, either in possibility or quantum.

583. One S&P Appeal Ground (S&P Appeal Grounds Matrix Row 1B, referring to Appeal Ground 34(e)) was that the requirements for establishing negligent misstatement set out in *Tepko* were not satisfied. That Appeal Ground is dismissed for the reasons at [569]-[582] above.

584. Against that background, it is necessary to turn to consider S&P's other Appeal Grounds. Each of the matters listed in [567] above will be addressed.

1.1.4 No reasonable foreseeability / risk of harm insignificant?

585. S&P contended at trial and on appeal that the risk of harm was not reasonably foreseeable and / or was insignificant with the consequence that S&P owed no duty of care: see [567] above and S&P Appeal Grounds Matrix Rows 12F and 12G. These Appeal Grounds are rejected.

586. A number of matters were relied upon by S&P. First, S&P's liability was indeterminate and, in particular, S&P did not know the identity of LGFS as a purchaser of the notes: S&P Appeal Grounds Matrix Rows 10A(a) and (d)-(e) and 10B(a) and (d)-(e). Second, LGFS was not vulnerable and, even if it was, S&P was not aware of LGFS' vulnerability: S&P Appeal Grounds Matrix Rows 10A(b), (c) and (e) and 10B(b), (c) and (e). Third, S&P did not control LGFS (it did not have a fiduciary or contractual relationship with LGFS) or have any direct dealings with LGFS (S&P Appeal Grounds Matrix Rows 10A(f)-(h), 10B(f)-(h), 12F and 12G) and, finally, LGFS acted unlawfully in dealing with, and advising in relation to, the Rembrandt notes: S&P Appeal Grounds Matrix Rows 12A, 12B, 12F and 12G. Each will be considered.

1.1.4.1 S&P's liability indeterminate and S&P not know identity of LGFS

587. When S&P published its ratings of the Rembrandt notes, S&P did not know the identity of LGFS. S&P submitted that the fact that S&P did not know of LGFS meant that the primary judge made an error in finding that S&P owed LGFS the duty earlier described. It is necessary to understand the foundation for that submission.

588. S&P submitted that it was a *pre-requisite* for the existence of a duty of care that a reasonable person would have foreseen that its conduct "involved a risk of injury [(1)] to the plaintiff ***or*** [(2)] to a class including the plaintiff" (emphasis added). As support for that general proposition, S&P referred to *Perre v Apand Pty Ltd* (1999) 198 CLR 180 at 220-222 [106] -[108] and 222 [111] ; *Wyong Shire Council v Shirt* (1980) 146 CLR 40 at 47-48 (Mason J,

Stephen and Aickin JJ agreeing); *Bryan v Maloney* (1995) 182 CLR 609 at 618 ; *Esanda Finance* at 289-291, 301-302 and 311 ; *Tame v New South Wales* (2002) 211 CLR 317 at 331 [12] where Gleeson CJ cited *Greenland v Chaplin* (1850) 5 Ex 243 at 248; 155 ER 104 at 106 (Pollock CB) (A person "is not … expected to anticipate and guard against that which no reasonable man would expect to occur") and *Roads and Traffic Authority (NSW) v Refrigerated Roadways Pty Ltd* (2009) 77 NSWLR 360 at 397-398 [178] .

589. **Following paragraph cited by:**

Roo Roofing Pty Ltd v Commonwealth (31 May 2019) (John Dixon J)

654. By contrast with liability in negligence, 'the concept of indeterminacy has no, or no separate, role in cases of negligent misstatement'. [158] Further, 'vulnerability is the consequence of, not an additional criterion of, knowledge (actual or which a reasonable person would have) of reasonable reliance by an ascertainable class of persons.' [159]

via

[159] Ibid 116 [598] .

Roo Roofing Pty Ltd v Commonwealth (31 May 2019) (John Dixon J)

S&P's contention fails on a number of bases. First, S&P misstates what constitutes indeterminacy and the role that concept plays in the proper allocation of risk in negligence claims. Second, the concept of indeterminacy has no, or no separate, role in cases of negligent misstatement or advice. Those ideas are not unrelated. Knowledge of the identity of the person or persons to whom a duty is owed is *not* necessary, or generally of significance, in determining the existence of a duty of care. That statement needs unpacking. Although it is dangerous to seek to pigeon hole a case into a particular category of claim (e.g., *Perre v Apand* at 210 [75]), the claim in tort that LGFS made against S&P was and remains a claim of negligent advice or information. Cases of that kind are not novel. The relevant criteria for cases of that nature are well-established and were most recently described by the High Court in *Tepko* : see [573]-[574] above. Put another way, when dealing with statements and advice, the criteria in *Tepko* are sufficient controls on the imposition of liability to effect an appropriate allocation of risk. Determinacy of class is not a criterion separate from, or in addition to, the criteria identified in *Tepko* .

590. It is therefore necessary to review the authorities cited by S&P in support of its general contention: see [588] above. Each concerned a negligence claim in what has been described as "novel" circumstances. The circumstances here were not novel. Expert information and advice is part and parcel of modern commercial life. The question (or at least one of the questions) that was required to be addressed was, and remains, whether the criteria in *Tepko* co ncerning allegedly negligent information and advice were satisfied. In the present case, they were satisfied: see [580]-[582].

591. That brings us to the third basis for rejecting S&P's general contention that it was a *pre-requisite* for the existence of a duty of care that a reasonable person would have foreseen that its conduct "involved a risk of injury [(1)] *to the plaintiff* **or** [(2)] to *a class including the plaintiff*" (emphasis added). The first limb of that statement finds no support in the authorities. There is no justification for a requirement that before a duty of care arises, the provider of advice or information must know the precise identity of the recipient of the information or advice. As we have noted, expert information and advice is part and parcel of modern commercial life. Often that expert information (as in this case) is by reference to (or in respect of) an instrument, not a particular person's individual position. S&P's business model was structured to exploit that situation. S&P's business included the provision of independent expert opinions on the creditworthiness of "products" and to hold itself out as doing so, amongst other things, by publicly publishing and explaining its ratings: J[34]-J[35]. Indeed, the only available information as to the creditworthiness of the Rembrandt notes was S&P's rating. The risk S&P assumed for reward was liability to those persons who invested in the Rembrandt notes in reliance on the rating and who then suffered loss caused by the fact that the creditworthiness of the notes was much lower than that disclosed by S&P's rating. From an allocation of risk perspective, it cannot be said that the precise identity of the recipient of the expert information was a necessary element. S&P knew the investors (described as "interested parties") existed and authorised the distribution of the rating to them. The criteria in *Tepko* were and are sufficient, without more, to address that aspect of the issue.

592. S&P's oral submissions placed considerable reliance upon McHugh J in *Perre v Apand* at 220-222 [106]-[108] and 222 [111] . None of those passages support S&P's contention. As McHugh J said at 221 [107]:

> Liability is indeterminate only when it cannot be realistically calculated. If both the likely number of claims and the nature of them can be reasonably calculated, it cannot be said that imposing a duty on the defendant will render that person liable ''in an indeterminate amount for an indeterminate time to an indeterminate class''.

593. That therefore brings us to the second limb of S&P's statement that it was a *pre-requisite* for the existence of a duty of care that a reasonable person would have foreseen that its conduct "involved a risk of injury … to *a class including the plaintiff*": see [591] above. That is not a separate criterion to the criteria in *Tepko* . However, even if it was a separate criterion, it was satisfied in the circumstances here. It was satisfied because the principle rises no higher than requiring that the *class* to whom the duty is owed be identified: *Perre v Apand* at 194 [10], 199-200 [32], 202 [42], 218-219 [100], 222 [110]-[111], 303 [336] and 305 [342] . Here, the class was not indeterminate. It was both known and identified. It was possible to identify the class to whom the duty was owed as investors in the Rembrandt notes. This is sufficient. Liability was not indeterminate because S&P did not know the precise identity of the members of the class, the exact number of members in the class or the exact loss. S&P *knew* what it needed to know. It knew the characteristics of the class. S&P knew that a characteristic of the class was that each was an investor in the Rembrandt notes. S&P also knew the foreseeable type of loss. It is the nature of the loss, not the precise amount which is

relevant: *Perre v Apand* at 221-222 [107]-[108] . Here, the nature of the foreseeable loss was not in doubt. S&P knew that if S&P's opinion as to the creditworthiness of the notes was careless, investors were likely to lose the money they had invested in the notes.

594. In the circumstances of the current appeal, not only was the nature of the loss foreseeable but other facts and matters prescribed the parameters of the class and the nature of the loss for S&P: see [580] above. For example, S&P knew the size of the notes issues ([580] above), the level of minimum subscription ([580] above), that the Rembrandt 2006-3 note issue was for a "bespoke investor" (a single subscriber) ([52] above), that investors would rely on S&P's ratings ([57] and [580] above), and the period of potential liability (the 10 year period to the maturity of the notes): see [50] above and J[290] and J[2950].

595. In other words, the class and the foreseeable loss were determined by the function S&P undertook. That function was delineated by the purpose of the rating (the first limb of *Tepko* a ddressed at [573] above) and the known reasonable reliance (the second limb of *Tepko* address ed at [574] above).

1.1.4.2 LGFS was not vulnerable and, even if it was, S&P did not know of its vulnerability

596. S&P contended at trial and on appeal that LGFS was not vulnerable because it was capable of protecting itself from the loss suffered. The primary judge found that LGFS was vulnerable: J [2950]. S&P submitted that finding was in error. Again it is necessary to address the legal and factual foundation for S&P's submission.

597. Legally, S&P submitted that vulnerability was a "prerequisite" for the existence of a duty of care to avoid pure economic loss: *Perre v Apand* at 220 [104], 225 [118] and 228 [125] (McHugh J) and *Caltex Australia Petroleum Pty Ltd v Charben Haulage Pty Ltd* [2005] FCAFC 271 at [273] . Vulnerability was described by S&P as the plaintiff's "inability to protect itself from the consequences of a defendant's want of reasonable care" (citing *Woolcock* at 530-531 [23]) or the plaintiff's inability to protect itself from the risk of injury by reason of ignorance or social, political or economic constraints: citing *Woolcock* at 548-549 [80] . In support of this contention, S&P referred to the statement by McHugh J in *Perre v Apand* that if the plaintiff could have taken steps to protect itself from the defendant's conduct, and was not induced by the defendant's conduct not to take such steps, there is no reason why the law should step in and impose a duty on the defendant to protect the plaintiff from the risk of pure economic loss: *Perre v Apand* at 225 [118] .

598. **Following paragraph cited by:**

Chopsonion Pty Ltd (Controllers Appointed) v Watts Meat Machinery Pty Ltd (No 2) (15 January 2025) (O'Sullivan J)
Minerva (Aust) Pty Ltd v Suburban Land Agency (20 April 2018) (McWilliam AsJ)

S&P's submission fails legally and factually. S&P misstates the relevant legal principles. As Gleeson CJ said in *Perre v Apand* at 194 [10] :

> In relation to the giving of advice or information, questions of reliance and actual foresight of the possibility of harm … are closely related. Moreover, knowledge (actual, or that which a reasonable person would have), of an individual, or an ascertainable class of persons, who is or are reliant, *and therefore vulnerable*, is a significant factor in establishing a duty of care.
>
> (Emphasis added.)

In the field of negligent misstatement, vulnerability is the consequence of, not an additional criterion of, knowledge (actual or which a reasonable person would have) of reasonable reliance by an ascertainable class of persons.

599. In the present case, S&P knew that an ascertainable class of persons (investors in the Rembrandt notes, of which LGFS was a member) would be reliant on S&P's conduct. However, the conduct of S&P was not at large. Its function was to rate the notes and, in particular, a certain aspect of the notes – their creditworthiness: see [40]-[57] above. S&P knew that its function was specialised and that the members of that ascertainable class were likely to rely on S&P carrying out its function. The only available information as to the creditworthiness of the notes was S&P's rating: see [581] above. And, it is important to recall that LGFS could not replicate or "second-guess" S&P's rating: see [39] and [580] above.

600. It was that function – to rate the notes and, in particular, the creditworthiness of the notes – that informed the duty of care owed by S&P to LGFS. S&P's duty was not to protect against any loss suffered by LGFS. Its duty was to exercise reasonable care in forming and expressing the relevant opinion about the credit risk of the Rembrandt notes. It was in that respect, and that respect alone, that S&P owed LGFS a duty of care because S&P knew of an ascertainable class of persons "who is or are reliant, *and therefore vulnerable*". Contrary to S&P's submissions, LGFS was not capable of protecting itself from the loss it suffered and LGFS was induced by S&P's conduct not to take steps to protect itself: *Perre v Apand* at 225 [118] . As we have said, LGFS could not replicate or "second-guess" S&P's rating: see [39] and [580] above.

601. The other factual matters relied upon by S&P do not support S&P's contention that LGFS was not vulnerable. The fact that LGFS held an AFSL and its officers had many years of experience in financial markets with financial products does not detract in any way from the fact that LGFS was a member of an ascertainable class that S&P knew would rely on its rating – the only rating – of the creditworthiness of the notes. In support of its contention that LGFS was not vulnerable, S&P also placed considerable reliance on the proposition that, in connection with its dealing in the Rembrandt notes, it was unlawful for LGFS to purchase and on-sell those notes: J[2947]-J[2949]. That legal issue is addressed in Section 1.1.4.4 below. To the extent that it is accurate, it does not detract from the fact that LGFS was a member of an ascertainable class that S&P knew would rely on its rating – the only rating – of the creditworthiness of the notes. What LGFS did with the notes after purchasing them does not detract from S&P's liability to LGFS.

1.1.4.2.1 Disclaimers

602. Finally, it is necessary to address S&P's contention that even if LGFS was vulnerable (and we consider that it was in the sense described by Gleeson CJ in *Perre v Apand*), her Honour

erred in failing to find that S&P was not aware of any such vulnerability: J[2950]. In support of this contention, S&P submitted that it was entitled to assume that sophisticated investors in complex securities such as the Rembrandt notes would read the disclaimers in the Pre-Sale and Post-Sale Reports, the Ratings Letters and other available documents prior to making the investment. According to S&P, those disclaimers made it plain that if the ratings were relied upon in making an investment, S&P would not be liable for *any* loss or damage suffered. The corollary according to S&P was that, contrary to her Honour's observation at J[2950], S&P would not have anticipated that any purchaser would have relied on the rating in the way that LGFS apparently did.

603. It was not in dispute that a disclaimer can inform the question whether a duty is owed and may negate a duty that would otherwise be owed: *Evatt* at 570 (Barwick CJ); *Hedley Byrne* at 492-493 (Lord Reid) and 504 (Lord Morris) and *Derring Lane* at 570 [36]-[38] (Ashley JA, Buchanan JA and Kellam AJA agreeing). However, in the circumstances of this case, S&P's contention based on the disclaimers fails.

604. LGFS read the Pre-Sale Report and the Ratings Letters (see [72], [77] and [92] above) before deciding to buy the notes. It is therefore necessary to turn to consider the disclaimers in those documents. The disclaimers in the Pre-Sale Report are set out at [49] above. The disclaimers in the Ratings Letters are set out at [51] above. We will deal with each in turn.

1.1.4.2.2 Pre-Sale Report

605. The disclaimer in the Pre-Sale Report (the **R-2 Disclaimer**) relevantly read:

> Information has been obtained by [S&P] from sources believed to be reliable. However, because of the possibility of human or mechanical error by our sources, [S&P] or others, [S&P] does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or the result obtained from the use of such information. Ratings are statements of opinion, not statements of fact or recommendations to buy, hold, or sell any securities.
> …
> Ratings are statements of opinion, not statements of fact or recommendations to buy, hold, or sell any securities. Ratings are based on information received by Ratings Services …

606. The disclaimer identifies three sources or types of information – (1) information and "results obtained" from that information, (2) "*statements of fact or recommendations to buy, hold, or sell any securities*" and (3) the ratings. As LGFS submitted, the first two sentences of the disclaimer address the first source or type of information, being the information provided by external sources. It is unsurprising that S&P would disclaim liability for that information, or the results it obtained from that information. However, it should be noted that the disclaimer records that S&P has obtained that information from sources believed to be reliable. That qualification to the disclaimer is not unimportant. By the qualification, S&P records that it exercises discretion in the information it relies upon in rating the identified instrument or product. It only uses information it believes comes from reliable sources.

607. The second and third sources or types of information referred to in the disclaimer are related. The disclaimer recognises that there is a distinction to be drawn between the rating (as a statement of opinion) on the one hand and a statement of fact or recommendation to buy,

hold or sell securities on the other. It is evident that the disclaimer in the Pre-Sale Report does not, and does not seek to, limit or exclude S&P's liability for the rating as a statement of its opinion. Put another way, the careless opinions and representations in S&P's rating of the Rembrandt notes was the "result" of S&P's conduct in forming the opinion, not from any source of information it received. S&P's conduct was that the volatility assumption it used as an input in modelling the creditworthiness of the notes was based on a misstatement about historical volatility when it in fact had the correct volatility data but did not use it. S&P did not challenge that finding on appeal. S&P's negligence was in making an assumption about volatility which was unjustified based on the facts known to S&P: see Part 3 above. That conduct, as well as the formation and communication of the rating by S&P, was not addressed in or the subject of the disclaimer.

608. As LGFS submitted, the disclaimer was unilaterally framed and inserted by S&P. If S&P intended to disclaim responsibility for the purpose for which the rating was obtained, it was required to say so in clear words: *BT Australia* at 236-7 . The applicable principles are well-established. Proper notice of a disclaimer is required (*National Exchange Pty Limited v Australian Securities and Investments Commission* (2004) 49 ACSR 369 at 381-382 [51]-[58]) and unless it is in unambiguous language and prominently displayed, it will not be effective. In the Pre-Sale Report, the disclaimer was published at the end of a report which otherwise describes S&P's reasoning for the rating and which was to the effect that the rating was reliable and did not seek to disclaim any liability for S&P's negligence in providing the rating.

609. In this context, it is necessary to address S&P's contention that a reasonable person would have understood the R-2 Disclaimer to mean, *inter alia*, that ratings are not statements of fact and therefore they cannot be relied upon as giving rise to any implied representations. In particular, S&P submitted that "the R-2 Disclaimer makes it clear to a reasonable person that the rating cannot be relied upon as giving rise to a statement, and if it is so-relied upon there can be no recourse to S&P in respect of any loss suffered". S&P's position was that although it accepted that the Pre and Post-Sale Reports (and the Ratings Letters) as a whole may be conveyed to potential investors, and that potential investors may act upon that information, the disclaimers made it clear that if they do so it is at their own risk. We reject that contention. The Pre-Sale Report must be read as a whole. It identified the basis for S&P's opinion and explained the reasoning for S&P's opinion. Unsurprisingly, the disclaimer stated that the rating was an expression of opinion as to risk, not a warranty or investment advice. The disclaimer was not directed to, and objectively would not be understood to be directed to, the representation necessarily conveyed by the statement of opinion – that S&P had reasonable grounds for the opinion or exercised reasonable care and skill in forming the opinion.

610. In any event, the R-2 Disclaimer was arguably replaced by two subsequent documents – the Ratings Letters. Those letters were the formal communication of the rating. The Pre-Sale Report contained only a "preliminary rating" of each issue of notes. Any limitation in the Pre-Sale Report was overtaken by the communication of the rating assigned in the Ratings Letter, and the terms of those letters. It is to the Ratings Letters we now turn.

1.1.4.2.3 Ratings Letters

611. LGFS received the R-2 Ratings Letter before committing StateCover to subscribe for the Rembrandt 2006-2 notes and received the R-3 Ratings Letter before subscribing for the Rembrandt 2006-3 notes: see [77] and [92] above.

612. Each Ratings Letter set out the rating assigned by S&P. Each contained a disclaimer in the terms set out at [51] above. Again, a careful reader of the disclaimer will notice that each Ratings Letter identifies what it is *not*. It is not "investment, financial, or other advice" and it went on to state that "you should not read and cannot rely upon the rating as such": J[318].

613. The rating was not advice. It was an expert opinion as to the creditworthiness or the credit risk of the Rembrandt notes. The words set out at [51] above are not a disclaimer to the effect that S&P accepts no responsibility for the function or task it was engaged to perform and that is not surprising. A disclaimer in those terms would render the rating devoid of content or meaning and, as the primary judge accepted at J[2525], would have rendered the rating content-less, futile and self-defeating.

1.1.4.3 S&P did not have direct dealings with or control LGFS

614. S&P had no contractual relationship with LGFS. S&P had a contractual relationship with ABN Amro. In evidence were two relevant pieces of correspondence – the Ratings Letters (at [51] and [53] above). The terms of those letters are relevant and significant.

615. As LGFS accepted, a contract purporting to exclude liability to non-parties to that contract may negate a duty to those non-parties: *The Owners – Strata Plan 61288 v Brookfield Australia Investments Limited* [2013] NSWCA 317 at [136]-[138] . The contract between S&P and ABN Amro (the Ratings Letters at [51] and [53] above) contained terms which identified the scope of S&P's responsibility. The letters identified that S&P's responsibility extended to non-parties. So, for example, the Ratings Letters identified the ratings as "public ratings" and stated that they did not create a fiduciary relationship between S&P and "other recipients of the rating". Next, each Ratings Letter stated that it constituted S&P's permission for ABN Amro to disseminate the rating to "interested parties" and, finally, S&P reserved the right to inform its own clients, subscribers and the public of the rating. As is self-evident, the Ratings Letters did not negate a duty being owed by S&P to the non-parties.

616. Next, it is necessary to address S&P's submission that the absence of a direct dealing between S&P and LGFS precludes a duty being owed by S&P to a non-party such as LGFS. That submission is rejected. It is inconsistent with:

1. The principles of determinacy that a duty can be owed to a class: see [591]-[595] above. As the single subscriber for Rembrandt 2006-3, LGFS was within the class of "interested parties" referred to in the Ratings Letters;

2. The authorities which have held a duty to be owed even where there has been no direct relationship between the person who owed the duty and the person to whom the duty was owed: *Caltex Oil (Australia) Pty Ltd v The Dredge "Willemstad"* (1976) 136 CLR 529 at 573-574 ; *Hedley Byrne* ; *Henderson* ; *Aiken*

v Stewart Wrightson Members Agency Limited [1995] 1 WLR 1281; *Kestrel Holdings* ; *Dartberg Pty Ltd v Wealthcare Financial Planning Pty Ltd* (2007) 164 FCR 450 and *BT Australia* ; and

3. What the primary judge described as the "real nature" of the transaction between S&P and ABN Amro: J[2780]. ABN Amro engaged S&P to provide the rating and paid S&P for it. But that statement is incomplete. It does not address the purpose of the rating, why S&P authorised the distribution of the rating or why S&P published the Pre-Sale Report and the Post-Sale Report: see [40]-[57] above. S&P knew that ABN Amro obtained and paid for the rating for the sole purpose of communicating the rating to "interested parties" so that those parties could consider the rating in deciding whether to invest in the notes: J[2759] and J [2775].

1.1.4.4 LGFS contravened s 912A of the *Corporations Act* ?: S&P Appeal Grounds Matrix Rows 12A-12E

1.1.4.4.1 Introduction

617. Section 912A(1) of the *Corporations Act* provides that a holder of an AFSL (such as LGFS) must:

(a) do all things necessary to ensure that the financial services covered by the licence are provided efficiently, honestly and fairly; and

(aa) have in place adequate arrangements for the management of conflicts of interest that may arise wholly, or partially, in relation to activities undertaken by the licensee or a representative of the licensee in the provision of financial services as part of the financial services business of the licensee or the representative; and

(b) comply with the conditions on the licence; and

(c) comply with the financial services laws; and

…

(e) maintain the competence to provide those financial services; and

…

Failure to comply with any of these requirements is an offence under s 1311(1) of the *Corpora tions Act* .

618. Both of LGFS' AFSLs authorised LGFS to give advice in relation to, and to sell, "securities": see [30]-[31] above. "Securities" includes "debentures": *Corporations Act* s 76 1A .

619. LGFS submitted that the notes were debentures and it was authorised to sell or advise in relation to "debentures". LGFS accepts that if the notes are not "debentures" then it was not authorised to sell or advise in relation to the notes because, if not "debentures", the notes are not otherwise "securities". A security is not a derivative: s 761D(3)(c) and s 764A(1)(a)) .

620. The primary question is whether the notes were debentures and therefore securities. "Debenture" was defined in s 9 of the *Corporations Act* (in the terms then in force), relevantly as follows:

> "**debenture**" of a body means a chose in action that includes an undertaking by the body to repay as a debt money deposited with or lent to the body. The chose in action may (but need not) include a charge over property of the body to secure repayment of the money. However, a debenture does not include:
>
> (a) an undertaking to repay money deposited with or lent to the body by a person if:
>
> (i) the person deposits or lends the money in the ordinary course of a business carried on by the person; and
>
> (ii) the body receives the money in the ordinary course of carrying on a business that neither comprises nor forms part of a business of borrowing money and providing finance;

621. It is accepted that, as found by the primary judge, the notes are choses in action satisfying that part of the definition: J[2368]. However, the primary judge held that the notes were not a "debenture" for two reasons. First, the chose does not "include an undertaking by the body to repay as a debt money deposited with or lent to the body": J[2374]-J[2377]. Second, para (a)(ii) of the exception to the definition operated because the body which received the money did not receive the money as "part of a business of … providing finance": J[2382]-J[2383].

622. LGFS submits that both those conclusions are wrong and that the notes created a debt and Perpetual Trustee Company Limited (**Perpetual**) received the loan as part of its business of providing finance.

623. This section of the judgment will consider (1) whether the notes were a "debenture" and (2) if not a debenture (and they are not), the legal consequences of LGFS selling and advising in relation to the notes in contravention of its AFSLs and s 912A of the *Corporations Act* .

1.1.4.4.2 Relevant Facts

624. Each of the Rembrandt Trusts was created pursuant to a Master Trust Deed, which contained the standard terms of the trusts: cl 2.1. Pursuant to the terms of the Master Trust Deed, Perpetual held the assets of the relevant Rembrandt Trust, here the rights under the swap with ABN Amro and payments received from ABN Amro, on trust: cl 2.4. Perpetual's liability as trustee was limited to those assets: cl 5.4. The obligation owed by Perpetual to note holders

corresponded to the power granted to Perpetual to borrow money by the issue of "Notes" when directed by ABN Amro: cl 5.1, cl 8. By cl 5.6 (albeit subject to the other instruments) a Bearer Note or entry in the Register of Holders relating to a note constituted an acknowledgement by Perpetual of its indebtedness to the note holder in relation to the note.

625. Perpetual as trustee was granted the power to borrow money and enter debt instruments: cl l11.1(c) and (d). The Master Trust Deed incorporated the Rembrandt Trust Master Definition Schedule: cl 1.1 of the Master Trust Deed. Clauses 4.7 and 4.8 of the Master Definition Schedule restate that those obligations are limited recourse obligations.

626. LGFS then submits that a consequence of the grant of power to Perpetual by cl 5.1, only referable to debt instruments, is that, on the construction by the primary judge, the issue of the Rembrandt notes is likely beyond power which was not the objective intention of the parties. LGFS contends that while unintended consequences due to the parties misconceiving the juridical character of the structure adopted are possible, the Court should prefer a construction which gives effect to the transaction objectively intended which is a good reason to construe the Rembrandt notes as creating a debt, consistent with the language the parties and their solicitors used.

627. The Rembrandt 2 and Rembrandt 3 trusts were created by notices dated 18 February 2004. We will consider, for illustrative purpose, the Rembrandt 2006-3 notes.

628. The Issue Notice for the Rembrandt 3 trust contained the terms of the Rembrandt 2006-3 notes. The introductory words of the Issue Notice described the notes as "secured limited recourse debt obligations". Clause 2.1 describes the notes as having those same characteristics, that is, secured limited recourse debt obligations, in accordance with cl 7.2 of the Master Trust Deed. By cl 2.3 of the Issue Notice, except in the case of Bearer Notes entries in the Register of Holders constituted the record of Perpetual's "indebtedness". The notes ranked *pari passu*, a concept familiar to the ranking of debts: see cl 2.4, also cll 6.1(e) and 6.2(e).

629. Clause 5.1 imposed an obligation on Perpetual to pay the "Coupon Amounts" (the quarterly interest payments), subject to the contingency of neither an "Early Redemption Event" nor a "Strategy Unwind Event" having occurred. By cl 7 (particularly cll 7.3 and 7.5), in the event of an "Early Redemption Event" or a "Strategy Unwind Event" Perpetual was required to redeem the notes, in an amount equal to the remaining assets of the trust, distributed *pari passu* . LGFS submits that this contingency and related obligation gave effect to the notes being limited recourse instruments.

630. Subject to such an Event, on the Maturity Date, Perpetual was required to redeem the notes by paying to the note holders the "Redemption Amount". The primary judge characterised cl 9 as a "key provision" and one which was critical to her conclusion that the notes did not create a debt: J[2370]-J[2371]. Clause 9 was follows:

> **9 Maturity**
>
> As long as no Early Redemption Event or Strategy Unwind Event has occurred, the Trustee will (at the direction of the Trust Manager) redeem the Notes on the Maturity Date by payment to the Holders (pro rata to their respective entitlements to the Notes) of an amount equal to the Redemption Amount.

631. The Redemption Amount did not mean the Principal Sum of $40 million. Rather, it was defined in cl 1.7 to mean the lesser of the Principal Sum outstanding, called the Scheduled Redemption Amount, and the Cash Deposit Value.

632. The effect of the definition of “Cash Deposit Value”, when read with the provisions of cll 7.3, 7.5 and cl 20, was that in the event of an Early Redemption Event or a Strategy Unwind Event, the amount payable to LGFS was less than the sum of $40 million, and may be zero.

633. LGFS contends that cll 7 and 9 gave effect to the limited recourse character of the debt, but did not otherwise change the character of the obligation. AHAC challenges this construction. AHAC’s submissions, to the effect that the Notes did not create an obligation in the nature of a limited recourse debt, focus on the fact that, properly characterised, the obligation which Perpetual had to the note holders was not one to repay them the Principal Amount but, rather, to pay on the maturity date, or such earlier date as may arise, through a cash-out event, a sum of money “which may or may not be the sum lent or deposited” calculated in accordance with the terms of the issue notice. AHAC observes, correctly, that the amount to be redeemed, which cannot be less than zero, or more than the amount paid as principal, may be anywhere in between, depending on the performance of the trading strategy embodied by the CPDO itself.

634. Accordingly AHAC submits that the primary judge was correct in concluding at J[2376] that the notes do not include an undertaking to repay as a debt money deposited with or lent to Perpetual because there is no debt, contingent or otherwise embodied by the notes, and for this reason the notes were not debentures within the meaning of s 9 of the *Corporations Act* .

635. Reference should also be made to a number of other provisions. One of them is cl 14 of the Issue Notice.

636. Clause 14 of the Issue Notice limited the liability of Perpetual. Clause 14.5 is declaratory of the effect of the Master Trust Deed. The effect of that deed is that Perpetual as trustee was liable for the debts of the trust (Master Trust Deed cll 5.4, 5.6) but, subject to limited exceptions, not otherwise (Master Trust Deed cl 11). Clause 14.5 of the Issue Notice, read with the Master Trust Deed, limited proceedings against Perpetual to the value of the assets held as trustee.

637. Clause 20 of the Issue Notice dealt with the Index Portfolio which comprised Notional Credit Default Swaps with a Notional Counterparty under which Perpetual was deemed to sell credit protection to the Notional Counterparty: see cl 20.1.

638. The Notional Credit Default Swaps were to be made in respect of the reference indices consisting of the five year iTraxx Europe Index and the five year DJ CDX Index series referred to in cl 20.1(i) and (ii).

639. The notional credit default swaps referred to in cl 20 are separate from the credit default swap described as a Derivative Contract in item 11 of the reference schedule on the first page of the Issue Notice. The Derivative Contract was an actual credit default swap between Perpetual and ABN Amro, the terms of which were set out in Schedule 2 to the Issue Notice.

640. The Derivative Contract between ABN Amro and Perpetual provided for a swap arrangement between those parties in relation to the $40 million of notes which were the subject of the Issue Notice. Importantly, this was an actual credit swap. It provided for payment by Perpetual to ABN Amro of the $40 million comprising the issuance proceeds of the notes. That payment was to be made on 2 November 2006 which was the Issue Date described in item 4 of the reference schedule to the Issue Notice and the "Effective Date" described in the General Terms of the swap between Perpetual and ABN Amro.

641. The General Terms went on to set out what amounted to a back-to-back loan arrangement between Perpetual and ABN Amro in respect of the subscription sum of $40 million received from LGFS for the notes. ABN Amro's obligations to Perpetual in terms of both the dates and amounts to be paid for interest and principal corresponded precisely with Perpetual's obligations to LGFS to pay the Coupon Amount and the Redemption Amount in respect of the notes.

1.1.4.4.3 The statutory definition of a debenture

642. **Following paragraph cited by:**

> Australian Securities and Investments Commission v M101 Nominees Pty Ltd (in liq) (No 8) (09 July 2025) (Button J)
>
> 364. At the outset of its analysis of the statutory definition of debenture, the Full Court in *ABN AMRO* observed that the statutory definition "departs in a number of respects from the common law meaning and from earlier statutory definitions": at [642] (Jacobson, Gilmour and Gordon JJ) . The Full Court went on to identify two of those departures from the earlier common law: at [645]–[647].

The definition of a debenture in s 9 of the *Corporations Act* departs in a number of respects from the common law meaning and from earlier statutory definitions. The new definition was introduced by amendments which became effective on 13 March 2000: see Ford HAJ, Austin RP and Ramsay IM, *Ford's Principles of Corporations Law* (LexisNexis, subscription service) at [19.070] (service 86).

643. Under the former definition a debenture was a document issued by a corporation that created or acknowledged a debt: *Explanatory Memorandum to the Corporate Law Economic Reform Program Bill 1998* (Cth) at 72. This followed the common law which grappled with difficulties in defining the precise nature of the term but accepted that the two essential characteristics of a debenture were:

> "... first that it is issued by a company and, secondly, that it acknowledges or creates a debt": *Handevel Pty Ltd v Comptroller of Stamps (Vic)* (1988) 157 CLR 177 at 195.

644. The amendments to the definition were intended to facilitate electronic commerce in debentures by focussing on the legal right to repayment of the debt rather than the piece of paper which evidenced it: *Explanatory Memorandum* at 72.

645. Thus, the amended definition departs from the earlier law in two respects. First, a debenture is defined as a chose in action rather that a document. This departure may be more of form than substance because a debenture has always been understood as constituting a chose in action: see for example, Gower LCB, *Modern Company Law* (2nd ed, Stevens and Sons Limited, 1957) p 385.

646. The second departure from the earlier definition is that the chose in action must include an undertaking by the body which issues the debenture to "repay as a debt" money that has been deposited with or lent to it.

647. The definition goes on to say that the chose in action may (but need not) include a security interest over property of the body to secure repayment of the money. This corresponds with the common law nature of a debenture under which the document generally, but not necessarily, contained a charge on the undertaking of the company to support its indebtedness: *Lemon v Austin Friars Investment Trust* [1926] 1 Ch 1 at 15 (Pollock MR).

648. The description of these essential characteristics of a debenture is contained in the chapeau to the definition in s 9. The chapeau is followed by a number of exclusions to which we will refer later.

649. **Following paragraph cited by:**

Application by New South Wales Minerals Council (No 4) (18 November 2021) (JUSTICE O'BRYAN (DEPUTY PRESIDENT) ; DR D ABRAHAM â€¦)

Financial Services Council Ltd v Industry Super Australia Pty Limited (25 July 2014) (Gilmour, Flick & Perram JJ)

34. In those circumstances, the Court sees no reason not to give effect to its conclusion that s 622(3) must be construed conformably with the compositional requirements of s 620(1A) . Whilst the applicant submitted that the two provisions were directly inconsistent and that the Court should give primacy to the latter over the former (citing *Project Blue Sky Inc v Australian Broadcasting Authority* (1998) 194 CLR 355) the Court does not share that view. Although in practical terms the result is no different, the Court accepts the submission of the Minister that the provisions are not directly inconsistent and that what is involved is rather the process of construing them in an harmonious fashion. In this case, that requires one to read s 622(3) as not extending to empower the President to appoint a fresh member to fill a casual vacancy in a way which is inconsistent with s 620(1A) . To reach this conclusion it is merely necessary to read the expression 'FWC Member' not in accordance with the dictionary definition in s 12 (i.e., all members of the Commission

regardless of class) but instead only as 'eligible FWC Member'. Although s 12 is not expressed to provide that the definitions which it contains apply unless the context otherwise requires that is, in fact, how s 12 is to be read: see *Knightsbridge Estates Trust Ltd v Byrne* [1940] AC 613 at 621 ; *Transport Accident Commission v Treloar* [1992] 1 VR 447 at 449-450 (FC); *Kelly v The Queen* (2004) 218 CLR 216 at 245 [84] and 253 [103] per McHugh J; *Anti-Doping Rule Violation Panel v XZTT* (2013) 214 FCR 40 at 62-63 [89]-[91] and most recently *ABN Amro Bank NV v Bathurst Regional Council* [2014] FCAFC 65 at [649] .

Whilst the chapeau purports to contain an exclusive definition of a debenture, it must be borne in mind that the function of a statutory definition is to act as an aid to construction of the statute. It is to be read as part of the fabric of the statute and is not to be given a narrow, literal meaning and then used to negate the purpose or policy of the substantive enactment: *Kelly v R* (2004) 218 CLR 216 at [84] and [103] (McHugh J).

650. It follows that the proper approach to the construction of the definition of a debenture in s 9 is to consider its meaning in light of the regulatory focus of the *Corporations Act* , in particular in Chs 2L and 6D. Those chapters of the *Corporations Act* recognise that the nature of a debenture is, as it always has been, inextricably bound up with its function as an important aspect of corporate fundraising.

1.1.4.4.4 The relevant provisions of the Corporations Act

651. The regulatory provisions of the *Corporations Act* are directed at the protection of investors who are invited to subscribe for or buy securities. There are a number of separate definitions of securities in the *Corporations Act* , each of which includes debentures.

652. Section 92(1) contains a general definition of securities but s 92(3) contains a separate definition which applies for the purposes of Chs 6 to 6CA.

653. However, neither of these definitions applies for the purpose of Ch 6D because s 700(1) provides that in Ch 6D "securities" has the same meaning as in Ch 7.

654. The relevant definition for the regulatory provisions of Ch 6D is therefore the definition of security in s 761A . It provides, relevantly, in sub-para (b) that a security means "a debenture of a body".

655. A debenture under this definition does not include an "excluded security" but the definition of that term in s 9 does not extend to a derivative.

656. Derivatives are a "financial product" for the purposes of Ch 7 of the *Corporations Act* and the issue and acquisition of such products is regulated by that Chapter. The existing Ch 7 was introduced by the *Financial Services Reform Act 2001* (Cth) . It covers a much broader range of financial products and financial services than the previous provisions of Chs 7 and 8: see *Ford's Principles of Corporations Law* at [22.090].

657. Chapter 7 contains a definition of derivative in s 761D(1) . The primary judge found at J [2367] that the notes were a derivative within the terms of that definition. That finding was not in issue on the appeal. However, as the primary judge went on to observe, it is necessary to refer to the exclusions from the definition in s 761D(3) which determines the scope of the operation of Ch 7 so as to exclude instruments that are both derivatives and debentures.

658. The effect of s 761D(3)(c) when read with s 764A(1)(a) and (c) is that a financial product which is a derivative is not treated as a derivative for the purposes of Ch 7 if it also amounts to a debenture. Her Honour referred to this at J[2367]. The regulatory régime, including its disclosure requirements, in Ch 6D therefore applies to hybrid securities which have the characteristics of both a debenture and a derivative: see the explanation given in Donnan J, "Debentures, Derivatives and Managed Investment Schemes – the Characterisation and Regulation of Investment Instruments" (2002) 13 *Journal of Banking and Finance Law and Practice* 28-35 at 35.

659. Other relevant provisions of the *Corporations Act* which deal with the issue of debentures are ss 124, 168 and 171.

660. Section 124(1)(b) provides that a company has power to issue debentures that are redeemable only upon a contingency. Sections 168 and 171 provide that if a company issues debentures it must maintain a register of debenture holders.

1.1.4.4.5 Discussion

661. The question which arises involves the application of the statutory definition of a debenture, considered in its proper context, to a highly complex financial product.

662. The statutory definition is to be considered in light of the legislative history of the nature of a debenture and its function as an element of corporate fundraising.

663. The term "debenture" has a long history. It derives from the Latin word "debentur" and has been in use for many centuries to mean an acknowledgment of a debt: *Palmer's Company Precedents* (15th ed, Stevens and Sons Limited, 1938) Part III, p 1; Wallace G and Young J, *A ustralian Company Law and Practice* (The Law Book Company Ltd, 1965) p 265.

664. The issue of debentures by companies as a means of capital raising grew to prominence in England from about the time of enactment of the *Companies Act 1862* (UK). Notwithstanding the difficulties expressed by eminent English judges in the 19th Century in stating a precise legal definition, the earlier authorities accepted that the essential features were, as we have said, a document issued by a company that evidences or acknowledges a debt: *Levy v Abercorris Slate and Slab Co* (1887) 37 Ch D 260 at 264.

665. However, there were a number of other characteristics commonly, but not always, found in the earlier forms of debenture. The learned authors of the 15th ed of *Palmer* listed nine such features at pages 3-4.

666. On the other hand, as Mason, Wilson, Deane and Dawson JJ observed in *Handevel* at 196, not every document creating or acknowledging a debt of a company constituted a debenture. They

went on to say that "commercial men and lawyers" would not use the term when referring to negotiable instruments, deeds of covenant and many other documents in which a company agreed to pay a sum of money.

667. It was accepted at common law that a certificate issued by a company that contained an acknowledgment of a debt payable in the future upon a contingency fulfilled the primary conditions for a debenture: *Lemon v Austin Friars*.

668. In that case, the contingency was that the debt was only payable out of profits earned by the company. The document contained special provisions as to the funds out of which the indebtedness was to be satisfied, but that did not detract from its characterisation as a debenture: *Lemon v Austin Friars* at 15, 17 and 19.

669. The reasoning which underlies *Lemon v Austin Friars* appears to be reflected in s 124(1)(b) of the *Corporations Act* . But what is not clear from that subsection is whether the contingency upon which the creditor's rights of redemption are conditioned is a contingency that relates to the conduct of the company's business or to a contingency that is independent of the affairs of the company. What constitutes a contingency is sometimes easier to recognise than define: see the authorities cited by Campbell JA in *BE Australia WD Pty Ltd v Sutton* (2011) 82 NSWLR 336 at 352-353 [72] .

670. In *Lemon v Austin Friars* the contingency was that there be profits earned by the company out of which the principal sum was repayable. That was consistent with the purpose for which the subscription moneys were raised, namely for the purpose of carrying on the undertaking of the company. Subject to the contingency that the company earned profits from its undertaking, a fund comprising 75% of the profits was earmarked for payment of the principal sum due to the creditor. If there were no profits from the undertaking there would be no funds available to repay the principal and the creditor took the risk of any shortfall.

671. In the present case, the noteholders' right to redemption, and the sum which was payable, was not linked to the conduct of the business of either ABN Amro or Perpetual. Rather the amount payable to the noteholders as the Redemption amount was linked to the performance of certain credit indices against which the value of the investment and the amount that was payable upon redemption was to be measured. Moreover, the contingency which determined the amount due to noteholders could arise prior to the maturity date. This was because an early repayment could be triggered at a fraction of the principal sum (or even zero) if an Early Redemption Event were to occur. The note was a financial product within the meaning of s 763A of the *Corporations Act* but that does not answer the question of whether it was a debenture.

672. The Rembrandt notes are analogous to, but more complex than, another form of investment which now appears to be commonly available in the financial community. In those instruments moneys received from investors are invested in a fund, or a variety of funds, and the amount repayable to the instrument holders is determined by reference to the performance of the fund: *Donnan* at 29.

673. The question which then arises is whether an obligation to redeem the Rembrandt notes at a time, or in an amount, contingent upon the notional returns generated by the performance of the underlying credit indices in which subscription moneys are notionally invested, is a debenture in accordance with the statutory definition in s 9. That is to say, does an instrument

which provides for a return of the amount deposited, at a time and in an amount, not linked to the conduct of the business of the company which issued it but instead measured by the performance of a separate index, fall within the meaning of a debenture?

674. In our opinion it does not, at least in relation to the Rembrandt notes. There are a number of reasons for this.

675. **Following paragraph cited by:**

Australian Securities and Investments Commission v Wallet Ventures Pty Ltd (24 July 2025) (Stewart, Cheeseman and Meagher JJ)

24. The appellant puts its grounds of appeal as follows:

Deposit of money or loan

1. The primary judge erred in holding that the Finder Earn product was not a debenture as defined by s 9 of the Corporations Act 2001 (Cth) (Act) because there was not a deposit of moneys or a loan to the Respondent when an investor used the Finder Earn product (at J[94]-[95]). Her Honour ought to have held that there was a loan or deposit [sic]:

a. on the proper construction of the Terms (as defined in the Judgment), the investor lent money to or deposited money with the Respondent on using the Finder Earn product and entering into a single arrangement to acquire TAUD and transfer and allocate that TAUD to the Respondent; or in the alternative,

b. by s 761B of the Act and because it is reasonable to assume that the parties to the Finder Earn product regarded the arrangements as constituting a single arrangement, the acquisition of TAUD and transfer of that TAUD to the Respondent were to be treated as if they together constituted a single arrangement for the purpose of determining whether the Finder Earn product was a debenture.

Undertaking to repay moneys "deposited or lent" as a debt

2. The primary judge erred in holding that the Finder Earn product was not a debenture as defined in the Act because there was no undertaking by Finder Wallet to repay money as a debt (at J[98]-[100]) because:

a. the definition required that the money deposited or lent had to be used for the Respondent's working capital when, on the proper construction of the definition, there is no requirement that the money be so used (to the extent the Full Court in *ABN Amro Bank NV v Bathurst Regional Council* (2014) 224 FCR 1; [2014] FCAFC 65 at [675] held that the definition of debenture in the Act imports the notion of an undertaking to repay a debt comprising a loan made to the company as part of its working capital it is wrongly decided); or in the alternative

b. the primary judge held that the money was not deposited or lent as part of the Respondent's working capital when the use was as part of the company's working capital.

Australian Securities and Investments Commission v Wallet Ventures Pty Ltd (24 July 2025) (Stewart, Cheeseman and Meagher JJ)
Australian Securities and Investments Commission v M101 Nominees Pty Ltd (in liq) (No 8) (09 July 2025) (Button J)

391. There is some controversy concerning whether the Full Court's reference, in *ABN AMRO* , to an "undertaking to repay a debt comprising a loan made to the company as part of its working capital" was intended to impose a discrete requirement that, in order to be a debenture, the loan must have been part of the issuer's working capital: at [675] (Jacobson, Gilmour and Gordon JJ) .

First, when the words of the chapeau to the definition in s 9, "to repay as a debt money deposited with or lent to" the company, are read in light of the regulatory provisions of Ch 2L and Ch 6D , it is evident that those words import the notion of an undertaking to repay a debt comprising a loan made to the company as part of its working capital.

676. Here, the nature of the loan and the obligation to repay it are quite different from that which is contemplated by the usual fundraising activities traditionally associated with the issue of debentures. The loan made by LGFS was a particular form of investment in a financial product under which the obligation to redeem the investment by paying the Redemption Amount, both as to time and amount, was linked to the performance of the indices against which the value of the loan moneys was to be measured.

677. In our view the obligation to redeem that form of investment cannot be characterised as an undertaking to repay the loan as a debt. The obligation is different in nature from that which is ordinarily involved in the repayment of a loan, even one which is limited in recourse: cf *Commissioner of Taxation v Firth* (2002) 120 FCR 450 at [73]-[74] .

678. Whilst the statutory definition of a debenture departs from the common law, it would be surprising if a statutory definition which was intended to facilitate electronic commerce in debentures drastically altered the nature of a commercial instrument as understood for many generations.

679. It is true that the regulatory régime which governs fundraising under Ch 6D of the *Corporations Act* assumes the possibility that a hybrid security may have the characteristics of a debenture and a derivative. But it does not follow that an instrument which provides for redemption of a loan, at a time and in an amount, contingent upon the performance of a derivative is itself a debenture. For the reasons set out above, we do not consider that the Rembrandt notes were a debenture.

680. In coming to this view we have taken into account the decision of Kaye J in *Humes Ltd v Comptroller of Stamps (Vic)* (1989) 89 ATC 4646. In that case, a hybrid security in the form of a convertible note was held to be a debenture for the purposes of the definition of that term in the stamp duties legislation as then in force.

681. In *Humes* , the terms of the convertible note provided that the issue price for the note was a loan to the company which was repayable by the company at its option in the event that the lender did not exercise its option before a specified date to convert the loan into shares.

682. Justice Kaye said, at 4,651, that the conditions of the convertible note issue operated to create a debtor and creditor relationship in respect of the money lent by the subscriber for the notes. His Honour said that the notes could be described in the terms stated by Professor Ford as "potential equity in the legal form of a debt".

683. Plainly, the convertible notes in *Humes* were issued as part of the ordinary fundraising activities of the company and included an obligation to repay the loan as a debt if the loan was not converted to share capital. The terms of the instrument in that case illustrate the stark difference between the nature of a debenture and the form of investment product constituted by the Rembrandt notes.

684. **Following paragraph cited by:**

Australian Securities and Investments Commission v Finder Wallet Pty Ltd (14 March 2024) (Markovic J)

44. ASIC submits that, as a matter of substance, the undertaking includes repayment as a debt of the money lent to, or deposited with, Finder Wallet by the customer and, in any event, the deposit to the account carried with it an obligation to repay on demand. ASIC contends that the obligation to repay constitutes a "debt" in the sense of being an ascertainable amount which is owed and is obliged to be paid, relying on *Geeveekay Pty Ltd v Director of Consumer Affairs Victoria* (2008) 19 VR 512 at [72] , and that the term "debt" is not one of precise or inflexible denotation and must be applied in a practical and common sense fashion, relying on ***ABN Amro*** *Bank NV v Bathurst Regional Council* (2014) 224 FCR 1 at [684] . ASIC submits that it is artificial to suggest that a transaction beginning and ending with AUD that a customer chooses to invest in Finder Earn, with a notional conversion to TrueAUD in the middle and a contractual obligation to "return" the TrueAUD and reconvert it to AUD, is not a loan to, or deposit with, Finder Wallet of money which Finder Wallet undertook to repay as a debt.

3Q Holdings Limited, in the matter of 3Q Holdings Limited (No 2) (09 November 2022) (Cheeseman J)

57. In *ABN AMRO* , the Full Court observed (at [684]):

> …it is true that a debt is capable of including a debt that is repayable on a contingency. But the word "debt" is not one of precise and inflexible

> denotation. It must be applied in a practical and common sense fashion, consistent with its context and statutory purposes: *Hawkins v Bank of China* (1992) 26 NSWLR 562 at 572. Similarly, any attempt to formulate a universally applicable definition of a contingent debt is difficult, if not impossible. What is, or what is not, a contingent debt depends largely upon the statutory context and the commercial usages in which the question arises.
>
> The Full Court continued at [689]:
>
> > As the High Court said in *Handevel* at 196, not every document creating or acknowledging a debt of a company was a debenture. Similarly, not every chose in action which includes an undertaking to make payment of a sum of money, dependent upon any form of contingency, constitutes a debenture of the type contemplated by the definition in s 9 .
>
> Highup Pty Ltd (in Liquidation) v Gubas (05 November 2014) (Buchanan J)
>
> 70. Much depends on the statutory context (*Hawkins* at 572D ; *ABN AMRO Bank NV v Bathurst Regional Council* [2014] FCAFC 65; (2014) 309 ALR 445 at [684]).

Second, it is true that a debt is capable of including a debt that is repayable on a contingency. But the word “debt” is not one of precise and inflexible denotation. It must be applied in a practical and common sense fashion, consistent with its context and statutory purposes: *Hawkins v Bank of China* (1992) 26 NSWLR 562 at 572. Similarly, any attempt to formulate a universally applicable definition of a contingent debt is difficult, if not impossible. What is, or what is not, a contingent debt depends largely upon the statutory context and the commercial usages in which the question arises.

685. Here, it seems to us that a debt consisting of an obligation to redeem the Rembrandt notes at a time, and in an amount, that is measured or determined by the performance of the underlying indices to which the obligation is linked is not a debt of the type which is contemplated by the notion of a debenture.

686. We recognise the force of the observations of Rares J who reached a different conclusion as to the nature of instruments, which are similar to those in the present case, in *Wingecarribee Shire Council v Lehman Brothers Aust Ltd* (2012) 301 ALR 1 at 314 [1197] ff.

687. We accept his Honour’s observation at [1201] that the word “repay” in the definition of “debenture” does not suggest that the concept of “as a debt” necessarily requires equivalence between the loan and what the borrower must repay. We also accept that a debenture may, in certain circumstances comprise a limited recourse borrowing, as in effect occurred in *Lemon v Austin Friars*.

688. But in our view the observations of Rares J in *Wingecarribee Shire Council* at 315 [1201] do not take into account the question of whether the undertaking to repay as a debt embraces an undertaking to pay a sum of money (which may be zero) at a time and in an amount that is

dependent on the performance of something that is separate from the conduct of the operations of the business of the company that received the loan.

689. As the High Court said in *Handevel* at 196, not every document creating or acknowledging a debt of a company was a debenture. Similarly, not every chose in action which includes an undertaking to make payment of a sum of money, dependent upon any form of contingency, constitutes a debenture of the type contemplated by the definition in s 9.

690. For the reasons stated above, the obligation to redeem the Rembrandt notes at a time and in an amount contingent upon the performance of the indices, is not an obligation to repay the moneys deposited, as a debt.

691. Third, as a general rule, the term debenture was not applied at common law to an instrument unless it purported to be a debenture: *Palmer* at 4, para (h). That is not to say that the question is to be determined as a matter of form over substance, but the form and structure of the document provides some guidance as to the intentions and commercial objectives of the parties.

692. Here, the Rembrandt notes were called "Notes". It is true that terms of the Issue Notice describe the Notes as creating a debt and that they use the language of debt to describe the obligations of Perpetual to the Noteholders. But instruments such as promissory notes would not ordinarily be described as debentures. Something more is required before the instrument can be characterised as a debenture: *Re Bauer Securities Pty Ltd; Austral Mining Construction Pty Ltd v NZI Capital Corp Ltd* (1990) 4 ACSR 328 at 335 ; affirmed in *Austral Mining Construction Pty Ltd v NZI Capital Corp Ltd* (1991) 4 ACSR 57.

693. There is a strong case for party autonomy in construing complex financial instruments: *Perpetual Trustee Co Ltd v BNY Corporate Trustee Services Ltd* [2010] Ch 347 at [58]; [2012] 1 AC 383 at [103] . But here, to the extent that party autonomy provides any guide to the proper characterisation of the instrument, it points against the view that the parties intended to issue the Rembrandt notes as a debenture.

694. Fourth, it is fundamental to the nature of a debenture that it be issued by the company which borrowed the funds: *Levy* at 264. It is that company which must acknowledge the debt and undertake to repay it. Here, this condition is not satisfied for reasons stated below.

695. It is true that the definition of debenture in s 9 does not specify the requirement that a debenture must be issued by the company. But there is no reason to think that the definition departs from or ignores a concept which has for so long been recognised as fundamental to the nature of a debenture.

696. Here, the Rembrandt notes appear on their face to be issued by Perpetual as Trustee of the Rembrandt Australia Trust. Perpetual acknowledges obligations, described as debt obligations, to the Noteholders. Perpetual also undertakes the obligation to redeem the Notes.

697. However, when the Issue Notice for the Rembrandt 2006-3 notes is considered as a matter of substance it is apparent that the subscription moneys are lent by LGFS to ABN Amro. This can be seen in the back-to-back loan arrangements set out in Schedule 2 to the

Issue Notice. As we have said, ABN Amro's obligations to Perpetual to pay the interest and the Redemption Amount mirror those which are set out in the body of the Issue Notice describing Perpetual's obligations to LGFS.

698. In our opinion, the substance of the contractual arrangements between the parties was that LGFS lent the moneys to ABN Amro which held those moneys subject to an obligation to procure the repayment to LGFS through the back-to-back loan arrangements described above. ABN Amro's obligation to redeem the notes, and the time and amount of its obligation depended upon the performance of the indices in the terms described in the Issue Notice and the Derivative Contract.

699. In substance, ABN Amro issued and stood behind the notes. The loan moneys were deposited with it. Perpetual was no more than an intermediary. The true issuer of the notes did not acknowledge any indebtedness to the depositor. Nor did it undertake to LGFS as the lender or depositor any obligation to repay, whether as a debt or otherwise, the moneys subscribed by LGFS for the notes.

700. It follows in our view that the Rembrandt notes were not a debenture within the chapeau to the definition. Accordingly, we do not need to consider whether her Honour was correct in finding at J[2382] that the exception in para (a)(ii) of the definition applied.

1.1.4.4.6 The legal consequences of LGFS selling and advising in relation to the Rembrandt notes in contravention of its AFSLs and s 912A of the Corporations Act.

701. As we have noted at [601] above, S&P contended at trial and on appeal that in circumstances where LGFS had acted unlawfully in contravention of s 912A(1) of the *Corporations Act* in connection with the notes, no duty of care arises because it would be incongruous for LGFS' behaviour to be proscribed by statute but for S&P to owe a duty of care to LGFS. Therefore, according to S&P, it owed no duty of care to LGFS or to the Councils. J[2947]-J[2949].

702. S&P identified three different categories of notes – the LGFS Retained Notes, the LGFS Sold Notes and the StateCover notes (i.e., the Rembrandt 2006-2 notes). Although this section of the judgment is concerned with the first category of notes, it is necessary to consider each category of notes.

703. First, the LGFS Retained Notes. The primary judge found that LGFS did not contravene s 912A of the *Corporations Act* or its AFSLs in relation to the LGFS Retained Notes because LGFS was dealing in the notes on its own behalf and therefore its conduct fell within the exception to the definition of "dealing" in s 766C(3) of the *Corporations Act* : J[2943] and J[2986]. S&P submitted on appeal that this finding was inconsistent with the primary judge's findings that at all relevant times LGFS intended to deal in all of the notes by on-selling them to councils: J [2486]. S&P further submitted that there was no finding to the effect that, absent this intention, LGFS would have acquired any of the Rembrandt 2006-3 notes for itself. Therefore, according to S&P, at the time LGFS acquired the notes with the intention of on-selling as many of the notes that it could, LGFS was not authorised by its AFSL to provide financial product advice in relation to the notes or to deal in the notes. The final step in S&P's argument was that LGFS' intention to on-sell the notes precluded LGFS' dealing in the LGFS Retained Notes from falling within the exception in s 766C(3) of the *Corporations Act* . S&P submitted that LGFS was advising about the notes and LGFS' advice extended to the whole

tranche acquired by LGFS (the LGFS Retained Notes and the LGFS Sold Notes) so that LGFS' dealings in all of the notes was in contravention of the *Corporations Act*.

704. These contentions are rejected.

705. LGFS carries on a financial services business and therefore must hold an AFSL covering its provision of those financial services. "Financial services business" is defined in s 761A of the *Corporations Act* to be the "business of providing financial services". Relevantly, a person provides a financial service when they provide *financial product advice* or deal in a *financial product*. "Financial product advice" is defined in s 766B(1) of the *Corporations Act*, relevantly, to mean a recommendation or a statement of opinion that is intended to influence a person in making a decision about a financial product or could reasonably be regarded as being intended to have such an influence. "Financial product" is defined broadly in s 764A(1) of the *Corporations Act* and includes "a security", "a derivative" and "a debenture, stock or bond issued or proposed to be issued by a government". "Dealing" in a financial product is defined, relevantly, in s 766C(1) to include:

(a) applying for or acquiring a financial product;

(b) issuing a financial product;

(c) …

(d) varying a financial product;

(e) disposing of a financial product.

706. There is however an important exclusion. A person is taken not to deal in a financial product if the person "deals in the product on their own behalf" unless the person is an issuer of financial products *and* the dealing is in relation to one or more of those products: s 766C(3) of the *Corporations Act*.

707. It was common ground that if the Rembrandt notes were not debentures, then they were derivatives. Derivatives are a "financial product": see [705] above. LGFS was prohibited from "dealing" in derivatives or providing "financial product advice" in relation to derivatives without an AFSL permitting it to do so. Its AFSLs did not provide that permission: see [30]-[31] above.

708. S&P's submission was that s 766B(1) (see [705] above) does not require any connection with a particular tranche of notes and that therefore LGFS' recommendations and statements of opinion in relation to the Rembrandt notes to influence the Councils to purchase the notes extended to the LGFS Retained Notes. S&P attempted to link the purchase of the LGFS Retained Notes to the on-sale by LGFS to the Councils, outside the authority of its AFSLs.

709. As the primary judge stated at J[2940], there was a critical difference between the LGFS Retained Notes and the LGFS Sold Notes – the fact of sale. LGFS acquired all of the Rembrandt 2006-3 notes unconditionally and on its own behalf: ss 766C(1)(a) and 766C(3). It intended to deal in those notes by selling them to councils. Some later time, it only partly succeeded. LGFS otherwise held the LGFS Retained Notes until the sale to its parent company, LGSS. If LGFS had been unable to sell any of the notes purchased, there could be

no contravention of s 912A of the *Corporations Act* . It was not a breach of s 912A (or LGFS' AFSLs) for LGFS to buy the notes. LGFS lawfully bought the notes and bought them willing to retain any unsold notes on its balance sheet: J[2941]. In *subscribing* for the notes, LGFS was not providing financial services to the Councils or anyone else.

710. What then is to be made of the fact that LGFS purchased all of the Rembrandt notes for the purpose, and with the intention, of on-selling them to local councils. As the primary judge found: (1) LGFS marketed the notes to all councils with which it had contact; (2) LGFS did not select councils to which to market the notes on the basis that LGFS wished to retain any of the notes for itself and (3) LGFS intended to sell as many of the Rembrandt 2006-3 notes to councils as it could. However, as we have just noted, the primary judge also found that LGFS was willing to retain any unsold notes on its own balance sheet if necessary: see [1074]- [1075] below and J[2941]. Indeed, the primary judge went further and accepted the evidence of Mr Tischler when he rejected the proposition that LGFS felt it "had to get rid of [the notes]", the implication being at any cost. S&P's Appeal Grounds are rejected. The "illegality" argument is irrelevant to the LGFS Retained Notes and LGFS' claims for its losses from purchasing the LGFS Retained Notes.

711. Next, the LGFS Sold Notes. S&P submitted at trial and on appeal that LGFS' contravention of s 912A(1) of the *Corporations Act* had the following consequences: (1) it precluded the imposition of a duty of care because loss and damage could not be reasonably foreseeable; (2) no duty of care could arise on the basis of the principles set out in *Miller v Miller* (2011) 242 CLR 446, it being "incongruous for the law to proscribe the plaintiff's conduct and yet allow recovery in negligence for damage suffered in the course, or as a result, of that unlawful conduct" (see *Miller* at 454-455 [16]) and (3) LGFS could not establish causation because the "real, essential, substantial, direct or effective cause of the loss or damage" (referring to the words of Gummow J in *Elna Australia Pty Ltd v International Computers (Aust) Pty Ltd (No 2)* (1987) 16 FCR 410 at 419) was not S&P's negligence but LGFS' unlawful conduct.

712. In support of this contention, S&P submitted that the main object of Ch 7 of the *Corporations Act* is identified in s 760A as being to promote:

> (a) confident and informed decision making by consumers of financial products and services while facilitating efficiency, flexibility and innovation in the provision of those products and services; and
>
> (b) fairness, honesty and professionalism by those who provide financial services; and
>
> (c) fair, orderly and transparent markets for financial products; and
>
> (d) the reduction of systemic risk and the provision of fair and effective services by clearing and settlement facilities.

713. S&P further submitted that Pt 7.6 of the *Corporations Act* "seeks to further these policies by strictly controlling those persons who are permitted to provide financial product advice and deal in financial products, limiting the scope of financial services licenses (sic) to cover only those products which the governing authority considers the licensed person has the expertise to advise in relation to and protect other persons from loss and damage that may otherwise be sustained by others as a consequence of unlicensed persons dealing in and advising in relation

to financial products they do not understand including by permitting the rescission of contracts and providing for the financial services provider to be responsible for all loss and damage suffered".

714. According to S&P it was incongruous for a duty of care to be owed to LGFS in connection with its purchase of the Rembrandt notes in circumstances where the purposes of the relevant provisions were:

1. To strictly control those persons who are permitted to deal in products such as derivatives (which LGFS accepts were not covered by its AFSLs);

2. To limit the scope of AFSLs issued to ensure that they only cover those products which the governing authority considers the licensed person has the expertise to advise in relation to (LGFS' licence was strictly limited and did not extend to the Rembrandt notes); and

3. To protect other persons from loss and damage that may otherwise be sustained as a consequence of unlicensed persons dealing in and advising in relation to financial products they do not understand (which purpose failed as a consequence of LGFS' failure to comply with its AFSLs' conditions and other requirements of s 912A(1) of the *Corporations Act*).

715. Put simply, S&P contended that the probable consequence of LGFS investing in the Rembrandt notes in contravention of s 912A(1) of the *Corporations Act* was that its clients would suffer loss and damage for which LGFS would be wholly responsible pursuant to s 917E of the *Corporations Act* . S&P then went further and submitted that the legislature intended LGFS, and no-one else, to bear the financial ramifications of its actions in contravention of s 912A(1) of the *Corporations Act* : s 917F(5) of the *Corporations Act* . As a result, S&P submitted that to find that S&P owed LGFS a duty of care in connection with the Rembrandt notes would have the effect of transferring liability for the loss and damage suffered from LGFS to S&P which would be inconsistent with the purpose of the statute in strictly governing LGFS' conduct and the financial consequences that flow from it. It was for that reason that S&P submitted that it could not owe LGFS a duty of care in relation to the Rembrandt notes, including the LGFS Sold Notes.

716. The primary judge rejected those contentions. The primary judge stated at J[2955] that:

> *Miller v Miller* at [16] discloses that the ultimate question in this context is whether it would be "incongruous for the law to proscribe the plaintiff's conduct and yet allow recovery in negligence for damage suffered in the course, or as a result, of that unlawful conduct?" So framed it is apparent that S&P's arguments in respect of the LGFS Retained Notes find no traction on the facts or in principle. The law did not proscribe LGFS's conduct in acquiring and holding on its own account the Rembrandt notes. There is no relevant incongruity. In respect of the LGFS Sold Notes, it must be kept in mind that *Miller v Miller* did not involve facts analogous to the present. In the present case S&P has emphasised its lack of knowledge of the particular investor and my reasons emphasise the function of the rating and S&P's actual or constructive knowledge that potential investors would rely on the rating because such reliance is the essential reason why an issuer such as ABN Amro bothered to obtain the rating and was willing to pay S&P for assigning it. I have also emphasised S&P's freedom to rate or

not to rate any product and to withdraw or revise any rating at any time as it saw fit. If there is incongruity it does not arise from LGFS seeking to make S&P liable for any loss or damage resulting from the rating. It is S&P denying the existence of a duty of care based on LGFS's contraventions of the *Corporations Act* in dealing with the councils. The incongruity arises because when it was assigning the rating S&P had no knowledge of the terms of LGFS's AFSL and no reason to suspect that LGFS would be contravening its AFSL in on-selling some of the notes. The same cannot be said of the passenger in *Miller v Miller* who knew the car was stolen. For these reasons I do not see any incongruity between the existence of a duty of care on the part of S&P in respect of the rating to LGFS as a member of the class of potential investors in the Rembrandt 2006-3 notes and LGFS's contraventions of the *Corporations Act* . Althoug h S&P was told that the 2006-3 notes were intended for a bespoke investor, as discussed, S&P must have reasonably anticipated that the bespoke investor of the entirety of the tranche would or could itself sell the notes to its own clients.

717. **Following paragraph cited by:**

City Pacific Ltd (in liq) v CBRE (V) Pty Ltd (30 April 2021) (Walton J)

336. The disclaimer does not, again as a matter of general principle, 'effectively negate' the representation conveyed by a valuation, to a reader, that the valuation is prepared with due care and skill; *ABN Amro* at [717] . Similarly, even though the alleged victim of misleading conduct ordinarily must prove actual reliance upon a breach, the mere presence of a disclaimer executed a plaintiff will not defeat a finding of reliance which is otherwise supported by the evidence (See the discussion in Colin Lockhart, *The Law of Misleading or Deceptive Conduct* (2019, 5th ed, Lexis Nexis Butterworths) at 446 [10.20]).

The answer is to be found in *Miller* at 454-455 [16]. A duty of care will not be imposed because of illegality if the imposition of the duty would result in a lack of congruence in the law. The question is can the law of negligence, and the provisions of the *Corporations Act* proscribing LGFS' conduct in relation to the Councils, be given congruent operation? Put another way, LGFS' illegality raises the question – is a duty owed? LGFS' illegality does not resolve that question by compelling the conclusion that no duty is owed: *Miller* at 453 [11] and 454 [13].

718. It is to the former question we now turn. Is it incongruous for the law to proscribe LGFS' conduct but permit recovery in negligence against S&P?: *Miller* at 454-455 [15]-[16]. Two sub-issues arise: (1) the nature of the illegal conduct and (2) the identity of the person to whom the duty is owed. Here, the illegal conduct was LGFS' sale of the notes. There is no relevant incongruity in S&P owing LGFS a duty of care as LGFS' conduct in buying and holding the notes was not illegal and S&P must have reasonably anticipated that LGFS would

sell the notes: see J[2955]. There is no basis to hold that a duty is not owed by S&P to LGFS. It is also not incongruous for S&P to owe a duty to the Councils who did not breach the *Corporations Act* or the *Local Government Act* : see Part 9, Section 2.5.5 below.

719. Next, the StateCover notes. StateCover's acquisition of the Rembrandt 2006-2 notes is addressed in Part 7 below. It was not in dispute that LGFS, as funds or investment manager, bought $10 million of the Rembrandt 2006-2 notes on behalf of StateCover (the first tranche of $6 million in notes was purchased by LGFS in StateCover's name. The second tranche of $4 million was purchased by LGFS in its own name, and later transferred to StateCover): J [2982]. Again, the question is whether it is incongruous for the law to proscribe LGFS' conduct but permit recovery in negligence against S&P?: *Miller* at 454-455 [15]-[16].

720. The answer to the first sub-issue (see [718] above) is that there was no illegal conduct by StateCover in acquiring the notes. The illegal conduct was LGFS' selling and advising StateCover in relation to the notes. The answer to the second sub-issue is that the duty was owed by S&P to LGFS and StateCover. In relation to the position of LGFS, there is no relevant incongruity in S&P owing LGFS a duty of care for the same reasons as the LGFS Retained Notes and S&P's reasonable anticipation that LGFS could or would deal in the notes. In relation to StateCover, there is also no relevant incongruity in S&P owing StateCover a duty of care as its conduct in buying and holding the notes was not illegal. There is no basis to hold a duty is not owed by S&P to StateCover.

1.2 **Breach of duty:** S&P Appeal Grounds Matrix Rows 12H-12I

721. If a duty was owed (and we consider that it was) S&P did not challenge the primary judge's finding that it failed to exercise reasonable care in rating the Rembrandt notes.

722. What then was the identified breach? S&P's breach was that it had no reasonable basis for the opinion it expressed in relation to the creditworthiness of the Rembrandt notes and did not exercise reasonable care and skill in forming that opinion: J[2829]-J[2836]. S&P's duty was not a duty to be correct but a duty to exercise reasonable care and skill in forming and expressing the relevant opinion about the credit risk of the Rembrandt notes. It failed to do so: see Part 3 above.

2. STATUTORY CLAIMS – APPLICATION OF SS 1041H, 1041E OF THE *CORPORATIONS ACT* 1041E AND S 12DA OF THE *ASIC ACT*

723. LGFS made a series of claims that S&P had engaged in misleading or deceptive conduct in contravention of ss 1041E and 1041H of the *Corporations Act* and s 12DA of the *ASIC Act* . T he primary judge held that S&P's rating of AAA of the Rembrandt notes was misleading and deceptive and involved the publication of information or statements false in material particulars to a class of potential investors in Australia, which included LGFS and the Councils, because by the AAA rating there was conveyed a representation that in S&P's opinion the capacity of the notes to meet all financial obligations was "extremely strong" and a representation that S&P had reached this opinion based on reasonable grounds and as the result of an exercise of reasonable care and skill (**S&P Representations)** when neither representation was true and S&P also knew them not to be true at the time they were made.

2.1 S&P's challenge to the primary judge's finding of liability under s 1041H of the *Corporations Act* : S&P Appeal Grounds Matrix Rows 14A, 14B, 15A and 15B

724. Under s 1041H of the *Corporations Act* , "[a] person must not, *in this jurisdiction*, engage in conduct, in relation to a financial product or a financial service, that is misleading or deceptive or is likely to mislead or deceive" (emphasis added).

725. At trial, and on appeal, S&P sought to resist LGFS' claim by arguing that its conduct was not "in this jurisdiction" as required by the terms of s 1041H : S&P Appeal Grounds Matrix Rows 15A and 15B. The ultimate basis for S&P's submission at trial was that "all of the impugned conduct of S&P occurred outside Australia" and the "conduct of S&P relied upon as being misleading or deceptive does not extend to anything that occurred in Australia": J[2891]. S&P further submitted that LGFS' case was undermined by the fact that LGFS did not plead that ABN Amro acted as S&P's agent in disseminating the rating: J[2895].

726. The primary judge rejected S&P's submission for the following reasons (J[2891]-J[2899]):

1. The "critical fact" was that "S&P communicated and intended to communicate the act of the assigning and authorising the dissemination of the rating in Australia": J[2892]. The Ratings Letters were both addressed to Mr Lewis of ABN Amro in Australia: J[2892]. It was these communications which assigned and authorised, unconditionally, the dissemination of the rating: J[2892]. The statement of the rating was made by S&P at the place of intended receipt, being Australia: J[2897]. The act of communication thus occurred in Australia and was conduct in this jurisdiction: J[2892].

2. S&P cited no authority for its proposition that *all* of the conduct must have occurred in the jurisdiction. Section 1041H is enlivened by conduct in this jurisdiction in relation to a financial product or a financial service that is misleading or deceptive or is likely to mislead or deceive. This is so whether or not there is other conduct outside of the jurisdiction: J[2899].

3. It was not material that S&P did not constitute ABN Amro as its agent. The relevant point was that S&P communicated the fact of its assignment of the rating to a product to be issued in Australia to ABN Amro in Australia for the very purpose of dissemination of the rating by ABN Amro to potential investors in Australia: J[2895].

727. On appeal, S&P submitted that the primary judge erred in finding that the impugned conduct was "in this jurisdiction" for the purposes of s 1041H of the *Corporations Act* because (S&P Appeal Grounds Matrix Row 15A):

1. Her Honour erred in construing the phrase "in this jurisdiction" in s 1041H as attaching to *any* conduct in Australia when, properly construed, the term "in this jurisdiction" in s 1041H requires *all* of the impugned conduct to have taken place in Australia. As all of the impugned conduct of S&P occurred outside Australia, S&P contended that s 1041H of the *Corporations Act* has no application;

2. In the alternative, s 1041H, properly construed, only attaches to conduct if, *in substance*, it occurred in Australia. As the impugned conduct *in substance* occurred outside Australia, S&P contended that s 1041H of the *Corporations Act* has no application;

3. Her Honour erred in finding that ABN Amro's intention to disseminate the rating in Australia (or S&P's intention that ABN Amro do so), and S&P's knowledge of that intention, was relevant to the question whether S&P's conduct was in this jurisdiction; and

4. Her Honour erred in finding that it was not material that ABN Amro was not S&P's agent.

728. At trial, LGFS' and the Councils' statutory claim against S&P under s 1041H of the *Corporations Act* were substantially the same (J[2977]) and there was no material difference in S&P's position in respect of those claims. The same situation arises on appeal. What follows, therefore, applies to S&P's challenge to the primary judge's findings under s 1041H in respect of both LGFS and the Councils.

2.2. Was the conduct "in this jurisdiction"?

729. It is necessary to begin by noting the text of the statute. What is to be located "in this jurisdiction" is the conduct that is misleading or deceptive. The conduct in this case was S&P's communication of the rating to ABN Amro and the authorisation given to ABN Amro to disseminate the rating in Australia. That conduct occurred in Australia.

730. It is then necessary to turn to S&P's principal submission – that s 1041H of the *Corporations Act* is engaged only if *all* of the impugned conduct took place in Australia. If this submission is accepted, then s 1041H would not be engaged because, as the primary judge noted at J[2899], at least the assignment of the rating occurred outside Australia. S&P did not cite any authority in support of this proposition: J[2899].

731. Instead, S&P referred to ss 9 and 5(1) and (2) of the *Corporations Act* as having the effect of defining "this jurisdiction" to be the States and Territories of Australia and its territorial waters. S&P argued that this construction is supported by the prima facie rule of interpretation of legislation that it is presumed not to have extraterritorial effect: *Jumbunna Coal Mine NL v Victorian Coal Miners' Association* (1908) 6 CLR 309 at 363; *Barcelo v Electrolytic Zinc Co of Australasia Ltd* (1932) 48 CLR 391 at 423; *Niboyet v Niboyet* (1878) 4 PD 1 at 7; *Trade Practices Commission v Australian Iron & Steel Ltd* (1990) 22 FCR 305; *Solomons v District Court of New South Wales* (2002) 211 CLR 119 at 130 [9]; *Meyer Heine Pty Ltd v China Navigation Co Ltd* (1966) 115 CLR 10 at 23, 30-31, 38 and 43 and s 21(1)(b) of the *Acts Interpretation Act 1901* (Cth).

732. S&P also contended that because s 1041H is based on the former s 52 of the *Trade Practices Act 1974* (Cth) (**TPA**) and s 52 was not expressed to be limited to conduct "in this jurisdiction", this difference in language makes it plain that the intention of the *Corporations Act* was to provide a more limited application of s 1041H than s 52 of the TPA. Finally, S&P cited *Chubb Insurance Co of Australia Ltd v Moore* (2013) 302 ALR 101 as support for its construction of the phrase "in this jurisdiction". In that case, the Court concluded that the

effect of the no extraterritorial operation principle was to construe the section in issue as being concerned only with misleading or deceptive conduct that occurred in New South Wales: *Chubb* at 132 [146] . That case does not assist S&P. Once the touchstone for the prohibition, misleading conduct, is correctly identified there is no question of the extraterritorial operation of the legislation. In this context, the prohibition is on misleadingly representing, in Australia, that the rating is the product of due care and skill (and not a careless rating). *Chubb* correctly identifies the location of the misleading conduct (not the fact that renders the conduct misleading) as being the necessary territorial connection.

733. There is no statutory warrant for interpreting the term "in this jurisdiction" in s 1041H of the *Corporations Act* as requiring that *all* of S&P's conduct have occurred in Australia. As the primary judge stated at J[2899], s 1041H(1) concerns conduct in this jurisdiction in relation to a financial product or a financial service that is misleading or deceptive or is likely to mislead or deceive. If there has been such conduct, the provision is engaged. This is so whether or not there is other conduct outside of the jurisdiction.

734. S&P's interpretation of s 1041H could potentially remove from the scope of its prohibitions false and misleading representations made in Australia by an overseas defendant, provided that the defendant could prove that some small aspect of the conduct occurred outside Australia. So, on S&P's construction of s 1041H , an issuer of a misleading product disclosure statement provided to investors in Australia could escape liability if the document was prepared overseas. That would defeat the operation of the section. If that were the purpose of s 1041H , the statute would have stated that each aspect of the relevant conduct had to be "exclusively" in "this jurisdiction" or used words to similar effect. There is no basis for interpreting "in this jurisdiction" as requiring that *all* of the relevant conduct occur in Australia. S&P's principal submission is rejected.

735. Next, S&P's alternative submission – that s 1041H of the *Corporations Act* is only engaged if the impugned conduct *in substance* occurred in Australia. S&P contended that the primary judge erred in finding that S&P engaged in conduct in Australia sufficient to engage s 1041H . In support of that contention, S&P pointed to the following facts and matters:

1. S&P is a company incorporated in England and Wales. The assignment of a rating to the Rembrandt notes, and all the work relating to that assignment, occurred in England.

2. None of the nine people the primary judge identified as being "relevant" from S&P resided or worked in Australia. In particular Mr Chandler and Mr Ding, each of whom principally worked on the rating, lived and worked in England and New York respectively.

3. S&P sent the Ratings Letters from England to ABN Amro in Australia. The Councils were not given copies of any of the Ratings Letters. ABN Amro provided LGFS with a copy of the R-3 Ratings Letter and the R-2 Ratings Letter. There is no evidence that LGFS was ever provided with a copy of the 5 January 2007 Ratings Letter. There is no claim that ABN Amro or LGFS acted as S&P's agents in informing LGFS or the Councils (respectively) of

the AAA rating referred to in the Ratings Letters. On or about 15 November 2006, S&P published the Post-Sale Report on the internet. There was no evidence or suggestion that S&P's servers were located in Australia.

736. Those facts and matters are immaterial. As the primary judge stated at J[2892], the critical conduct was the communication by S&P (to ABN Amro in Australia) that it had assigned the AAA rating and S&P's authorisation of its dissemination in Australia. If S&P had never communicated the assignment of the rating to ABN Amro in Australia and authorised it to disseminate the rating in Australia, there would be no case.

737. Accordingly, it is not the location of S&P's servers or the location where the ratings were assigned that is relevant. What is relevant is that the Ratings Letters issued by S&P were issued to Mr Lewis at ABN Amro Tower, 88 Phillip Street, Sydney. By those communications S&P authorised the dissemination of the AAA rating in Australia: J [2892]. S&P communicated to ABN Amro that it had assigned a AAA rating to the Rembrandt notes "for the very purpose of dissemination of the rating by ABN Amro to potential investors in Australia": J[2895]. Her Honour found that "the rating meant nothing to ABN Amro other than as a marketing tool and S&P knew this to be the case" (at J[2794]) and that the Ratings Letters were "the culmination of S&P's retainer from ABN Amro" (at J [2897]). Equally, whether ABN Amro (or anyone else) was S&P's agent is irrelevant: J [2895]. The relevant conduct was S&P's *communication* of the rating to ABN Amro and its authorisation to ABN Amro that it could disseminate the rating in Australia. Whether ABN Amro disseminated in Australia (whether as an agent or otherwise) is immaterial for the purposes of S&P's liability under s 1041H .

738. S&P submitted on appeal that the alleged failures of S&P were failures relating to the rating of the Rembrandt notes and the evidence showed that no work was done in relation to the rating of the notes in Australia – it was all done in New York and London. Consequently, S&P argued that the impugned conduct occurred outside Australia and therefore the requisite degree of connection with Australia was absent for the purposes of s 1041H . As the primary judge found at J[2987], the assigning of the rating was not an "act complete in itself", because if that were so the Ratings Letters would have been unnecessary. The relevant conduct was the communication of the rating by S&P to ABN Amro via the Ratings Letters, including the authorisation to disseminate the rating, conduct which occurred in Australia. S&P submitted that the primary judge erred in so finding, because "[c]ontrary to her Honour's findings, it was not 'necessary' for the R-3 Ratings Letter to be sent to *S&P* in Australia. It was not necessary for a copy of that letter to be provided to LGFS or the Councils, and the Councils were not provided with copies." For the purposes of addressing this argument, we have assumed that S&P's statement that it was not necessary for the R-3 Ratings Letter to be sent to *S&P* in Australia was a mistake and that it in fact intended to state that the letter should not have been sent to *ABN Amro* in Australia.

739. **Following paragraph cited by:**

Lew Footwear Holdings Pty Ltd v Madden International Ltd (08 August 2014) (Elliott J)

The error in S&P's submissions was to focus on the facts or actions which falsified the representation. The prohibition is on engaging in misleading conduct. The relevant conduct, the representation, occurred in Australia where the communication was made. That the communication was misleading, because of facts and events occurring outside Australia, is not to the point. The communication of the representation and not those acts or omissions in the rating process is the misleading conduct. S&P's submissions erroneously conflate the misleading conduct (the representation) with the acts or omissions which falsify the representation. The primary judge correctly concluded (at J[2892]) that the fact of communication by S&P occurred in Australia and was conduct in this jurisdiction.

740. S&P further contended that the primary judge erroneously found that S&P engaged in conduct "in this jurisdiction" by sending the Ratings Letters from England to Australia because in reaching this conclusion her Honour erred in relying on matters that were not relevant to this issue. Those matters included (1) S&P's knowledge of where potential investors were located or where the rating was to be communicated; (2) that S&P communicated the fact of its assignment of the rating to a product to be issued in Australia for the very purpose of dissemination of the rating by ABN Amro to potential investors in Australia and that S&P knew or intended that ABN Amro would disseminate the rating in Australia and (3) the facts about the intended and actual communication of the rating which the primary judge held supported the conclusion that the statement of the rating was made by S&P at the place of intended receipt, being Australia: J[2893], J[2895] and J[2897]. Those matters were argued by S&P to be irrelevant because S&P's "knowledge", "purpose" or "intention" with regard to the communication and dissemination of the rating was not "conduct" for the purposes of s 1041H .

741. Even if that were true, this Appeal Ground would fail. S&P does not dispute that the Ratings Letters were *in fact* sent to and received in Australia and that authorisation was given by S&P in Australia, through the sending of those letters, for the rating to be disseminated in Australia: J[2895]. For the reasons stated at [735]- [740] above, that is enough to enliven s 1041H irrespective of S&P's purpose and intention in issuing the letters. Furthermore, it is difficult (if not impossible) to reconcile the proposition that S&P's intention is irrelevant with the High Court decision in *Voth v Manildra Flour Mills Pty Ltd* (1990) 171 CLR 538. In that case the plurality stated at 567-568 that:

> In some cases an act passes across space or time before it is completed. Communicating by letter, telephone, telex and the like provide examples… If a statement is directed from one place to another place *where it is known or even anticipated that it will be received by the plaintiff*, there is no difficulty in saying that the statement was, in substance, made at the place to which it was directed, whether or not it is there acted upon. And the same would seem to be true if the statement is directed to a place where *it ought reasonably to be expected* that it will be brought to the attention of the plaintiff, even if it is brought to attention in some third place. But in every case the place to be assigned to a statement initiated in one place and received in another is a matter to be determined by reference to the events and by asking, as laid down in [*Distillers Co (Biochemicals) Ltd v Thompson* [1971] AC 458], where, in substance, the act took place.
>
> (Emphasis added.)

742. S&P submitted that the primary judge erred in her application of the reasoning in *Voth* at 567-568 to the issue in the present case: J[2896]-J[2897]. S&P reasoned that if the above passage of *Voth* was directly applied to the identification of "conduct" the subject of s 1041H of the *Corporations Act*, then any statement that was "anticipated" to be received in Australia, would be "conduct" in Australia regardless of whether it was, in fact, ever received. This, S&P submitted, was a broad interpretation inconsistent with the ordinary meaning of the term "conduct" and would have far-reaching consequences and could not have been intended by the legislature. That submission is rejected. It is illogical. A party could not rely on a communication if it was never received and therefore caused no harm. Following *Voth*, it is relevant to consider (as the primary judge did) where S&P intended or reasonably anticipated that the statement would be received. Plainly, that was Australia, given that the Ratings Letters were issued to ABN Amro in Australia at the address of its Australian office. Her Honour correctly found that while *Voth* could only be applied "by way of analogy", on the facts in this case it was appropriate to conclude that the statement of the rating was made by S&P at the place of intended receipt, being Australia: J[2897].

743. S&P also referred to *Chubb*, a decision which was handed down after the trial decision in this case. The Court stated in *Chubb* that "[t]he essential enquiry is as to where, in substance, the act or omission giving rise to the complaint took place" (at 133 [150], citing *Voth* at 567-569) and that "[w]here there is some quality of the wrongdoer's conduct that is critical, it is usually very important to look to *where the wrongdoer acted*, not to where the consequences of the wrongdoer's conduct were felt" (at 134 [151]). The Court in *Chubb* also referred to *Dow Jones & Co Inc v Gutnick* (2002) 210 CLR 575, where the High Court stated (at 606 [43]), in the context of considering where defamatory conduct occurred in circumstances where the relevant material was placed on the internet, that:

> In the end the question is "where in substance did this cause of action arise"? [citing *Distillers* at 468 and *Voth* at 567]. In cases, like trespass or negligence, where some quality of the defendant's conduct is critical, it will usually be very important to look to where the defendant acted, not to where the consequences of the conduct were felt [citing *Voth* at 567].

Dow Jones does not assist S&P. It was a defamation case and the High Court ultimately looked to where the damage to reputation occurred in determining where the cause of action accrued, rather than where the wrongdoer acted or where its servers were located: see *Dow Jones* at 606-607 [44].

744. **Following paragraph cited by:**

Clurname Pty Limited v McGraw-Hill Financial, Inc (10 November 2017) (Wigney J)

> 159. The fifth and sixth contentions can also be dealt with shortly. As for the fifth contention, a fair reading of the proposed pleading reveals that it does not impermissibly mix fraudulent and non-fraudulent claims. It pleads those claims separately and in the alternative. As for the sixth contention, Standard & Poor's contended that Clurname's case as pleaded is that it relied on representations by the Commonwealth Bank. That contention is rejected for the reasons already given. Clurname alleges

that it relied on the S&P Representations in completing its acquisition of the SCDOs. Standard & Poor's submissions concerning inducement appeared to be based on the merits or otherwise of Clurname's case, rather than any pleading difficulty. The merits of Clurname's case in relation to inducement are a matter for trial. It should also be noted that similar arguments concerning reliance and inducement were made and rejected in relevantly similar and analogous circumstances in *ABN AMRO* at [744].

Finally, S&P contends that there was no claim that ABN Amro or LGFS acted as S&P's agents in informing LGFS or the Councils (respectively) of the ratings referred to in the Ratings Letters. S&P contends that the primary judge erred in finding that the absence of agency was not material: J[2892]-J[2895]. The difficulty with S&P's submission is that it is based on a false premise. It is not necessary for LGFS or the Councils to plead that there was an agency relationship between S&P and ABN Amro or LGFS in order for s 1041H to be engaged. What was important was the contractual relationship between S&P and ABN Amro, as contained in the Ratings Letters: see [614] above. The Ratings Letters expressly authorised ABN Amro to disseminate the rating without restriction or limitation. ABN Amro did what S&P expressly authorised it to do as part its contract with ABN Amro. In the circumstances, S&P cannot now seek to distance itself from ABN Amro's dissemination of the rating.

745. The primary judge was correct to conclude that S&P engaged in misleading or deceptive conduct "in this jurisdiction" in contravention of s 1041H.

2.3 Section 1041E of the *Corporations Act*: S&P Appeal Grounds Matrix Rows 23A, 23B, 26A and 26B

746. Section 1041E, entitled "False or misleading statements", relevantly provides that:

> A person must not (whether in this jurisdiction or elsewhere) make a statement, or disseminate information, if:
>
> …
>
> (c) when the person makes the statement, or disseminates the information:
>
> …
>
> (ii) the person knows, or ought reasonably to have known, that the statement or information is false in a material particular or is materially misleading.

"Statement" is defined in s 9 to include a matter "that is not written but conveys a message". "Information" is defined in s 9 to include a complaint.

747. The primary judge held that S&P made a statement and disseminated information when it published the rating it assigned to the Rembrandt notes. At trial and on appeal, S&P

contended that s 1041E attaches to written or oral statements or information but not to conduct with the result that s 1041E cannot have any application to representations arising from conduct: S&P Appeal Grounds Matrix Rows 26A and 26B.

748. The first step is the proper identification of the statement or information upon which LGFS relied. This point was not directly addressed in the submissions. The parties' submissions proceeded on the basis that the "statement" or "information" was S&P informing ABN Amro that it had assigned a AAA rating to the Rembrandt notes and its authorisation for ABN Amro to disseminate that rating to "interested parties" and its subsequent publishing of the Post-Sale Report: see [51] and [53]-[55] above. Those paragraphs repay careful reading.

749. The next step is to ask whether s 1041E was engaged.

750. **Following paragraph cited by:**

In the matter of Mediation & Online Dispute Resolution Operating Network Pty Ltd (23 February 2022) (Rees J)

99. As the plaintiffs submitted, the term "statement" embraces a "representation": *ABN AMRO Bank NV v Bathurst Regional Council* (2014) 224 FCR 1; [2014] FCAFC 65 at [750] , [752]-[753] . The representations constituted statements for the purpose of their claim pursuant to section 1041E(1) ; those statements were false in a material particular or materially misleading. Further, they were representations of fact, and matters that were known to be false by Mr Polito. The representations were of a kind that would instil a level of comfort in a potential investor. The plaintiffs *did* consider the provisions of the Original Constitution and found comfort in those provisions, given they were investing in a start-up company that had, to that point, been controlled by one individual. The plaintiffs *did* have regard to the intellectual property ownership issues, as they recognised that these were the Company's only asset. Mr Polito knew or ought reasonably have known that the statements were false.

As we have seen, s 1041E provides that a person must not "make a statement, or disseminate information" which has certain proscribed qualities. S&P sought to draw a distinction between representations on the one hand and statements and information on the other hand. In support of this so-called distinction, S&P referred to the reasons of Ipp J (with whom Anderson and Owen JJ agreed) in *Australian Securities Commission v Macleod* (2000) 22 WAR 255 at 260 [21] where his Honour observed that there had been "no challenge mounted" against the conclusion put by one party in that case that "statements" embraced "representations".

751. S&P contended that the only statement or information capable of being the subject of s 1041E was the statement or information that S&P had assigned a AAA rating to the Rembrandt

notes, that that statement and information was correct and there was therefore no falsity or knowledge of falsity for the purposes of s 1041E . The primary judge correctly rejected these contentions.

752. As the primary judge correctly found (J[2908]), the statement and information was not simply that "this product (the Rembrandt notes) was rated AAA". That was not the statement. Such a statement ("that the product was rated AAA") was meaningless. The statement that was made, and the information that was disseminated, by S&P was not limited to the fact that the product was rated AAA. It included (1) that the rating was S&P's opinion; (2) for which it had reasonable grounds; (3) that it had exercised reasonable care and skill in forming that opinion and (4) that the instrument (the Rembrandt notes) had an extremely high likelihood of meeting its obligations: see [55] and [50] above. Those statements and that information were set out in the Pre-Sale Report and the Post-Sale Report (see [55] and [50] above) which were, according to S&P, to be read with the criteria and related articles available on the Ratings Direct website (described as the real-time Web-based source for S&P's credit ratings, research and risk analysis at www.ratingsdirect.com) and on S&P's website at www.standardpoors.com: see [55] and [50] above including the last paragraph of the extract at [50].

753. The statements made, and the information disseminated, by S&P fell within the scope of s 1041E . The distinction S&P would seek the Court to draw between written or oral statements or information and conduct is not a relevant distinction. It asks the wrong question. The statutory questions posed by s 1041E are (1) whether a party (here, S&P) has made statements, or disseminated information and (2) if the answer to (1) is yes, did that person know, or should they reasonably have known, that the statement or information was false in a material particular or was materially misleading? In dealing with S&P, the answer to both questions is 'yes'. The statements and the information have been identified. S&P does not challenge the primary judge's finding that S&P knew, or ought reasonably to have known, that the statement or information (i.e., that identified at [752] above) was false in a material particular or was materially misleading. The product should not have been rated AAA. The published rating was not based on reasonable grounds and was not the product of the exercise of reasonable care and skill: J[2910].

2.4 Section 12DA of the *ASIC Act* : S&P Appeal Grounds Matrix Rows 17A, 17B and 22A-22E

754. Under s 12DA of the *ASIC Act* , "[a] person must not, in trade or commerce, engage in conduct in relation to financial services that is misleading or deceptive or is likely to mislead or deceive".

755. At trial and on appeal, S&P sought to resist LGFS' claim under s 12DA by submitting that (S&P Appeal Grounds Matrix Rows 17A and 17B):

1. Section 12DA is presumed not to have extraterritorial operation, except to the extent stated in s 12AC(1): S&P Appeal Grounds Matrix Rows 22A(a)-(b) and 22B;

2. Section 12DA does not apply to S&P's conduct because S&P was not "carrying on business in Australia" as required by s 12AC(1)(a): S&P Appeal Grounds Matrix Rows 17A(c) and 22C;

3. For the purposes of s 12AC(2), LGFS had not obtained the requisite Ministerial consent to bring proceedings relating to conduct outside Australia: S&P Appeal Grounds Matrix Rows 17A(d) and 22D;

4. S&P's impugned conduct was not in relation to "financial services": S&P Appeal Grounds Matrix Rows 17A(e)-(f) and 22E; and

5. S&P's impugned conduct was not misleading or deceptive or likely to mislead or deceive.

The primary judge rejected each of these grounds and correctly concluded that s 12DA was engaged.

756. The first three grounds may be dealt with together. LGFS does not rely upon misleading and deceptive conduct that occurred *outside* Australia. As we have explained (see [729]-[745] above), the relevant conduct occurred in Australia, not outside Australia. Contrary to S&P's submissions, it is unnecessary to address its contentions that s 12DA does not have extraterritorial operation.

757. That leads to the next Appeal Ground – whether the impugned conduct was in relation to "financial services". S&P's contention at trial and on appeal was that its conduct was not in relation to "financial services" because it was anterior to, and separate from, the financial service LGFS provided by dealing in and advising about the Rembrandt notes. The primary judge correctly rejected that submission: J[2904].

758. Section 12BAB of the *ASIC Act* defines the concept of "financial service". The definition is drafted by reference to when a person provides a financial service. Relevantly for present purposes, a person provides a financial service when they "provide a service … that is otherwise supplied in relation to a financial product": s 12BAB(1)(g) . S&P unsurprisingly accepted that the Rembrandt notes were financial products. The statutory question therefore was, and remains, whether, in expressing an opinion as to the creditworthiness of the Rembrandt notes by communicating the rating, S&P "provide[d] a service … that [was] otherwise supplied in relation to a financial product". In our view, the answer is yes. S&P provided a service (the rating) and that service was *in relation to* a financial product (the Rembrandt notes). The service was not for any other purpose or in relation to any other thing. Contrary to S&P's submissions, this was not a new formulation of LGFS' claim. LGFS relied upon these facts at trial to establish the contention that S&P had contravened s 12DA of the *ASIC Act* .

759. **Following paragraph cited by:**

Davis v Wilson (21 February 2025) (Shariff J)

The conclusion that in expressing an opinion as to the creditworthiness of the Rembrandt notes by communicating the rating, S&P "provide[d] a service … that [was] otherwise supplied in relation to a financial product" is consistent with authority: *Australian Securities and Investments Commission v Narain* (2008) 169 FCR 211 where an ASX release by a company about its products was "in relation to a financial product", namely shares in the company (particularly at 216-217 [19]-[22] (Finkelstein J) and at 222-224 [66]-[87] (Jacobson and Gordon JJ)) and *Australian Securities and Investments Commission v Australian Lending Centre Pty Limited (No 3)* (2012) 213 FCR 380 at 422 [176] . As the primary judge said at J [2904], the words "in relation to" are of wide import (*Narain* at 222 [68]) and, "[i]n the context of misleading and deceptive conduct claims, the relationship that is required to be established between the product and the service 'is at the lower end of the spectrum' and an 'indirect or less than substantial connection is sufficient' (*Narain* at 223 [76])". The rating was not "anterior to and separate from the provision of financial product advice" (*Avoca Consultants Pty Ltd v Millenium3 Financial Services Pty Ltd* (2009) 179 FCR 46 at 87-88 [232]); it was *in relation* to the Rembrandt notes.

760. That is sufficient to dispose of this Appeal Ground. However, there is a further basis on which s 12DA of the *ASIC Act* was engaged. As the primary judge held (at J[2904]), S&P's rating itself constituted "financial product advice" within the definition of that phrase in s 12BAB(5) . Section 12BAB(5) relevantly provided that, for the purposes of s 12BAB , *financial product advice* means:

> … a recommendation or a statement of opinion, or a report of either of those things, that:
>
> (a) is intended to influence a person or persons in making a decision in relation to a particular financial product or class of financial products, or an interest in a particular financial product or class of financial products; or
>
> (b) could reasonably be regarded as being intended to have such an influence;
>
> but does not include anything in:
>
> (c) a document prepared in accordance with requirements of Chapter 7 of the *Corporations Act* , …; or

Advice given by a lawyer in his or her professional capacity about matters of law, legal interpretation or the application of the law to any facts is not financial product advice: s 12BAB(6) .

761. As s 12BAB(5) provides, the section extends to include specified conduct intended to (or that reasonably could be expected to intend to) *influence* a person in making a decision in relation to a particular product. There are two limbs. First, we need to identify "a recommendation or a statement of opinion, or a report of either of those things" that was not prepared in accordance with requirements of Chapter 7 of the *Corporations Act* . S&P did not address this first limb. Each of S&P's ratings, at the very least, was a statement of opinion: see [752] above.

762. That leaves the next limb – could the ratings be reasonably regarded as being *intended* to influence a person or persons in making a decision in relation to a particular financial product, namely the Rembrandt notes? The answer to that question is of course. The facts set out at [580] above support that finding. Put simply S&P knew, and authorised, that its rating of the Rembrandt notes would be disseminated to potential investors in the same financial product – the Rembrandt notes. It was intended to have that effect. It was *the* reason that S&P was paid

for the rating. The primary judge was correct to conclude that the rating itself constituted "financial product advice" within the definition of that phrase in s 12BAB(5) .

763. S&P submitted that the primary judge's finding that the rating itself constituted "financial product advice" within s 12BAB(5) was "directly inconsistent" with express statements in the Ratings Letters. In particular, S&P submitted that the finding was inconsistent with the statements in the Ratings Letters that:

> The rating is not investment, financial, or other advice and you should not and cannot rely upon the rating as such.
>
> The rating is not a "market rating" nor is it a recommendation to buy, hold, or sell any obligations.

764. We reject that contention. The ratings constituted "financial product advice" within s 12BAB (5) notwithstanding these statements. Section 12BAB(5) contains the two limbs we have identified. The section's gateway is not "financial advice" but a recommendation or a statement of opinion (or a report of either of those things) which could reasonably be regarded as being *intended* to influence a person or persons in making a decision in relation to a particular financial product. Again, the facts set out at [580] above support that finding.

2.5 Was S&P's conduct misleading or deceptive?: S&P Appeal Grounds Matrix Rows 27A, 27B, 30A and 30B

765. This section of the reasons addresses LGFS' claims under ss 1041H and 1041E of the *Corporations Act* and s 12DA of the *ASIC Act* .

766. S&P accepted that the impugned conduct was "relevantly indistinguishable" from the impugned conduct relevant to the common law tort claims. The relevant conduct was the publication by S&P of the Pre-Sale Report and the Post-Sale Report: see [49]-[50] and [55] above. The primary judge found that "by assigning and authorising the AAA rating, S&P represented to all potential investors its expert opinion that the capacity of the Rembrandt notes to pay scheduled interest to noteholders and principal at maturity was extremely strong and that this opinion was based on reasonable grounds and had been reached by S&P having exercised reasonable care and skill": J[2919].

767. **Following paragraph cited by:**

J and a Vaughan Super Pty Ltd (Trustee) v Becton Property Group Pty Ltd (No 3) (17 December 2014) (Pagone J)

7. The elements necessary to establish a cause of action under s 1041H were considered recently by the Full Federal Court in *ABN AMRO Bank NV v Bathurst Regional Council* (2014) 309 ALR 445 where the court said at [767] in upholding the decision of the trial judge:

> At trial, LGFS established that (a) by communicating the rating S&P made the representations as to having reasonable grounds for and exercising reasonable care and skill in forming its opinion, (b) S&P did not have

> reasonable grounds nor did it exercise reasonable care and skill, and (c) in those circumstances S&P engaged in misleading or deceptive conduct. S&P does not challenge (b) and subject to its reliance on the disclaimers does not challenge (a). Point (c) follows from (a) and (b), subject only to the disclaimer point.
>
> The loss or damage claimed as compensation under s 1041I by Vaughan Super in this case is pleaded in paragraph [25] of the proposed pleading as arising from the matters referred to in paragraphs [15] to [24]. The foundation of the cause of action claimed by Vaughan Super in this connection are the specific statements made in the ASX Statement which are pleaded in paragraph [15] and are annexed to the proposed pleading as Schedule B. Paragraph [18] of the proposed pleading sets out what Vaughan Super claims to be the representations which Vaughan Super contends were made by those statements to the ASX which are pleaded in paragraph [15]. It is the representations said to be made by the statements which the proposed pleading claims were relied upon by Vaughan Super to its detriment and to be the cause of loss and damage.

At trial, LGFS established that (a) by communicating the rating S&P made the representations as to having reasonable grounds for and exercising reasonable care and skill in forming its opinion, (b) S&P did not have reasonable grounds nor did it exercise reasonable care and skill, and (c) in those circumstances S&P engaged in misleading or deceptive conduct. S&P does not challenge (b) and subject to its reliance on the disclaimers does not challenge (a). Point (c) follows from (a) and (b), subject only to the disclaimer point.

768. S&P submitted that (S&P Appeal Grounds Matrix Rows 30A and 30B):

> A reasonable person, having been provided with a copy of the [Post-Sale Report] …, would have read it (including the R-3 Disclaimer) prior to investing in the Rembrandt 2006-3 notes. A reasonable person would not simply have relied on the reference to the rating in the report, and ignored the remainder of it including the disclaimers. As discussed above in the context of the negligent mis-statement requirements for imposition of a duty of care, that reasonable person would interpret the conduct of S&P as a whole, including S&P's inclusion of the R-3 Disclaimer in the [Post-Sale] Report, as meaning that any statement or representation conveyed by the rating ought not be relied upon in making a decision to invest and, if it is relied upon, there can be no recourse to S&P in respect of any loss or damage suffered. That is, the R-3 Disclaimer effectively negate (sic) the effect of any conduct of S&P that might otherwise be interpreted as being misleading or deceptive. … [F]or the reasons discussed in connection with negligent misstatement, the R-2 Disclaimer alone would have the effect of negating the implied representations.

769. Those contentions are rejected for the reasons set out at [606]- [610] above. Three further points should be noted. Contrary to S&P's submissions, LGFS did not have the Post-Sale Report when it caused StateCover to subscribe for the Rembrandt 2006-2 notes on 5 September 2006 and when it subscribed for the Rembrandt 2006-3 notes on 2 November 2006, having only received the report on 16 November 2006: see [77] and [93]-[94] above.

770. Second, whether conduct is misleading or deceptive is to be determined in all the circumstances: *Campbell v Backoffice Investments Pty Ltd* (2009) 238 CLR 304 at 319 [25] (French CJ) and 341 [102] (Gummow, Hayne, Heydon and Kiefel JJ) approving *Butcher v Lachlan Elder Realty Pty Limited* (2004) 218 CLR 592 at 625 [109] . Here, the circumstances included the disclaimers and the primary judge took those disclaimers into account (see J [2916]) in concluding that in all the circumstances S&P's conduct was misleading. No appealable error is identified.

771. **Following paragraph cited by:**

Davis v Wilson (21 February 2025) (Shariff J)
CBRE (V) Pty Ltd v City Pacific Ltd (in liq) (11 April 2022) (Bell CJ, Leeming and Brereton JJA)

68. This accords with what was said in comparable circumstances by a Full Court of the Federal Court in *ABN Amro Bank NV v Bathurst Regional Council* (2014) 224 FCR 1; [2014] FCAFC 65 at [771] , reproduced by the primary judge at [334] :

> "Next, as with the claim in tort, it is necessary to consider the separate communication of the disclaimers. A reasonable person would not understand the various disclaimers to have the consequence that the rating could not be relied on. As the facts reveal (see [72]–[93] above), LGFS read the documents it had prior to subscribing for the Rembrandt notes — the Surf presentation, the term sheets, the ratings letters and the pre-sale report. A reasonable person would understand that the rating was an opinion as to creditworthiness held out to be carefully formed, and having a reasonable basis. That reasonable person would not understand the disclaimer to render the rating an exercise in futility, or an opinion with no reliable content: see [602]–[613] above."

City Pacific Ltd (in liq) v CBRE (V) Pty Ltd (30 April 2021) (Walton J)

Next, as with the claim in tort, it is necessary to consider the separate communication of the disclaimers. A reasonable person would not understand the various disclaimers to have the consequence that the rating could not be relied on. As the facts reveal (see [72]-[93] above), LGFS read the documents it had prior to subscribing for the Rembrandt notes – the Surf Presentation, the term sheets, the Ratings Letters and the Pre-Sale Report. A reasonable person would understand that the rating was an opinion as to creditworthiness held out to be carefully formed, and having a reasonable basis. That reasonable person would not understand the disclaimer to render the rating an exercise in futility, or an opinion with no reliable content: see [602]-[613] above. S&P's submission that a reasonable person would understand the disclaimer to "effectively negate" the conduct which was misleading is rejected. As LGFS stated, if the conduct is negated, it would also "effectively negate" the rating.

772. In this context, it is necessary to address a further attack by S&P (which was raised in two contexts and constituted two Appeal Grounds – S&P Appeal Grounds Matrix Rows 30A and 30B). S&P's contention was that the primary judge erred in *failing to find* that for the purposes of determining whether the impugned conduct, statements or information of S&P was misleading or deceptive, the question was whether an ordinary and reasonable member of a class of persons comprised of sophisticated wholesale investors in complex structured finance products able to invest a minimum of $500,000 would have been misled or deceived. Although the two relevant Appeal Grounds remained, S&P's written and oral submissions did not address them. In any event, the Appeal Grounds are rejected. The question was not and is not the question posed by S&P. As we have said, whether conduct is misleading or deceptive is to be determined in all the circumstances: see [770] above. That is a question of fact. It is an objective question. And that question (whether the conduct is misleading) is determined by reference to the "ordinary" or "reasonable" members of the class: *Taco Company of Australia Inc v Taco Bell Pty Ltd* (1982) 42 ALR 177 at 202 and *Campomar Sociedad Limitada v Nike International Ltd* (2000) 202 CLR 45 at 85 [102] . Here, LGFS was and remained one of the ordinary or reasonable members of the relevant class of potential investors who were likely to have been misled.

773. S&P's conduct was misleading or deceptive.

3. CAUSATION, RELIANCE AND REMOTENESS

3.1. Introduction

774. This section of the judgment addresses LGFS' claim in tort and its statutory claims against S&P. S&P accepted that the analyses substantially overlap.

775. The primary judge accepted (at J[2837]) that:

> The principles to be applied in assessing whether the impugned conduct of S&P caused loss or damage … in negligence are determined by reference to s 5D(1) of the *Civil Liability Act* [*2002* (NSW)]. Section 5D(1)(a) reflects the "but for" test at common law and is called "factual causation" in that sub-section. As for the common law, the "but for" test is not determinative of the question of causation. Section 5D(1)(b) provides that it must also be "appropriate for the scope of the negligent person's liability to extend to the harm so caused (scope of liability)". This reflects the former "common sense" approach to causation.

776. Section 5D of the *Civil Liability Act 2002 (NSW)* (**Civil Liability Act**) provides that:

> (1) A determination that negligence caused particular harm comprises the following elements:
>
> (a) that the negligence was a necessary condition of the occurrence of the harm ("factual causation"), and
>
> (b) that it is appropriate for the scope of the negligent person's liability to extend to the harm so caused ("scope of liability").

(2) In determining in an exceptional case, in accordance with established principles, whether negligence that cannot be established as a necessary condition of the occurrence of harm should be accepted as establishing factual causation, the court is to consider (amongst other relevant things) whether or not and why responsibility for the harm should be imposed on the negligent party.

(3) *If it is relevant to the determination of factual causation to determine what the person who suffered harm would have done if the negligent person had not been negligent*:

(a) the matter is to be determined subjectively in the light of all relevant circumstances, subject to paragraph (b), and

(b) any statement made by the person after suffering the harm about what he or she would have done is inadmissible except to the extent (if any) that the statement is against his or her interest.

(4) For the purpose of determining the scope of liability, the court is to consider (amongst other relevant things) whether or not and why responsibility for the harm should be imposed on the negligent party.

(Emphasis added.)

777. Under s 5E of the *Civil Liability Act* , "[i]n proceedings relating to liability for negligence, the plaintiff always bears the onus of proving, on the balance of probabilities, any fact relevant to the issue of causation".

778. The primary judge concluded that S&P's negligence and the breach of its statutory duties were a necessary condition to the harm suffered by LGFS: J[2966]. A number of matters should be noted. First, in dealing with LGFS' case against S&P, the causation analysis must address the three distinct losses suffered by LGFS: (a) its loss on the Rembrandt notes it subscribed for and held, (b) its loss on the notes sold to the Councils and (c) its loss on the notes it subscribed for on StateCover's behalf.

779. Next, for both the common law tort cause of action and the statutory causes, the primary judge undertook the same two stage inquiry required to determine whether S&P's conduct caused LGFS' losses. The first step in the inquiry is whether each loss was *in fact caused* by S&P's negligent or misleading conduct (i.e., factual causation): s 5D(1)(a) of the *Civil Liability Act* and *I & L Securities Pty Ltd v HTW Valuers (Brisbane) Pty Ltd* (2002) 210 CLR 109 at 128 [57] . That inquiry *may* be approached by adopting the "but for" test. The primary judge undertook that inquiry and concluded, in relation to each of the losses suffered by LGFS, that factual causation was established: J[2959], J[3353] and J[2965].

780. The primary judge held that LGFS bought the Rembrandt 2006-2 notes (J[1164]-J[1167], J[1169], J[1171], J[2154]-J[2156], J[2485], J[2847] and J[2965]) and the Rembrandt 2006-3 notes (J[1167]-J[1169], J[1171], J[1293]-J[1297], J[1304], J[2154]-J[2156], J[2485], J[2843]-J[2845], J[2847], J[2852], J[2857], J[2965] and J[2966]) in reliance on the AAA rating

assigned by S&P to each issue of the notes and in reliance on S&P's opinion, conveyed by the rating, that the notes had an extremely low probability of default. "But for" the AAA rating assigned by S&P, LGFS would not have purchased the Rembrandt 2006-3 notes and LGFS would not have caused StateCover to subscribe for the Rembrandt 2006-2 notes. Those findings were based on the primary judge's acceptance of the evidence of Mr Hilder and Mr Tischler, LGFS' contemporaneous documents including the document "ABN's SURF CPDO Product" which listed the pros and cons of CPDOs (see [80] above and J[1049], J[1030]-J[1031] and J[1073]) and ABN Amro's understanding based on LGFS' contemporaneous statements that LGFS would only buy the Rembrandt notes if they were assigned a AAA rating: see J[687] and J[2485].

781. The second step in the inquiry was whether it was appropriate that S&P be held liable for the actual losses suffered by LGFS (i.e., scope of liability). At trial, LGFS' case was that the rating conveyed S&P's opinion as to the extremely low probability of the notes defaulting as well as the representations about the quality of that opinion. The primary judge found that the AAA rating conveyed a representation that in S&P's opinion the capacity of the notes to meet all financial obligations was "extremely strong" and a representation that S&P had reached this opinion based on reasonable grounds and as the result of an exercise of reasonable care and skill when neither was true and S&P knew neither not to be true at the time it made the representations. S&P's opinion was wrong. S&P had no reasonable basis for its opinion: see Part 3 above.

782. LGFS understood the rating and relied on it as an expert opinion as to default risk: J[1167]-J[1171], J[1173] and J[2154]-J[2156]. S&P caused LGFS' loss occasioned by the cashing out of the Rembrandt notes. S&P's duty was to exercise reasonable care in the assigning of the rating. S&P knew or ought to have known that potential investors would rely on the rating as communicating S&P's opinion as to the creditworthiness, or default risk, of the Rembrandt notes. The Rembrandt notes cashed out because of sustained spread widening. Sustained spread widening was thus a reason (or a mere reason) for the loss. For the purpose of determining S&P's liability, S&P was the cause of the loss because it failed to exercise reasonable care in the assigning of the rating of AAA in circumstances where it must be taken to have known that potential investors such as LGFS would rely on the rating as communicating S&P's opinion as to the creditworthiness, or default risk, of the Rembrandt notes: *Travel Compensation Fund v Tambree* (2005) 224 CLR 627 at 642 [45] referring to *Environment Agency v Empress Car Co (Abertillery) Ltd* [1999] 2 AC 22. It would be inappropriate if S&P's liability did not extend to the harm it caused. The rating was directed to a particular risk and it was that risk which materialised: J[2849].

783. As LGFS submitted, S&P's obligation, corresponding with the function it was engaged and paid to perform, was to exercise reasonable care and skill to form and express an opinion, having a reasonable basis, as to the risk of the notes defaulting: see [566] and [585]-[595] above. LGFS bought the notes and marketed the notes in reliance on S&P's opinion and on the opinion being the product of due care and skill. LGFS had a reasonable basis for acting in reliance on the AAA rating: J[2154]-J[2156], J[2180], J[2194] and J[2261]. S&P's breach of duty, and misleading conduct, corresponded with the loss LGFS suffered. The loss suffered extends to the notes held by LGFS and LGFS' liability to StateCover and the Councils: J[2852].

784. That conclusion is not harsh. It accords with the facts. S&P's business model depended on the fact, which S&P knew, that potential investors would treat S&P's rating as the best independent information about risk of loss on the notes: see [40] above. Applying the normative judgment required by s 5D of the *Civil Liability Act* and s 1041I of the *Corporations Act* , S&P caused each of the types of loss suffered by LGFS and, in *Civil Liability Act* terms, liability should be imposed on S&P.

3.2 S&P's contentions on appeal

785. S&P submitted that the evidence was insufficient to discharge LGFS' onus of proof of causation and, in any event, it was not appropriate for S&P to be found liable for the alleged harm given the gross negligence and / or unlawful conduct of LGFS: S&P Appeal Grounds Matrix Rows 31A, 31B, 32A and 32B. S&P relied upon five matters (S&P Appeal Grounds Matrix Rows 38A and 38B):

1. There was no factual causation for the purposes of s 5D(1)(a) of the *Civil Liability Act* and the statutory claims because LGFS did not prove that "but for" any negligence of S&P, they would not have suffered loss and damage (the **Altern ative Universe Contention**).

2. The representations, acknowledgements and disclaimers are inconsistent with a finding that LGFS relied on S&P (the **Disclaimers Contention**).

3. The "real, essential, substantial, direct or effective cause of the loss or damage" (referring to the words of Gummow J in *Elna Australia* at 419) of LGFS was not the negligence of S&P but rather the unlawful conduct of LGFS in dealing in the notes in contravention of the *Corporations Act* (the **Real Cause of Loss Contention**).

4. S&P's conduct did not cause loss or damage in circumstances where the impugned conduct was not any statement made to or conduct directed at LGFS (the **Indirect Causation Contention**).

5. LGFS' loss and damage was too remote to be recoverable (the **Remoteness Contention**).

Each contention will be addressed.

3.2.1 Alternative Universe Contention

786. S&P's principal complaint was that *unless* LGFS proved what it would have done with the relevant funds had it not purchased the Rembrandt notes, its case must fail.

787. The primary judge rejected that contention: see J[2850]-J[2862]. We would uphold that finding but on other grounds. First, it is inconsistent with s 5D(3) of the *Civil Liability Act* : see [776] above. Section 5D(3) provides: " ***[i]f it is relevant*** *to the determination of factual causation to determine what the person who suffered harm would have done if the negligent person had not been negligent*", then the matter is to be determined subjectively in the light of all relevant circumstances subject to a qualification which presently does not arise (emphasis

added). The section acknowledges that there are circumstances when determination of factual causation does not require any reference to or consideration of the "alternative universe".

788. Second, S&P's Alternative Universe Contention is inconsistent with established authority. In *Marks v GIO Australia Holdings Ltd* (1998) 196 CLR 494 at 512-513 [42] , the Court expressed the test as requiring a comparison "between the position in which the party that allegedly has suffered loss or damage is in and the position in which that party would have been *but for the contravening conduct*" (emphasis added). As is readily apparent, this does not require any speculation about what LGFS would have done with the funds had it not purchased the Rembrandt notes.

789. The primary judge considered the question of LGFS' alternative universe at J[2852] and again at J[2857]. The primary judge stated:

> S&P assigned the rating of AAA. In so doing it was negligent. What would have occurred had S&P not been negligent is clear. The rating of AAA would not have been assigned to the CPDO notes. Accordingly, LGFS would not have purchased the CPDO notes and marketed them to the councils. …
>
> For its own purposes [LGFS] decided that its first entry into the structured products market had to involve a product rated AAA. I am satisfied that there is no real chance that LGFS would have done otherwise in any alternative universe.

The primary judge found that LGFS would not have purchased (and marketed) a structured financial product which did not carry a rating of AAA: see J[2852], J[1167]-[1169], J[1171], J[1293]-[1297], J[1304], J[2154]-[2156], J[2485], J[2843]-[2845], J[2847], J[2857] and J[2965]-J[2966].

790. Consistent with *Marks v GIO* , the comparison was between LGFS position because S&P's conduct was negligent and the position LGFS would have been in if S&P's conduct had not been negligent. That was a comparison between investment in the cashed out Rembrandt notes and the position LGFS would have found itself in from investing in a product which was carefully rated AAA, being a product with an extremely strong capacity to meet obligations and less than 0.728% probability of default. That comparison does not require or involve any irrelevant speculation contrary to the principles discussed in *Abigroup Contractors Pty Ltd v Sydney Catchment Authority (No 3)* (2006) 67 NSWLR 341 at 354-355 [59]-[63] .

3.2.2 Disclaimers Contention

791. S&P's contention at trial and on appeal was that the representations, acknowledgements and disclaimers in the documents LGFS received were inconsistent with a finding that LGFS relied on S&P. There are multiple answers.

792. First, disclaimers may be relevant to the scope of liability because it may assist in identifying the scope of that duty: see [603] above. Here, the disclaimers relied on by S&P were not to the effect that S&P took no responsibility for the reliability of its opinion or that its opinion had no reasonable foundation: see [606]-[613] above.

793. Second, and no less importantly, on the proper construction of the disclaimers, the disclaimers were not directed to reliance on the rating as an opinion about the risk of default. As we have

noted, the disclaimers do not disclaim S&P's responsibility to communicate a reliable opinion: see [613] above.

794. Third, factual causation was pleaded and established: see [779] and [780] above. The disclaimers do not and cannot affect that finding.

3.2.3 Real Cause of Loss Contention

795. S&P's contention at trial and on appeal was that in all the circumstances the "real, essential, substantial, direct or effective cause of the loss or damage" was not the negligence of S&P, but rather the unlawful conduct of LGFS in dealing in the notes in contravention of the *Corporations Act*. The primary judge rejected that contention at J[2969]-J[2970].

796. S&P's contentions are rejected for the reasons set out in Part 4, Section 1.1.4.4 above. Moreover, this contention fails on the facts: see Section 3 above. S&P's rating of the Rembrandt notes was unreasonable, unjustified and misleading: see Part 3 above. S&P authorised the rating to be disseminated to a class including LGFS. LGFS relied on that rating and suffered loss: see Part 4, Section 3.1 above.

3.2.4 Indirect Causation Contention

797. Next, S&P submitted that its conduct did not cause loss and damage because the impugned conduct was not a statement made to or conduct directed at LGFS and it is insufficient that a third party, such as LGFS, rely on allegedly misleading conduct which results in loss and damage: *Ingot Capital Investments Pty Ltd v Macquarie Equity Capital Markets Ltd* (2008) 73 NSWLR 653 at 731-732 [612]-[619] and see J[2877]-J[2881] and J[2920].

798. This contention fails on the facts: see Section 3.1 above especially at [780] above. As that factual analysis demonstrates, S&P authorised the rating to be disseminated to a class including LGFS. LGFS did not rely on a third party relying on S&P's rating. LGFS' case was based on its own direct reliance. Indirect causation does not arise.

3.2.5 Remoteness Contention

799. S&P's contention was simply that LGFS' loss was too remote to be foreseeable. In support of that contention it referred to J[2882] where the primary judge stated:

> S&P submitted that the councils were three layers of relationship removed from S&P and S&P could not have foreseen a risk of harm to them in connection with the Rembrandt notes. For the reasons already given I disagree. As discussed, S&P conveyed the AAA rating to ABN Amro (the first layer) on the express basis that the rating (and, as noted, the rating alone) could and no doubt would be communicated to potential investors. S&P had no reason to believe that ABN Amro would not market the Rembrandt notes to permit a bespoke investor such as LGFS to also market the notes. To the contrary S&P, acting reasonably, must have anticipated that ABN Amro might do so as there was nothing unusual in such an occurrence. So too S&P must have known that its AAA rating would be communicated on to the ultimate investor. The loss the councils suffered is precisely the kind of loss that S&P should have reasonably foreseen potential investors who relied on the AAA rating would suffer in the event of negligence by S&P in the assigning of the rating.

800. S&P's contention fails. First, questions of remoteness are subsumed into the statutory scope of liability issue (see [781] above) or the normative judgment as to whether a person who engaged in misleading conduct ought to be liable for losses caused by that conduct: see [784] above. S&P's Appeal Grounds relevant to those issues have been addressed and rejected: see [781]- [784] above. If, contrary to the view we have formed, foreseeability of loss remains the touchstone for liability, in addition to factual causation and scope of liability and not subsumed into those criteria, then the reasons set out at [781]-[782] above establish that the loss was foreseeable.

PART 5: LGFS' PURCHASE OF 2006-3 NOTES: ABN AMRO

801. LGFS made three claims against ABN Amro. First, that ABN Amro made negligent misrepresentations and engaged in misleading and deceptive conduct by publishing information and statements false in a material particular. Second, that ABN Amro was knowingly concerned in S&P's contraventions of ss 1041E and 1041H of the *Corporations Act* and s 12DA of the *ASIC Act* and, third, in breach of the contractual obligations ABN Amro owed LGFS, ABN Amro failed to exercise reasonable care in modelling and structuring the Rembrandt 2006-3 notes so that they would have a degree of risk commensurate with a AAA rating. Each was held by the primary judge to have been established.

802. This section of the judgment will consider the tort claims, the statutory claims and then the contractual claims.

1. TORT CLAIMS

1.1 Introduction

803. ABN Amro was found to owe LGFS two duties. The first was a duty to exercise reasonable care and skill in providing to LGFS information and advice about the Rembrandt notes (**First Duty**): J[3179] and J[3182]. The second was a duty to exercise reasonable care to arrange, and cause to be issued to LGFS, a financial product which had a degree of security commensurate with its AAA rating (**Second Duty**): J[3013] and J[3200]. That duty was derived from the function that ABN Amro undertook and agreed to undertake in relation to each issue of Rembrandt notes by the terms of the Mandate Letter: see [83] above.

804. On appeal, ABN Amro challenged the imposition of both these duties: ABN Amro Appeal Grounds Matrix Rows 77B, 77C and 77E.

1.2 First duty – to exercise reasonable care and skill in providing to LGFS information and advice about the Rembrandt notes

1.2.1 Introduction

805. LGFS' case was one of alleged negligent misstatement. ABN Amro's complaint on appeal was that the primary judge misapplied the applicable legal principles. ABN Amro submitted that the imposition of a duty of care depends, among other things, on the existence of a relationship between the person providing the information or advice (the **representor**) and the person(s) receiving it (the **representee**) which possesses the characteristics identified by Barwick CJ in *Evatt* at 569-572, as restated by Brennan J in *San Sebastian* at 371-372 . In

support of that general proposition, ABN Amro also referred to *Tepko* at 16-17 [47] and *Esanda Finance* at 249-250, 255-257, 261 and 273-274 .

806. ABN Amro submitted that the evidence did not support a finding, and the primary judge did not find, that a relationship existed between ABN Amro and LGFS which possessed the necessary characteristics: ABN Amro Appeal Grounds Matrix Rows 77B and 77C. Specifically, ABN Amro's case at trial and on appeal was that the evidence did not support a finding that ABN Amro realised or ought to have realised that LGFS would trust in ABN Amro's especial competence in relation to giving it information or advice about the Rembrandt 2006-3 notes, particularly information or advice about the creditworthiness of the notes. ABN Amro identified a number of matters which were said to support this proposition, including:

1. LGFS was financially sophisticated and not vulnerable to any want of reasonable care by ABN Amro;

2. LGFS made it a precondition to its acquisition of the Rembrandt 2006-3 notes that S&P (not ABN Amro) assign the notes a AAA rating;

3. The terms of the Mandate Letter;

4. The disclaimers in the Surf Presentation and the Rembrandt 2006-3 term sheet.

807. This section of the judgment will consider the applicable principles and then turn to address the evidentiary matters that ABN Amro contends did not support a finding that ABN Amro realised or ought to have realised that LGFS would trust in ABN Amro's especial competence in relation to giving it information or advice about the Rembrandt 2006-3 notes.

1.2.2 Applicable principles

808. The applicable principles have been addressed at [573]- [578] above. That analysis is adopted for this section of the judgment.

809. On appeal, ABN Amro sought to redraft the principles. ABN Amro's description of the characteristics necessary for the imposition of a duty in negligent misstatement was divided into four components:

1. The representor realises or ought to realise that the representee will trust in the representor's *especial competence* to give the relevant information or advice, the subject matter of the information or advice being of a serious or business nature: *San Sebastian* at 371.7, 372.7 ;

2. The representor realises or ought to realise that the representee intends to act upon the information or advice in respect of the representee's person or property in connection with some matter of business or serious consequence: *San Sebastian* at 371.9-372 .1, 372.3;

3. It would be reasonable for the representee in all the circumstances to seek, or to accept, and to rely on the information or advice: *San Sebastian* at 372.2-372 .8; and

4. It is reasonably foreseeable that the representee is likely to suffer loss should the information tum out to be incorrect or the advice turn out to be unsound: *San Sebastian* at 372.8.

(Emphasis added.)

810. ABN Amro acknowledged that it was *not* essential that the relevant information or advice be provided in response to a request from the person claiming to have suffered loss but emphasised that instances of liability for a misstatement *volunteered* negligently would be rare: *Evatt* at 571-572 . In support of that last proposition, ABN Amro placed considerable reliance on the statement by McHugh J in *Esanda* at 275 that "... absent a statement to a particular person in response to a particular request for information or advice or an assumption of responsibility to the plaintiff for that statement, it will be difficult to establish the requisite duty of care unless there is an intention to induce the recipient of the information or advice, or a class to which the recipient belongs, to act or refrain from acting on it".

811. The significance of ABN Amro's redrafting was not explained and is not self-evident. There are two relevant criteria – those in *Tepko* : see [573] above. ABN Amro did not contend that *Tepko* should not be followed. Mention, however, must be made of ABN Amro's reference to *especial competence*. The context in which it is used by ABN Amro in the first component of its summary of the relevant principles is apt to mislead. *Especial competence* was referred to by Brennan J in *San Sebastian* at 372 ("the representee will trust in his especial competence to give that information or advice") by reference to Barwick CJ's classic formulation of the essential elements which must be exhibited by the relevant relationship in *Evatt* at 571.

812. *Especial competence*, while words of limitation, do not restrict the duty to expressions of expert opinion. As Barwick CJ stated in *Evatt* at 571 :

> I think the circumstances must be such as to have caused the speaker or be calculated to cause a reasonable person in the position of the speaker to realize that he is being trusted by the recipient of the information or advice [1] to give information which the recipient believes the speaker to possess or [2] to which the recipient believes the speaker to have access or [3] to give advice, about a matter upon or in respect of which the recipient believes the speaker [4] to possess a capacity or opportunity for judgment, in either case the subject matter of the information or advice being of a serious or business nature. It seems to me that it is this element of trust which the one has of the other which is at the heart of the relevant relationship. I should think that in general this element will arise out of an unequal position of the parties which the recipient reasonably believes to exist. *The recipient will believe that the speaker has superior information, either in hand or at hand with respect to the subject matter or that the speaker has greater capacity or opportunity for judgment than the recipient.* But I do not think it can be said that this must always be so, that inequality in these respects must necessarily in fact be present or be thought to be present if the special relationship is to exist.

(Emphasis and numbering added.)

A duty may be imposed in a variety of circumstances. Relevantly, an ability by the speaker "to make careful inquiry" is sufficient foundation for a duty: *Hedley Byrne* at 503 approved by Brennan CJ in *Esanda Finance* at 249, at 252 (where Brennan CJ does not add the criterion of "especial competence"), at 256 (Dawson J) and 261 (Toohey and Gaudron JJ).

1.2.3 Evidentiary issues on appeal

813. The facts surrounding LGFS' purchase of the Rembrandt notes are addressed in Sections 4 (ABN Amro) and 6 (Sale of notes to LGFS) of Part 2 above. The primary judge considered the relevant facts at J[2997]-J[3005]. It is unnecessary to set out in detail those factual findings. For present purposes, it is sufficient to note that these facts demonstrate that:

1. ABN Amro created the CPDO, of which the Rembrandt notes were each a "vanilla issue": see [37]-[38] and [157]-[178] above. ABN Amro had a special knowledge of the notes, the characteristics of the notes, how the notes were designed to perform and the particular vulnerabilities of the notes, and the deficiencies in the modelling process;

2. In April 2006, ABN Amro discussed with LGFS a proposal that it create for LGFS an investment product that would meet the objectives of councils in New South Wales. "Central to that proposal was that the product would need to provide a high degree of security and a stable rating": see [60], [62] and [122] above and J [2997]. That product was the Rembrandt notes. At the time, ABN Amro was "conscious of the limited level of knowledge of complex financial products such as CDOs and similar products" and was "trying to identify a strategy which would be achievable and sensible for LGFS and the NSW councils in general" and it knew that "there [was] no independent specialist reviewing the transactions making it difficult for the council to truly understand the level of risk associated with the investment": see [122] above.

3. ABN Amro's task, reflected in its letter to LGFS dated 5 April 2006, was to develop a product that "may suit the requirements of NSW councils for high quality investments" and "which would meet the objectives of NSW councils (that is, return above BBSW) plus a high degree of security and rating stability of the structure": see [60], [62] and [122] above and J[3088] and J[3243].

4. The Rembrandt notes were not for anyone – they were for LGFS to sell to local councils. ABN Amro "knew that LGFS required a product for councils with a very low risk of default (i.e. with characteristics consistent with a high rating"): see [60], [62] and [122] above and J[2997(1)].

5. ABN Amro knew the notes were being purchased by LGFS specifically so the notes could be sold to local councils: see [60], [74], [75] and [121]-[122] above and J[3523]. ABN Amro knew that LGFS intended to market and sell the Rembrandt 2006-3 notes to councils in New South Wales (a defined and narrow market or limited class consisting of public bodies dealing with public funds): see [60], [74], [75] and [121]-[122] above and J[3243] and [3272].

6. ABN Amro knew it was a precondition of LGFS' purchase of the Rembrandt 2006-3 notes that the product be assigned a AAA rating: see [75] above and J[675], J[687], J[2485], J[3075], J[3171], J[3195], J[3227], J[3243], J[3272], J[3274] and J[3522].

7. ABN Amro chose to pay S&P to rate the CPDO (including the Rembrandt notes) because doing so would facilitate the marketing of the notes to those investors which needed the rating to assess the creditworthiness of the notes: see [39], [41] and [57] above and J[2777] and J[2816]. ABN Amro engaged S&P to rate the Rembrandt notes because it knew the rating was essential to its marketing.

8. ABN Amro sought a AAA rating: see [39] and [86] above;

9. ABN Amro knew that unless S&P assigned a rating of AAA to the Rembrandt notes, LGFS would not proceed with the purchase: see [75] above and J[2845].

10. ABN Amro was involved in the rating process and knew how S&P had formed its opinion expressed by the rating: see [179]-[206], [240]-[245], [248]-[258] and [265]-[280] above. The rating of the notes was as much a product of ABN Amro's assessment and pressure as it was of S&P's analysis: J[3090]-J[3091] and J[95]ff.

11. ABN Amro knew (and the Mandate Letter made clear) that it was a precondition of LGFS' purchase of the notes that they obtain a AAA rating: see [60], [62], [75] and [86] above.

12. ABN Amro knew LGFS would reasonably rely on S&P's rating and the ABN Representations: J[3191]. Indeed, ABN Amro intended that LGFS would rely on the rating: J[3197].

13. ABN Amro marketed the Rembrandt notes to LGFS on the basis that the notes had the "high degree of security" that ABN Amro knew LGFS required: see [60]-[63] above and J[3088].

14. ABN Amro deployed information (including the rating) in its marketing of the notes: see [61]-[63], [65]-[69], [92] and [94] above.

15. ABN Amro was able to, and did, provide to LGFS information about the Rembrandt notes and the rating: see [71]-[73], [80], [87]-[88] and [91] above. For example, ABN Amro explained the rating to LGFS in the Surf Presentation, orally and in other communications: see [61]-[63], [71], [92] and [94] above.

16. ABN Amro knew LGFS would market the notes to councils on the basis of the AAA rating and on the basis of the ABN Representations (see [881] below) it made to LGFS: see [61]-[69] above and J[3171] and J[3273].

17. ABN Amro knew LGFS needed to be able to communicate the AAA rating to councils and that the AAA rating would be communicated to potential council investors: J[3243]. ABN Amro knew LGFS would convey to councils that the

AAA rating meant that the product had a degree of security or default risk commensurate with the AAA rating, meaning it had an extremely strong capacity to pay interest and principal: J[3243].

18. ABN Amro knew LGFS was going to sell the Rembrandt notes to local councils in New South Wales so that if LGFS was misled, those dealing with LGFS may also be misled: see [60], [74], [87]-[88], [120]-[122] above and J [3192].

19. ABN Amro knew that LGFS and the local councils in New South Wales did not have the ability or capacity to understand sophisticated financial products like the CPDO: see [120]-[122] above and J[3075].

20. ABN Amro knew that LGFS and the local councils in New South Wales (who were potential purchasers of the Rembrandt notes) would rely on statements made, and information provided, by ABN Amro about the notes, including the rating of the notes, in deciding whether to invest: see [57] above and J[2765].

814. In short, ABN Amro created and marketed the Rembrandt notes, and deployed information (including the rating) in relation to the notes. Unless the rating and ABN Amro's statements about the rating were to be relied on, why would ABN Amro obtain and use the rating in its promotion of the notes, pay S&P a substantial fee for the rating or "highlight" the rating in its marketing? In all the circumstances, ABN Amro must have known that LGFS would reasonably rely on the rating and the representations it made about the notes: J[3191].

1.2.4 Findings and Appeal Grounds

815. The primary judge concluded, correctly, that ABN Amro owed LGFS a duty to exercise reasonable care and skill in providing to LGFS information and advice about the Rembrandt notes: J[3179], J[3182] and J[3200]. The primary judge applied the correct legal principles: J [3184]- [3192].

816. It is against that background that we turn to consider ABN Amro's Appeal Grounds.

1.2.4.1 LGFS financially sophisticated and not vulnerable

817. ABN Amro submitted at trial, and on appeal, that LGFS: (a) was a sophisticated, licensed financial services company; (b) conducted a business which involved the provision of information and advice to clients about complicated financial products, such as the Rembrandt 2006-3 notes; (c) had senior executives with considerable experience in global financial markets and (d) had access to the experience and expertise of FuturePlus and its subsidiaries.

818. ABN Amro's case was that these facts point against the relationship between ABN Amro and LGFS being one where ABN Amro realised, or ought to have realised, that LGFS would trust in ABN Amro's especial competence in the provision to it of information or advice about the Rembrandt 2006-3 notes.

819. What then were the identified errors relied upon by ABN Amro? As we best understood the argument, there were two.

820. First, it was that the primary judge (at J[3190]) erred in concluding that LGFS was vulnerable in the sense of being unable to protect itself from any want of reasonable care by ABN Amro in the provision of information or advice about the Rembrandt notes. ABN Amro acknowledged that the primary judge had regard to LGFS' financial sophistication in considering whether LGFS was vulnerable but submitted that her Honour failed to take into account the one fact which meant that LGFS was not vulnerable – its ability to negotiate for contractual warranties. ABN Amro submitted that negotiation of such warranties was and remains the ordinary way in which a purchaser obtains protection from a seller (or arranger) against the risk of being provided with inaccurate or incomplete information or advice. At a level of principle, ABN Amro contended that sellers (and arrangers) do not generally owe common law duties of care to protect purchasers from pure economic loss resulting from the failure to exercise reasonable care and skill in relation to the information or advice they provide. If they did, every misleading conduct case would be a negligence case too.

821. In support of this contention, ABN Amro placed considerable reliance on McHugh J in *Perre v Apand* at 226-227 [120]-[122] where his Honour said at 226 [120] :

> In determining whether the plaintiff was vulnerable, an important consideration will be whether the plaintiff could easily have protected itself against the risk of loss by protective action, particularly by obtaining contractual warranties ... Where another body of law can effectively deal with economic loss, a court should be slow to use negligence law to impose a duty of care on a defendant. This is particularly important where to do so would interfere with a coherent body of law in another field.

822. And, continuing at 227 [122], his Honour added (footnotes omitted):

> ... if we are to aspire to a coherent law of civil obligations, courts must keep the contractual background in mind in determining whether a duty of care should be imposed on the defendant in pure economic loss cases. Developments in negligence should occur in sympathy with the law of contract. In *Hill v Van Erp*, Gummow J said:
>
> > Bingham LJ has observed that, like equity, the law of torts may, in appropriate circumstances, fill what otherwise are perceived to be 'gaps' in what should be one coherent system of law ... That, of course, is not to assert that the function of the law of tort, with respect to recovery of economic loss caused other than by reliance on deceitful statements, is limited to the filling in of gaps left by the law of contract. But it is a starting point ...

823. We reject this so-called "error". The contention fails legally and factually. The applicable legal principles were addressed at [597]- [598] above. That analysis is applicable here. As we said at [598] above, in the field of negligent misstatement, vulnerability is the consequence of, not an additional criterion of, knowledge (actual or which a reasonable person would have) of reasonable reliance by an ascertainable class of persons. As LGFS submitted, there is no superadded requirement of vulnerability in addition to the *Tepko* criteria.

824. Next, the factual analysis. First, although ABN Amro described LGFS as "sophisticated", LGFS was in no position to question or "second guess" the rating, or undertake its own analysis of the credit risk of the Rembrandt notes: J[2771], J[2778], J[2816] and J[2927] and see [39], [580] and [600] above. Indeed, it must be recalled that ABN Amro Sydney (in

distinction to ABN Amro London) was "flying blind" in relation to the rating: J[265], J[298], J[2774] and see [258]-[298] above.

825. Second, ABN Amro knew or ought reasonably to have known that LGFS would use and rely on the rating to understand the credit risk involved: see [813] above.

826. Third, LGFS repeatedly approached ABN Amro for information about the notes in the course of LGFS' due diligence: see [813(15)] above. ABN Amro knew or ought to have known that LGFS would rely on the information provided. Otherwise, why ask the questions? Was the process, adopted by LGFS in which ABN Amro was intimately involved, of no utility? Of course not. The fact that LGFS asked ABN Amro about the notes and ABN Amro provided information about the notes is consistent with the fact that the complex notes were ABN Amro's creation: see [267(1)] above.

827. Fourth, ABN Amro volunteered further information about the rating to LGFS, including ABN Amro's erroneous explanation of the effect of the changed volatility assumption: see [91] above.

828. Put simply, ABN Amro's contention that LGFS was not vulnerable as it could obtain all necessary information about the notes elsewhere is wrong. It could not. And that contention, in any event, is inconsistent with the fact that ABN Amro provided information to LGFS: J [3190]-J[3191].

829. That leaves ABN Amro's contention that LGFS was not vulnerable because it could have negotiated a contractual warranty. That contention is also rejected. There was no evidence that ABN Amro would have agreed to any relevant warranty: *Barclay v Penberthy* (2012) 246 CLR 258 at 285 [47] and *Brookfield* at [37]-[40] . That evidence was uniquely in ABN Amro's capacity to adduce. In any event, the presence or absence of a warranty (had it been proved one may have been given) is a factor relevant to, but not determinative of, whether a duty is owed: *Barclay* at 285 [47] .

830. ABN Amro's reliance on the passages of McHugh J's judgment in *Perre v Apand* (see [821] -[822] above) does not assist it. McHugh J referred to whether a plaintiff could *easily* have protected itself against the risk of loss by protective action, particularly by obtaining contractual warranties. As LGFS submitted, as was the position in *Barclay* , there was no evidence that ABN Amro would have given the warranty and, second, and no less importantly, McHugh J recognised that there was no blunt exclusionary rule precluding negligent misstatement because a warranty may be available: see *Perre v Apand* at 227 [122], extracted at [822] above. That conclusion is not surprising. A duty or obligation will often be owed although no warranty has been given. For example, in the fields of financial products and services, auditors, financial advisors, promoters and banks often owe a relevant duty to exercise reasonable care not to make a misstatement despite not having given a warranty touching on that subject.

831. ABN Amro's role must be at the forefront of any consideration of the First Duty. Contrary to ABN Amro's submissions, ABN Amro was not a mere vendor of the Rembrandt notes. It created and produced the notes, and (importantly for the negligent misstatement case) it promoted the notes by providing information about the notes to LGFS: see [813(15)] and [825] above. If ABN Amro provided information to LGFS, it owed a duty to exercise reasonable care to do so accurately or adequately. Once ABN Amro provided information to

LGFS (as it did in the circumstances set out in [813] above), the criteria in *Tepko* were satisfied and a duty was owed. No other conclusion was open.

832. ABN Amro's second alleged error in the finding of vulnerability on the part of LGFS, notwithstanding its financial sophistication, was said to be that by focussing on LGFS' inability to verify S&P's AAA rating, her Honour incorrectly framed ABN Amro's duty of care (which was otherwise a general duty in relation to the provision of any information and advice about the notes) by reference to the alleged breach of that duty (which concerned S&P's rating). We also reject this "error".

833. ABN Amro misstated the task undertaken by the primary judge. The primary judge (at J [3181]-J[3182]) held that the duty was *not* to be formulated by reference to the particular breach. In the passage identified by ABN Amro (at J[3190]-J[3191]), the primary judge did not formulate the duty by reference to the alleged breach of that duty but engaged with, and gave reasons for rejecting, an argument advanced by ABN Amro at trial which imported an additional factor to those recognised as necessary for the imposition of a duty to exercise reasonable care in providing information and advice. The passages at J[3190]-J[3191] were directed to showing that ABN Amro's argument was wrong. No error has been identified in those passages.

1.2.4.2 LGFS' precondition to acquisition of Rembrandt 2006-3 notes was that S&P (not ABN Amro) assign AAA rating

834. ABN Amro submitted that the primary judge made a "finding" that LGFS made it a precondition to its acquisition of the Rembrandt 2006-3 notes that the notes be rated AAA *by S&P* (emphasis added): J[1293]-J[1297]. Two contentions were said by ABN Amro to flow from that "finding": (1) the finding was inconsistent with the relationship between ABN Amro and LGFS being one where ABN Amro realised, or ought to have realised, that LGFS was trusting in ABN Amro's especial competence in the provision to it of information and advice on, at least, that issue and (2) the fact that LGFS required an independent, third party, expert to rate the creditworthiness of the notes undermines entirely any suggestion that LGFS placed – or that ABN Amro realised, or ought to have realised, that LGFS placed – trust in ABN Amro's competence in that respect. Those submissions are rejected.

835. The AAA rating was a "critical factor" and "crucial prerequisite" to LGFS' assessment of the CPDO: J[1293]. However, in all the circumstances, that fact cannot, and did not, relieve ABN Amro of a duty to exercise reasonable care and skill in providing to LGFS information and advice about the Rembrandt notes.

836. First, ABN Amro by the Mandate Letter promised to "model and structure" a note which had a creditworthiness consistent with a AAA rating: see [83] and [84] above. As the Mandate Letter makes clear, ABN Amro assumed responsibility for procuring the rating, communicating the rating and explaining the rating to LGFS. LGFS was entitled to, and ABN Amro ought reasonably to have understood that LGFS would, rely on both the rating and what was said about the rating by ABN Amro.

837. Second, ABN Amro in fact did what it was retained to do: see [813(1)] above. ABN Amro obtained the rating from S&P (see [813(2) and (3)] and [825] above), made statements to LGFS about the rating for a reason (because it knew the statements would be relied on) (see [813] above) and then went further than S&P, amongst other things, by giving the rating

numerical content, explaining the changed volatility assumption, referring to rating stability and referring to the “design” of the notes in relation to creditworthiness: see [813] above.

838. In those circumstances, ABN Amro ought reasonably to have realised that LGFS would rely on its statements as well as the rating. Indeed, no other conclusion was open.

1.2.4.3 Mandate Letter

839. Next, ABN Amro submitted that the terms of the Mandate Letter were inconsistent with LGFS trusting in ABN’s especial competence in relation to the provision to it of information and advice about the Rembrandt 2006-3 notes. ABN Amro referred to three aspects of the Mandate Letter.

840. First, that ABN Amro was appointed to provide such services as the parties agreed were necessary to “close” – or bring to conclusion – “the Transaction” (being LGFS’ “firm order to purchase” $40 million of the Surf CPDO): see chapeau, and cl 1.1 at [83] above. The services which ABN Amro was to provide to LGFS included to “model and structure the Transaction”: see cl 1.2 at [83] above.

841. Second, cl 3.2, which was part of cl 3 headed “Parameters of [ABN Amro’s] Role”, provided that, “[ABN Amro] will have no responsibility for providing or obtaining on [LGFS’] behalf any ... specialist advice in connection with the Transaction. [LGFS] shall be responsible for obtaining any such advice ... and may not rely on [ABN Amro] for any such advice. Any such advice provided to [LGFS] shall be the direct legal responsibility of the provider of such advice and not of [ABN Amro]”.

842. Third, cl 3.4, which also formed part of cl 3 dealing with the parameters of ABN Amro’s role, provided: (a) “[LGFS] acknowledges that [ABN Amro] is not acting as a fiduciary but is an independent contractor retained solely for this Transaction”; (b) “[d]efining the scope of any due diligence exercise, conducting any due diligence, analysis of any due diligence results, and the prudence, desirability and commercial merits of the Transaction are all entirely decisions for and ultimately the sole responsibility of [LGFS]”; (c) “[a]ny valuation or other analysis undertaken by [ABN Amro] is provided on the understanding that [ABN Amro] does not accept responsibility for the accounting or other data (including commercial or technical assumptions) on which such analysis is based and it is [LGFS’] sole responsibility to assess and evaluate such analysis, advice, data and assumptions” and (d) “no opinion or advice rendered by [ABN Amro] or any of its Associates may be construed as a recommendation to any person as to what action they should take in relation to the Transaction”.

843. ABN Amro had two complaints about the way in which the primary judge (at J[3185]-J[3187]) addressed the Mandate Letter. ABN Amro’s first complaint was that the Mandate Letter covered services to enable the intended transaction to be completed and did not extend to services to assist LGFS to make a decision on whether to proceed with the transaction, such as giving information or advice about the notes to LGFS. In other words, ABN Amro submitted that had the relationship been one where LGFS trusted ABN Amro’s especial competence in giving information and advice about the notes to it, then the Mandate Letter would have addressed the provision of such services by ABN Amro.

844. ABN Amro’s second complaint was that the primary judge failed to appreciate that the terms of the Mandate Letter were inconsistent with LGFS placing any trust in ABN Amro in relation

to the provision of advice, which would necessarily be specialist advice (e.g., as to creditworthiness), regarding its purchase of the Rembrandt 2006-3 notes. In particular, ABN Amro submitted that cll 3.2 and 3.4 "pointed away from the relationship between ABN Amro and LGFS being one in which LGFS trusted, and ABN Amro realised or ought to have realised that LGFS trusted, in ABN Amro's especial competence in giving it information and advice about the notes". In simpler terms, ABN Amro submitted that the primary judge failed to address a relevant enquiry – whether the terms of the Mandate Letter were consistent with the existence of a relationship between ABN Amro and LGFS of the kind required for the imposition of the First Duty.

845. ABN Amro's contentions are legally and factually wrong. It is legally impermissible to seek to take one or two sub-clauses of a contract out of context. In construing bilateral private documents (such as a contract), the law gives effect to the words that the parties have chosen to express their rights and obligations, being the entirety of their rights and obligations and not some aspects of them. That is, the basic question presented in any contract case is what is "the intention disclosed by the language the parties have employed": *Masters v Cameron* (1954) 91 CLR 353 at 362 and *Australian Broadcasting Corporation v XIVth Commonwealth Games* (1988) 18 NSWLR 540 at 549. The intention is disclosed by all of the language the parties employed as recorded in the whole of contract and not just one or two clauses. The task of construction is not undertaken in the abstract. We are concerned with the engagement of the words with a particular set of facts and circumstances. How do these words apply to these facts?

846. First, the Mandate Letter. As we have just noted (at [840] above), ABN Amro was appointed as "structurer" and promised to "model and structure" a note with the characteristics referred to in the attached term sheet which included a AAA rating: cl 1.2.1 read with the chapeau set out at [83] and [84] above. Structuring involved designing and creating the notes with the promised characteristics, including a degree of creditworthiness consistent with a AAA rating. ABN Amro's obligation to "model" referred to the modelling of the notes' performance in different market conditions (there was no other modelling) which was directly related to creditworthiness: see Part 3 above. ABN Amro modelled the Rembrandt notes for its own purposes and at S&P's request as part of the rating process see Part 3 above. That obligation informs the existence of the First Duty.

847. Consistent with its appointment, which ABN Amro accepted, as "structurer" (including the services under cl 1.2.1, set out at [83] above), ABN Amro was in a position to reliably explain the creditworthiness, and other features, of the notes to LGFS. The fact that the Mandate Letter does not contain an *obligation* to provide information does not detract from that conclusion. It does not detract from that conclusion because:

1. The information had in large part already been provided when the Mandate Letter was signed: see [59]-[81] above;

2. The "Services" (defined inclusively in cl 1 (see [83] above) was sufficiently broad to include the provision of that information; and

3. Both before and after the Mandate Letter was signed, ABN Amro provided information to LGFS about the notes: see [813] above.

An express contractual promise to provide information was unnecessary.

848. Clause 3.1 (see [83] above) is not inconsistent with that conclusion. Clause 3.1 prevented LGFS from seeking advice, other than accounting or legal advice, in relation to the Rembrandt 2006-3 notes before "*close*" except with the prior consent of ABN Amro. The effect of that prohibition was that, from the date the Mandate Letter was signed, LGFS was required to obtain all information about creditworthiness from ABN Amro. Viewed objectively, it was reasonable for LGFS to rely, and ABN Amro ought reasonably to have known that LGFS would rely, on information from ABN Amro about the creditworthiness of the notes.

849. Next, cl 3.2 of the Mandate Letter: see [83] above. It restricts ABN Amro's obligations. It excluded an obligation on ABN Amro to provide or obtain (on LGFS' behalf) "any legal, regulatory, accounting, taxation or other specialist advice in connection with the Transaction". That restriction informed the content of cl 1. However, it must be read in context. First, a careful reader will notice that cl 3.2 did not address S&P's opinion as to creditworthiness or the disclaimer in the attached indicative term sheet (see [84] above) stating that a rating was a statement of opinion, not financial advice. Indeed, cl 3.2 says nothing about the reliability of the statements in fact made by ABN Amro about the rating. Next, cl 3.2 must be read with cl 3.1. Read together, it is apparent that the advice to which cl 3.2 was directed was the advice provided by lawyers and accountants, not opinions about creditworthiness. It was directed to defining ABN Amro's obligation to provide advice, not its duty in relation to the information ABN Amro in fact provided. That construction of cl 3.2 is supported by the express words of cl 3.4. It is to that clause that we now turn.

850. Again, cl 3.4 must be read as a whole and in context. The first sentence is to the effect that ABN Amro owed no fiduciary duty to LGFS. It does not refer to or exclude a common law duty. The second sentence is to the effect that it is LGFS' (thus not ABN Amro's) obligation to define the scope of LGFS' due diligence. That sentence was not directed to and does not affect the First Duty.

851. The third sentence is important. It is consistent with the First Duty being imposed. After acknowledging that ABN Amro may provide a valuation or other analysis (as it in fact did, see [813] above especially at [813(15)]), the clause then set out what was excluded from ABN Amro's responsibilities. Significantly, it only excluded ABN Amro's responsibility for underlying data, not the valuation or the analysis itself. Those two aspects were reinforced in the fourth sentence. It stated that advice and information may be provided by ABN Amro under the Mandate Letter, again giving further content to cll 1 and 3.2. ABN Amro's duty in respect of that advice and information was not limited except to the extent that the advice and information was intended solely for LGFS and limited to the transaction. The fifth sentence then provided content to the advice and information ABN Amro provided. It stated that the advice was not to be understood as a recommendation to any person as to what action they should take in relation to the transaction. As LGFS submitted, the First Duty was not excluded by the terms of the Mandate Letter. On the contrary, the terms of the Mandate Letter supported the imposition of the First Duty.

1.2.4.4 Disclaimers in Surf Presentation and Rembrandt 2006-3 term sheet

852. ABN Amro submitted that both the Surf Presentation (which ABN Amro provided to LGFS) and the Rembrandt 2006-3 term sheet contained disclaimers which made it clear that the relationship between ABN Amro and LGFS was not of the requisite kind, namely one where

ABN Amro realised, or ought to have realised, that LGFS trusted in ABN Amro's especial competence in giving to LGFS information and advice about the Rembrandt 2006-3 notes.

853. ABN Amro placed considerable emphasis on the following aspects of those documents. It first referred to the following statements in the "Disclaimer" section of the Surf Presentation (see [69] above):

> No representation, warranty or assurance of any kind, express or implied, is made as to the accuracy or completeness of the information contained herein. [ABN Amro] accepts no obligation to any recipient to update or correct any such information. No act or omission of [ABN Amro] or any of its directors, officers, employees or agents in relation to the information contained herein shall constitute, or be deemed to constitute, a representation, warranty or undertaking of or by [ABN Amro] or any such person.
>
> …
>
> By accessing this presentation and before entering into any transaction each recipient represents, warrants and agrees that ... (ii) they are a professional/institutional/accredited /expert investor with sufficient knowledge, experience and professional advice to make their own evaluation of the merits and risks of making a complex investment of this type, (iii) they shall, at all times, be solely responsible for making their own independent appraisal of the reference entity(ies) and investigation into the business, financial condition and creditworthiness thereof, (iv) they are fully aware that they may lose a significant amount or all of their investment, (v) they are responsible for making their own independent investigation and appraisal of the risks, benefits and suitability of any investments envisaged by this document, and for obtaining their own independent financial advice, and (vi) [ABN Amro] shall not incur any responsibility or liability whatsoever to any recipient in respect thereof.

854. In the Rembrandt 2006-3 term sheet (see [84] above), ABN Amro referred to the section on page 7 headed "Important Information". The second paragraph of that section (starting in line 8 with the words "Each recipient represents ..."), contained a disclaimer in substantially the same terms as the second passage quoted above from the Surf Presentation. In addition, the third paragraph of the "Important Information" section stated:

> The securities described in this term sheet may be assigned a credit rating by one or more rating agencies. A credit rating is not a recommendation to buy, sell or hold Securities and may be revised or withdrawn by the relevant rating agency at any time. Each rating agency has its own methodology and modelling assumptions for rating transactions; ratings are sensitive to the methodology and modelling assumptions used and different methodologies, models and/or assumptions may, and in all likelihood will, produce different ratings. Any rating assigned to the securities represents the relevant rating agency's opinions regarding the credit quality of such securities; it is not a guarantee of quality or performance, nor is it an evaluation or indication of the likelihood or risks of fluctuations in market value. Any rating assigned to the securities may not fully reflect the true risks of an investment therein and may, in any event, be subject to qualifications. The risks, returns and performance of the securities described in this term sheet may differ from those of an equivalently-rated corporate bond.

855. ABN Amro submitted that the following conclusions should be drawn from these disclaimers:

1. ABN Amro expressly disclaimed responsibility for the accuracy or completeness of any information it provided;

2. LGFS accepted responsibility for making its own independent investigation and appraisal of the risks, benefits and suitability of the notes, and released ABN Amro from any responsibility or liability to it in respect thereof; and

3. The term sheet made it plain that the AAA credit rating assigned to the notes was purely a statement of S&P's, not ABN Amro's, opinion, which was subject to change.

856. There are a number of answers to those contentions. First, the identified passages do not address the First Duty. The passages expressly acknowledge that ABN Amro was providing information and its opinions. For example, the disclaimer in the Surf Presentation records that the presentation is for "information… purposes". The second paragraph of the Surf Presentation disclaimer, to the effect that ABN Amro was not acting as a financial adviser or as a fiduciary to the reader of the Surf Presentation, also does not address the First Duty. Indeed, contrary to ABN Amro's submissions, the purpose of the Surf Presentation was to provide information which would be relied on. The disclaimers can and should be construed consistently with the presentation having content. Similarly, the disclaimer in the term sheet was directed to identifying that ABN Amro was not making representations in relation to "tax, legal or accounting matters". Those limitations were not directed to the imposition of the First Duty, a duty of a different character. There was, and is, no basis for construing those passages as excluding ABN Amro's responsibility for the provision of that information. On the contrary, the passages support the imposition of the First Duty.

857. Second, as the primary judge held (at J[3101]), a reasonable reader would not understand the disclaimer in the Surf Presentation (*[n]o representation, warranty or assurance of any kind, express or implied, is made as to the accuracy or completeness of the information contained herein …*) as being directed to the rating. If ABN Amro's construction was adopted, it would render ABN Amro's repeated references to the rating futile and contrary to how ABN Amro in fact marketed the notes: see [813] above. Consistent with that view, the disclaimer was directed to the *content* of the *presentation*. It did not address the many other occasions ABN Amro made statements to LGFS about the rating: see [813] above. In that context, it is important to recall that the disclaimer in the term sheet sought to explain the rating further, which is consistent with ABN Amro having a duty to exercise reasonable care to explain the rating accurately.

858. Third, for the reasons set out above at [602]-[613] [paragraph 72 of LGFS' submissions in response to S&P], the disclaimers did not have the exclusionary effect for which ABN Amro contended. Finally, although the rating was a statement of S&P's opinion, not ABN Amro's opinion, once ABN Amro relied on and explained S&P's opinion (as it did in the manner set out at [813] above), ABN Amro had a duty to exercise reasonable care to say what it knew about the reliability of the opinion.

859. ABN Amro raised two further matters: an inutility point and illegality. The argument that the First Duty lacks utility is directed at too high a level of generality. This appeal is not about the duties of promoters and structurers in general. The imposition of a duty is fact dependent. In this appeal, ABN Amro knew or ought to have known the deficiencies in the

rating and yet it continued to rely on and market the rating and (incompletely) provided LGFS with information about the rating: see Part 3 and [813] and [825] above. There is no inutility in imposing the First Duty. On the contrary, the First Duty advances, coherently with the prohibition on misleading or deceptive conduct, a duty to exercise reasonable care when providing information about a product which the person who is the structurer and promoter is selling.

860. The illegality point has been addressed in Part 4 , Section 1.1.4.4 above. ABN Amro relied on the submissions of S&P. These Appeal Grounds are rejected for the same reasons.

1.3 Second Duty – to exercise reasonable care to arrange and cause to be issued to LGFS a financial product which had a degree of security commensurate with its AAA rating

861. ABN Amro accepted (and it is not disputed) that the existence of the duty was to be determined by a close analysis of the facts bearing on the relationship between ABN Amro and LGFS in order to identify the "salient features" affecting the appropriateness of imputing it: J[3183].

862. However, ABN Amro submitted that the primary judge erred in finding ABN Amro owed the Second Duty to LGFS because (ABN Amro Appeal Grounds Matrix Row 77E):

1. The existence of the Second Duty was inconsistent with the terms of the Mandate Letter: J[3195];

2. The only effect of the Second Duty would be to cause ABN Amro to warrant to LGFS the correctness of any AAA rating S&P gave the Rembrandt 2006-3 notes;

3. To the extent that the Second Duty required ABN Amro to attempt to assess the competency with which S&P rated the creditworthiness of the Rembrandt 2006-3 notes, the Second Duty was inefficient, inutile and, therefore, inappropriate; and

4. The unlawfulness of LGFS' conduct precluded the imposition of the Second Duty.

863. Each matter will be addressed in turn.

1.3.1 Mandate Letter

864. ABN Amro submitted that the terms of the Mandate Letter obliged ABN Amro to model and structure the Rembrandt 2006-3 notes so that they had the defined characteristics (as to term, size, note type, coupon etc.) set out in the indicative term sheet attached to the Mandate Letter but did not oblige ABN Amro to model and structure the notes so that they had a level of security commensurate with any AAA rating S&P gave them.

865. ABN Amro's argument does not accord with the language used in the Mandate Letter (see [83]-[84] above), or accord with the commercial purposes of the parties. In the chapeau of the

Mandate Letter (see [83] above), it stated that ABN Amro promised to use “all reasonable endeavours” and to “model and structure” the Rembrandt notes and not, as ABN Amro suggested, simply to complete some documents: see, in particular, cll 1.1 and 1.2.1.

866. Of course the Mandate Letter did not prescribe how ABN Amro should or could perform that obligation. It could have adopted the structuring and modelling it already performed but that fact does not limit the proper construction of the obligation attaching to its function: cl 1.1. Similarly, although it was directed to defining ABN Amro’s role, cl 3 did not restrict that role in the manner ABN Amro contended. Indeed, the language of the term sheet – that the notes were expected to receive a AAA rating from S&P (see [83]-[84]) – was consistent with (a) the obligations created by cll 1.1 and 1.2 and (b) a duty to exercise reasonable care to structure the notes so that the notes, if issued, had a creditworthiness consistent with the rating. In that context, it must be recalled that a AAA rating was a precondition to LGFS’ investment and ABN Amro knew that fact: see [813(11)] above.

867. The express terms of the Mandate Letter were consistent with the imposition of the Second Duty.

1.3.2 Warranty?

868. The second issue was the alleged warranty point. ABN Amro submitted that if S&P had rated the notes correctly, then the Second Duty would add nothing. However, if S&P negligently rated the notes AAA, then the effect of the Second Duty would be to give LGFS a claim against ABN Amro (in addition to any claim it might have against S&P). Contrary to ABN Amro’s submission, the construction adopted by the primary judge (at J[3194]-J[3196]) and by this Court on appeal does not result in ABN Amro providing a contractual warranty as to the notes’ creditworthiness. ABN Amro had two obligations – a contractual obligation to use “all reasonable endeavours” (cl 1.1) and the corresponding Second Duty – a duty to exercise reasonable care to arrange and cause to be issued to LGFS a financial product which had a degree of security commensurate with its AAA rating. Neither has the character of a warranty. Neither was a promise by ABN Amro to perform S&P’s function. Each was a promise to use reasonable endeavours to structure a product to achieve the rating, structuring being an area of ABN Amro’s professed expertise.

1.3.3 S&P should have detected lack of creditworthiness in the notes

869. The third issue was ABN Amro’s reliance on S&P to negate the imposition of the Second Duty. It is necessary to understand the way in which ABN Amro put this contention. ABN Amro submitted that *insofar* as the imposition of the Second Duty required it to assess the competency with which S&P rated the Rembrandt 2006-3 notes, the duty was inefficient, inutile and therefore inappropriate.

870. The factual foundation for that contention was said by ABN Amro to be:

1. ABN Amro (like other arrangers) was not expert in conducting credit ratings, whereas S&P (as an expert credit rating agency) was. Put simply, ABN Amro contended that the Second Duty required the inexpert to assess the competency of the expert;

2. Not having designed the CPDO, S&P was independent of the Rembrandt 2006-3 notes, whereas ABN Amro, as the arranger of the product, was not. Thus, the duty required the potentially partial arranger to judge the competency of the impartial rating agency – like one team in a sporting contest assessing the competency of the referee;

3. Although it could (and generally did) choose to do so, S&P was not obliged to disclose to ABN Amro its rating methodology or reasoning. Thus, the duty required ABN Amro to undertake a task which it could not necessarily perform, even if otherwise qualified to do so;

4. Potential purchasers of the Rembrandt 2006-3 notes were interested in S&P's, not ABN Amro's, opinion as to the creditworthiness of the notes.

ABN Amro's complaint was that, viewed overall, the imposition of the Second Duty required ABN Amro to incur significant costs without being likely to produce any commensurate benefit or, indeed, any benefit at all. That contention is without foundation.

871. First, the contention is contrary to the terms of the Mandate Letter: see Part 5, Section 1.2.4.3 and Section 1.3.1 above. ABN Amro's role was to "model and structure" the transaction by which LGFS would purchase the Rembrandt 2006-3 notes having a rating assigned by S&P of AAA.

872. Second, ABN Amro's factual foundation was and remains misstated: see Part 5, Section 1.2.3. ABN Amro participated in the rating process and knew S&P had not detected deficiencies in the rating process, deficiencies it knew existed: see Part 3 above.

873. Third, the fact that S&P should have detected a lack of creditworthiness in the Rembrandt notes cannot and does not inform the duty ABN Amro took on by the Mandate Letter. The fact that another person or entity may owe an overlapping or co-extensive duty does not negate the existence of a duty being owed. An auditor owes a duty although the auditor is able to correctly say that the company's directors owed a duty to find any significant error in the company's financial statements (and the reverse also applies). Promoters owe a duty although other professionals also owe duties in relation to statements made in the course of promoting the product or the company.

874. Indeed, so much appears to have been conceded by ABN Amro. It did not challenge the imposition of the *whole* of the Second Duty. It challenged it only *insofar* as the imposition of the Second Duty required it to assess the competency with which S&P rated the Rembrandt 2006-3 notes. The balance of that duty – a duty to exercise reasonable care to arrange and cause to be issued to LGFS a financial product which had a degree of security commensurate with its AAA rating – remains. It is that duty, in its entirety, that was correctly imposed.

1.3.4 Vulnerability

875. LGFS' vulnerability has been addressed at [817]- [833] above. Those considerations apply equally to the Second Duty. In addition, the terms of the Mandate Letter, including, in particular, cll 1.1, 1.2 and 3.1 are inconsistent with ABN Amro's contention that LGFS was not vulnerable.

1.3.5 Unlawfulness

876. The illegality point has been addressed in Part 4 , Section 1.1.4.4 above. ABN Amro relied on the submissions of S&P. These Appeal Grounds are rejected for the same reasons.

1.4 Were these duties breached?

877. ABN Amro appeals against the primary judge's finding that ABN Amro breached the First Duty and the Second Duty it owed to LGFS. Each duty will be considered separately.

1.4.1 First Duty – negligent misstatement

1.4.1.1 Introduction

878. ABN Amro's case at trial (and on appeal) was that ABN Amro did not breach the First Duty because it did not make the representations and, even if it did, the making of the representations was not negligent or misleading: ABN Amro Appeal Grounds Matrix Row 78C. On appeal, ABN Amro contended the representations were not made, because ABN Amro was a mere conduit of S&P's AAA rating. It asserted that the primary judge wrongly concluded (at J[3095]-J[3096]) that ABN Amro made the representations to LGFS by its Surf Presentation: see [61]-[63] above. It will be necessary to return to consider the Surf Presentation in further detail later in this section of the judgment.

879. It was common ground that whether a representation was conveyed depended on analysing ABN Amro's conduct in relation to LGFS as a whole in all the relevant circumstances, including: what ABN Amro and LGFS each knew, or may be taken to have known; the subject matter of the alleged representations and the nature of the transaction in which they were engaged: *Butcher* at 604-605 [37], 605 [39]-[40] and 631-632 [128]-[129] . That approach was not disputed by LGFS and was the approach adopted by the primary judge: see J[3094].

880. This section of the judgment addresses the following questions: (1) what were the representations and did ABN Amro make each of them? and (2) was the making of the representations negligent or misleading?

1.4.1.2 Representations made?

881. The first step is to identify the representations. The primary judge held (at J[3007], J[3009]-J[3010] and J[3086]-J[3104]) that ABN Amro made the following representations:

1. The risk of default of the Rembrandt notes was commensurate with the risk of default of a AAA rated bond, namely the capacity of the issuer to repay interest and principal was extremely strong and involved a risk of default of not more than 0.728%;

2. The Rembrandt notes had a risk of loss commensurate with the AAA rating or not greater than 0.728%; and

3. S&P's opinion, that the risk of interest not being paid on time for the term of the Rembrandt 2006-3 notes or of principal not being repaid in full on maturity

was commensurate with the risk of default on a AAA rated bond, could be safely relied on.

(the **ABN Representations**).

882. The second step is to address ABN Amro's submission that it did not, in all the circumstances, convey each ABN Representation to LGFS: ABN Amro Appeal Grounds Matrix Row 59B.

883. The relationship between ABN Amro and LGFS was summarised at [813] above. As that factual analysis demonstrates, ABN Amro knew, when ABN Amro first approached LGFS with the Rembrandt notes, that LGFS required a product which had the characteristics of a AAA rated note: J[3088]. ABN Amro provided to LGFS the Surf Presentation: J[3095]. That presentation (a) emphasised the AAA rating (see [62]-[68] above), (b) described the CPDO as being designed to have a high and stable rating (see [62]-[68] above), (c) described the notes as "suitable" for investors who required a high rating (see [62]-[68] above) and (d) emphasised, including by deploying the rating, the asserted very low risk of default of the notes: see [62]-[68] above. The presentation also explained the rating and the issues in assessing credit risk (see [62]-[68] above) and explained that assumptions may change (see [62]-[68] above). ABN Amro expressed (and explained) the rating as conveying S&P's opinion that the notes had a not more than 0.728% probability of default, an explanation inconsistent with a mere passing on of the rating.

884. But, as the analysis in Part 3 (especially at [246], [247], [442], [443] and [517]-[524]) demonstrates, the Surf Presentation was a partial explanation of the rating and its modelling. That explanation, without the known deficiencies in the rating, had the consequence (a) that the rating was not passed on for what it was worth and (b) that having given a partial explanation ABN Amro was duty bound to give a full explanation of what it knew about the rating. In deploying and explaining the rating, but not its known deficiencies and thus lack of reliability, ABN Amro represented that the rating was a reliable expression of opinion in the terms described. ABN Amro also conveyed a representation that the rating could be safely relied on (deploying the rating in its marketing without qualification conveyed that meaning).

885. What then were the matters relied on by ABN Amro to support its contention that it was a mere conduit which made no representation? There were seven.

886. First, ABN Amro submitted that each of the ABN Representations concerned a matter of opinion – that is, the creditworthiness of the Rembrandt 2006-3 notes – about which LGFS believed S&P (and not ABN Amro) was appropriately qualified and able to render an independent, expert assessment. This matter was addressed at [872] above and is rejected. Also, it must be recalled that ABN Amro did not "*make it apparent that it … expressly or impliedly disclaims any belief in [the rating's] truth or falsity, merely passing [the rating] on for what it is worth …*": *Yorke v Lucas* (1985) 158 CLR 661 at 666 approved in *Butcher* at 605 [38]-[39] and 629-630 [123] . On the contrary, ABN Amro deployed the rating as part of its marketing, which is inconsistent with both passing on and disclaiming any belief in the reliability of S&P's opinion: see [813] above. Indeed, LGFS was concerned to know ABN Amro's opinion of the creditworthiness of the Rembrandt notes – ABN Amro had, after all, created them.

887. Second, ABN Amro submitted that, subject to one qualification, each of the ABN Representations was identical with and added nothing to representations which the primary judge found that S&P had made, including to LGFS, as to the creditworthiness or risk of default of the Rembrandt 2006-3 notes. This matter was addressed at [873] above and is rejected.

888. Third, ABN Amro submitted that LGFS had no reason to believe, and there was no evidence that it did believe, that ABN Amro had engaged in its own comprehensive assessment of the creditworthiness of the Rembrandt 2006-3 notes. That contention only needs to be stated to be rejected. ABN Amro, the designer and structurer of the notes, retained by LGFS under the Mandate Letter to achieve a particular outcome, said that the notes had been designed to have a high and stable rating, consistent with that stated outcome: see [813] above. A statement to that effect conveys to a reasonable reader that ABN Amro employed some assessment of creditworthiness in the course of that design, as ABN Amro in fact did: see [813] above. Absent disclaimer of any belief in the reliability of the rating, a reasonable person would understand ABN Amro to be asserting its reliability and would not think that ABN Amro had made no assessment of its own of the Rembrandt notes' creditworthiness.

889. That is especially so when ABN Amro:

1. Claimed in the Surf Presentation to have conducted back-testing to see how the CPDO would have performed if issued between February 1996 and August 2003, an assessment of the stability of S&P's rating in hypothetical future market conditions and a sensitivity analysis to see how the notes performed in different credit spread scenarios: see [62] above;

2. Spoke to the Surf Presentation, "highlighting" the rating: see [813(15)] above;

3. Deployed the rating as part of its marketing: see [813(14) and (15)] above. Once ABN Amro deployed the rating in that context ABN Amro was required to disclose the facts inconsistent with the meaning conveyed by the communication of the rating and ABN Amro's failure to do so was misleading or negligent;

4. Continued providing information, including about the rating, to LGFS after it provided the Surf Presentation to LGFS: see [813(15)] above;

5. Participated, to a substantial extent, in the rating process and could assess the quality of the rating: see [813(10)] above. ABN Amro prepared the model used (see J[102]), performed its own modelling (see J[119], J[138]-[146], J[172]-[175], and J[242]), built its model "by applying aspects of the way S&P informed the market that it had modelled some of the risks …" (see J[590]-J[591]) and had considerable knowledge of the rating process.

ABN Amro was not passing on what was solely S&P's opinion, but was communicating an opinion which was "as much a result of ABN Amro's assessment and pressure" as S&P's analysis: J[3091].

890. Fourth, ABN Amro referred to the "Important Information" section of the Rembrandt 2006-3 term sheet provided to LGFS before it purchased the notes and, in particular, the disclaimers in that section of the term sheet: see [854] above. The disclaimers in the term sheet were considered at [856]- [858] above. The disclaimers do not assist ABN Amro.

891. Fifth, ABN Amro submitted LGFS was, and was known to ABN Amro to be, a sophisticated licensed financial services provider. This matter was addressed at [824]ff above and is rejected. In that context, ABN Amro submitted that LGFS was "capable of critically reviewing the reasonableness of S&P's base case modelling assumptions". ABN Amro did not refer to any evidence or any finding in support of that submission. Indeed, the submission would appear to conflict with a finding by the primary judge (at J[3197] and J[2771]) that LGFS could not "second-guess", or verify the reliability of, the rating. That leads to rejection of the next matter relied upon by ABN Amro, namely that LGFS could be expected to, and did, carefully consider the documents that had been provided to it prior to its purchase of the Rembrandt notes. That statement is without content. As ABN Amro knew, LGFS could not assess creditworthiness beyond accepting the rating and the facts it was told about the rating. The purpose of the rating ABN Amro procured, paid for, deployed and highlighted was to provide the necessary information about creditworthiness: see [57] above.

892. ABN Amro next relied on the terms of the Surf Presentation: see [61]-[69] above. The presentation cannot be divorced from the other facts to which reference has just been made. J [3095] and J[3103].

893. ABN Amro described the primary judge's analysis of the content of the Surf Presentation in the following terms:

> The points … can be grouped as follows: (a) *first*, the presentation drew attention to the combination of coupon at 190 bps and S&P's AAA rating on coupon and principal as desirable features of the Rembrandt 2006-3 notes (e.g., by describing the notes as a "breakthrough" and as suitable for investors who "require high rating of principal and coupon payments"); (b) s*econdly*, in a number of places, the presentation stated that the notes were "designed to have a stable rating", being a rating of AAA on principal and coupon; (c) *thirdly*, at pages 21-22, the presentation described S&P's rating methodology and the meaning of its AAA rating, including statements that the "probability of receiving the rated coupons and principal at maturity is benchmarked to the default probability of an S&P bond with the same rating and tenor" and "[t]he S&P 10 year AAA cumulative default probability is [0.728]%"; and (d) *fourthly*, at page 23, the presentation contained a section on rating sensitivity based on ABN's modelling.
>
> (Emphasis in original.)

ABN Amro did not dispute those points but submitted that the primary judge erred in failing to have regard to, or in misunderstanding, what it described as "at least seven other significant features of the presentation".

894. The seven points, in summary, were that:

1. The AAA rating was expressly identified as *S&P's* rating of the Rembrandt 2006-3 notes;

2. The presentation of S&P's rating methodology and of the meaning of its AAA rating accorded with what the primary judge found S&P to have represented by its AAA rating;

3. The rating sensitivity section of the presentation took S&P's rating model and base case assumptions as a given for the purposes of assessing the sensitivity of the rating to change;

4. The presentation repeatedly referred readers to S&P's base case modelling assumptions;

5. The presentation contained prominent statements cautioning readers about the reliability of the modelling assumptions mentioned in it, including those of S&P;

6. The presentation contained a "Disclaimer" section on page 39; and

7. The presentation contained no express statement that ABN Amro agreed with S&P's AAA rating of the Rembrandt 2006-3 notes, or believed that the rating could be safely relied on.

895. The first four of ABN Amro's points in relation to the Surf Presentation are slightly different ways of making the same point – that the rating was S&P's opinion and was expressed to be S&P's opinion. So much can be accepted. However, as we have repeatedly noted, that does not diminish ABN Amro's duty, or the representations made: see [837] above. The statements ABN Amro made about the rating must be considered in the context in which those statements were made: see [883]-[891] above. A reasonable person in LGFS' position would have understood ABN Amro to be saying that (a) the rating could be safely relied on (otherwise there was no point to deploying the rating) and (b) the product had a risk of default commensurate with the rating, ABN Amro having not only repeatedly described the rating, but it also having stated that it designed the notes to have a high degree of security and rating stability.

896. The fifth proposition repays careful analysis. It contains a number of errors. The Surf Presentation does not contain "prominent statements cautioning readers about the reliability of modelling assumptions, including those of S&P". None of the notations contained in the presentation are to the effect that the modelling is or may be unreliable. Further, other than page 29 of the Surf Presentation (under the heading "Key Risk Factors") (see [62] above), the modelling referred to was ABN Amro's modelling: at pages 14 (under the heading "Cashing-In") (see [62] above) and 23 (under the heading "Rating Sensitivity") (see [62] above). There is no relevant (in the sense of derogating from the representations) caution, prominent (in terms of language or placement or size) or otherwise, in the Surf Presentation. ABN Amro's argument demonstrates the dangers of not reading the presentation as a whole and in all of the circumstances. In the context of the other statements in the Surf Presentation and the use made of the rating by ABN Amro, the statements identified by ABN Amro may be put to one side: see [857] above.

897. That leaves ABN Amro's criticism of the primary judge's treatment (at J[3100]) of the "words of caution" on page 23 of the Surf Presentation: see [62] above (under the heading "Rating Sensitivity"). The words relied upon by ABN Amro were the following: "*[t]he assumptions underlying the analysis illustrated above are unlikely to be consistent with actual*

experience. In addition, S&P can change their rating assumptions, rating models and the way they monitor the rating at any time". ABN Amro submitted that, contrary to the primary judge's finding that the statement did not relate to "any analysis of S&P", it was clear from the way in which rating sensitivity was assessed that the assumptions underlying the analysis included S&P's base case assumptions. ABN Amro misread the passage. S&P's base case assumptions were referred to. However, read in context and as a whole, that statement in that section of the Surf Presentation directed attention to the analysis that was illustrated directly above it. That was an analysis by ABN Amro. The presentation was doing no more than stating the obvious – no particular projection will correspond exactly to the real world daily performance. That section of the report was not directed to the reliability of S&P's rating.

898. ABN Amro's sixth point relied on the disclaimers in the Surf Presentation. For the reasons addressed earlier at [852]-[858], they do not assist ABN Amro. Additional points about the disclaimer in the Surf Presentation should be noted. The disclaimer was directed to the Surf Presentation and not to other representations made by ABN Amro over many months: see [813] above. The disclaimer was ineffective to disclaim responsibility for what was said when ABN Amro's employees marketed the Rembrandt notes (and does not purport to). The disclaimer was not directed to ABN Amro's negligent and misleading conduct. The disclaimer was not directed to ABN Amro's "opinions and views", which were not the subject of the disclaimer beyond the explanation that those "opinions and views" may change.

899. In the context of dealing with the disclaimers in the Surf Presentation, it is necessary to address ABN Amro's contention that the primary judge "completely misread the disclaimer" when dealing with it at J[3103]. The primary judge did not misread the disclaimer. The disclaimer (set out at [69] above), reads:

> By accessing this presentation and before entering into any transaction each recipient *re presents, warrants and agrees* that (i) they are considering this investment for their own account, (ii) they are a professional/institutional/accredited/expert investor with sufficient knowledge, experience and professional advice to make their own evaluation of the merits and risks of making a complex investment of this type, (iii) they shall, at all times, be solely responsible for making their own independent appraisal of the reference entity(ies) and investigation into the business, financial condition and creditworthiness thereof, (iv) they are fully aware that they may lose a significant amount or all of their investment, (v) they are responsible for making their own independent investigation and appraisal of the risks, benefits and suitability of any investments envisaged by this document, and for obtaining their own independent financial advice, and (vi) [ABN Amro] shall not incur any responsibility or liability whatsoever to any recipient in respect thereof.
>
> (Emphasis added.)

900. The primary judge dealt with the disclaimer in the following way at J[3103]:

> The representations, warranties and agreements provision also appears as part of a larger paragraph without any indication to the reader that by entering into a transaction in respect of the product ABN Amro is attempting to foist upon them those representations, warranties and agreements which may or may not be accurate. For a

provision such as this to be effective it would require far more prominence in the document than it has been given. Given the extensive nature of the purported representations, warranties and agreements the reader's attention would have to be directed to the provision in clear terms. Given the lack of prominence of this provision, it cannot be concluded that any reasonable investor was aware of the existence of these purported representations, warranties and agreements let alone their content.

901. As is self-evident, her Honour was not suggesting that the disclaimer was referring to any representations or warranties by ABN Amro. On the contrary, her Honour's criticism (we would say valid criticism) of the disclaimer was its lack of prominence and, no less importantly, that it was in terms seeking to shift responsibility to LGFS for representations, warranties and agreements that were inaccurate by having LGFS representing, warranting and agreeing that it, amongst other things, had taken certain steps.

902. **Following paragraph cited by:**

Postorino v Encryption Technologies Corporation Pty Ltd (19 June 2015) (Lloyd-Jones J)

145. The second representation simply stated is that ETC was worth $30 million or more. This was contained in an email from Coombs to Postorino, dated 19 August 2008 in which Coombs represented that ETC was worth $30 million and he attributed the increase in value, at least in part, to the "*Russian deal*". The references to value were not simply passed, but instead were emphasised as the reference to the "*Russian deal*" was one of Coombs additions. It was a response to Postorino's previous email obviously calculated to reinforce the representations as to the value. The 19 August 2008 email was not in terms that suggested Coombs was merely passing on information for what it was worth, as it was cast in terms of statement unequivocally made and reinforced by repetition and explanation. None of the three types of passing on identified by McHugh J in *Butcher v Lachlan Elder Reality Pty Ltd* (supra) are engaged. Put slightly differently:

> *…[g]enerally, when a speaker deploys and highlights an opinion, while marketing a financial product to be sold for many millions of dollars, absent clear words to the effect that the speaker disclaims belief in the reliability of the opinion, the speaker is reasonably to be understood to assert that the opinion is reliable:..*
>
> (*ABN AMRO Bank NV v Bathurst Regional Council* (2014) 224 FCR 1 at [902])

That this present case involves shares to be sold for $125,000 makes no difference to that analysis.

ABN Amro's seventh point – that the presentation contained no express statement that ABN Amro agreed with S&P's AAA rating of the Rembrandt 2006-3 notes, or believed that the rating could be safely relied on – is irrelevant. Generally, when a speaker deploys and highlights an opinion, while marketing a financial product to be sold for many millions of dollars, absent clear words to the effect that the speaker disclaims belief in the reliability of the opinion, the speaker is reasonably to be understood to assert that the opinion is reliable: see, by way of example, *Yorke v Lucas* and *Butcher* . Express endorsement is not required in addition to deploying and, in this appeal, explaining the opinion. And at no time did ABN Amro state that it disclaimed belief in S&P's opinion, in circumstances when it knew it had no grounds for believing in it.

903. Accordingly, contrary to ABN Amro's contentions, ABN Amro did make each of the ABN Representations in respect of Rembrandt 2006-2 and Rembrandt 2006-3. No error has been identified. As a whole, ABN Amro's conduct and statements conveyed the ABN Representations: see [883]-[902] above. It was and remains impermissible to divorce words in parts of the Surf Presentation from (a) the balance of the presentation and (b) the circumstances and other statements made by ABN Amro to LGFS: see Part 2 , Section 6 above.

904. In this context, ABN Amro submitted that no LGFS witness gave evidence that he understood the ABN Amro Representations to have been made. That contention was correctly rejected by the primary judge at J[3099]. There are two answers to ABN Amro's submissions. First, they again reproduce only part of the reasoning in J[3099]. Second, there was evidence that established both the representations and reliance. For example, as the primary judge explained, Mr Hilder's understanding necessarily involved an understanding of the representations made by ABN Amro as he explained (a) his belief in the reliability of the rating and (b) gave that explanation in terms of ABN Amro's explanation of the rating, not only S&P's description of the rating. The evidence, taken as a whole, explained LGFS' understanding by reference to what was said, and its reasons for acting.

905. Finally, ABM Amro submitted that the primary judge (at J[3093]) was influenced by an irrelevant consideration – ABN Amro's participation in the ratings process. Again, that complaint is wrong. The relevant passage (at J[3093]) contained a rejection (not adoption) of LGFS' submission that ABN Amro's participation in the rating process *was to be* taken into account in determining whether ABN Amro was a mere conduit. There are however, two further matters to be noted. As the primary judge went on to point out, "ABN Amro's involvement [was] relevant to other aspects of the cases against it". That is not open to debate – ABN Amro's involvement was relevant to its knowledge of the deficiencies in the rating (Part 3 above and [813] above) and its defence that it was a mere conduit: see [889] above.

1.4.1.3 Representations misleading?

906. The relevant statements were about S&P's opinion which was conveyed by the rating. LGFS accepted that, for ABN Amro's statements to be a negligent misstatement or misleading, ABN Amro must have known or ought reasonably to have known that S&P did not have a reasonable basis for that opinion. The primary judge held that (1) ABN Amro knew or ought reasonably to have known that there was not a reasonable basis for the rating, and (2) thus the representations were misleading. No error has been identified. As the reasons in Part 3 demonstrate, ABN Amro knew or ought reasonably to have known that there was not a reasonable basis for the rating: see also Part 5, Section 1 above.

1.4.2 Second Duty – duty as structurer

907. At trial, LGFS submitted that ABN Amro breached the Second Duty by causing the Rembrandt 2006-3 notes to be issued in circumstances where: (a) it knew, or ought reasonably to have known, that the notes did not have a degree of risk commensurate with a AAA rating and/or (b) there was no reasonable basis for ABN Amro to believe that the notes would have such a degree of risk when issued. The primary judge made that finding at J [3213].

908. ABN Amro appealed that finding: ABN Amro Appeal Grounds Matrix Row 78E. ABN Amro contended that it did not breach the Second Duty because it had reasonable grounds to believe S&P's AAA rating of the Rembrandt 2006-3 notes. The Rembrandt notes did not have a degree of security commensurate with a AAA rating, as a direct result of the structure adopted by ABN Amro, and ABN Amro knew that: see [813] and Part 3 above. ABN Amro did not have reasonable grounds to believe S&P's AAA rating of the Rembrandt 2006-3 notes: see Part 3 above.

909. Further, ABN Amro breached the Second Duty regardless of its knowledge of the defects in the rating because it acted with the goal of obtaining the AAA rating, not with the goal of designing a product that had characteristics consistent with that rating. Had it done the latter it would have: (a) informed S&P of the true historical volatility; (b) wanted to know the effect of historical spreads; (c) told S&P about the effect of falling spreads; (d) told S&P about the errors in the model and (e) in light of the critical effect of small changes in assumptions (and thus real world conditions) on the creditworthiness of the notes, designed a different product.

910. Finally, it must be recalled that S&P does not challenge the finding that its conduct in publishing the rating of the Rembrandt notes lacked reasonable care, and that there was not a reasonable foundation for the rating. Once it is accepted that there was a lack of a reasonable foundation for the rating, ABN Amro's approach of pushing for the AAA rating rather than re-considering the product or features of the product is sufficient to establish its breach of the Second Duty.

2. STATUTORY CLAIMS

2.1 Introduction

911. ABN Amro was found to have contravened ss 1041H and 1041E of the *Corporations Act* and s 12DA of the *ASIC Act* in relation to LGFS. ABN Amro challenged those findings: ABN Amro Appeal Grounds Matrix Rows 60A and 60B. Sections 1041H of the *Corporations Act* and s 12DA of the *ASIC Act* will be dealt with together.

2.2 Section 1041H of the *Corporations Act* and s 12DA of the *ASIC Act*

912. As with the negligent misstatement case (see Part 5, Section 1.4.1 above), there were two questions to be considered: (i) what was ABN Amro's conduct? and (ii) was that conduct misleading?

913. LGFS' claim against ABN Amro under s 1041H of the *Corporations Act* and s 12DA of the *ASIC Act* was that ABN Amro had engaged in misleading conduct by making the ABN

Representations: see [881] above. The primary judge found that ABN Amro made each of the ABN Representations. ABN Amro appealed against those findings contending that ABN Amro did not make any of the ABN Representations and was merely acting as a conduit for S&P's opinion. Those Appeal Grounds rely upon the same issues, and are rejected for the reasons, considered at [881]- [905] above.

914. The primary judge also found (at J[3105]-J[3165]) that ABN Amro's conduct was misleading. ABN Amro appealed against those findings contending that its conduct was not misleading. Those Appeal Grounds rely upon the same issues, and are rejected for the reasons, considered at [906] above. ABN Amro knew, or ought to have known, that S&P's rating of the notes was negligent and, further, ABN Amro did not have reasonable grounds for the opinions it expressed through the ABN Representations: see Part 3 above. ABN Amro lacked a reasonable basis for its representations as to the creditworthiness of the notes: see Part 3 above. ABN Amro lacked a reasonable basis for its representations as to the reliability of S&P's rating: see Part 3 above. The primary judge was correct to find that ABN Amro in fact knew that S&P's rating was not reliable: see Part 3 above.

2.3 Section 1041E of the *Corporations Act*

915. LGFS' claim was that ABN Amro, by making the ABN Representations, contravened s 1041E of the *Corporations Act* . The primary judge made that and related findings at J[3088]-J[3196]. ABN Amro's Appeal Grounds repeated the matters it raised in relation to s 1041H and are dismissed for the same reasons: see [913] above. Next, ABN Amro submitted on appeal that the primary judge erred in finding that it knew, or ought to have known, that S&P's AAA rating of the Rembrandt notes was misleading. For the reasons at [906] and [914] above, those Appeal Grounds are rejected.

3. CAUSATION

3.1 Introduction

916. The primary judge found that LGFS would not have purchased the Rembrandt notes but for ABN Amro's contraventions: J[3168]. ABN Amro appealed against that finding: ABN Amro Appeal Grounds Matrix Row 64C, 79C, 81D and 81E. It submitted that LGFS failed to establish causation because, contrary to the primary judge's findings:

1. In relation to the First Duty and LGFS' misleading conduct case, LGFS had not proved reliance on the ABN Representations (the **Reliance Contention**);

2. LGFS did not establish that, absent ABN Amro's impugned conduct, it would have adopted a course of action other than purchasing the Rembrandt 2006-3 notes, as a result of which it would have been better off than it in fact was (the **Alternative Universe Contention**); and

3. The conduct of LGFS dealing in the Rembrandt 2006-3 notes was unlawful (the **Unlawful Conduct Contention**).

917. The Unlawful Conduct Contention was addressed in Part 4 , Section 1.1.4.4 above. On appeal, ABN Amro relied on S&P's submissions. These Appeal Grounds are rejected for the same reasons.

918. ABN Amro's Reliance Contention and Alternative Universe Contention must be addressed by reference to the two stage enquiry described in Part 4 , Section 3.1 above – factual causation and scope of liability. The next section of the judgment addresses these Appeal Grounds against that legal analysis.

3.2 Reliance Contention – First Duty and LGFS' misleading conduct case

919. These submissions are not relevant to, and do not arise in relation to, the Second Duty.

920. ABN Amro accepted that LGFS relied on S&P's rating as providing a reliable opinion about the notes' likelihood of default: see J[3172]-J[3176]. ABN Amro also accepted that the primary judge correctly described the "orthodox proposition" that LGFS had to prove "that [ABN Amro's] alleged misleading conduct was at least one of the decisive considerations" in it purchasing the Rembrandt 2006-3 notes: J[3169].

921. ABN Amro's case at trial and on appeal was that LGFS failed to prove that it had relied on one or more of the ABN Representations in deciding to purchase the notes. The primary judge rejected that contention at J[3172]- [3178]. On appeal, ABN Amro submitted that the primary judge made two "distinct errors".

922. The two "distinct errors" were said to be:

1. The finding that LGFS had proved reliance on one or more of the ABN Representations when there was no evidence to support that finding or, if there was any evidence, it was contrary to that finding and, further, there was no basis on which it could be inferred that the ABN Representations were a decisive consideration in LGFS' decision to purchase the Rembrandt 2006-3 notes; and

2. The finding that LGFS did not need to prove reliance on any of the ABN Representations in order to establish causation.

Each alleged error will be addressed in turn.

3.2.1 Finding LGFS proved reliance

923. As noted at [922] above, ABN Amro's criticism was that there was no evidence to support the finding of reliance on one or more of the ABN Representations or, if there was any evidence, it was contrary to that finding and, further, there was no basis on which it could be inferred that the ABN Representations were a decisive consideration in LGFS' decision to purchase the Rembrandt 2006-3 notes.

924. ABN Amro's submission was as follows:

> First, there was no evidence from any LGFS witness of reliance on any of the ABN Representations. … [N]one of the witnesses called for LGFS gave evidence that they even understood [ABN Amro] to have conveyed those representations, let alone that any one of the representations was a decisive consideration in LGFS's decision to purchase the Rembrandt 2006-3 notes. In the first paragraph of LGFS's submissions quoted at J[3175] it was said that [ABN Amro's] submission overlooked "the evidence of Mr Hilder referring to Rembrandt having a 0.728% chance of default", which could

> only have come from the Surf [P]resentation. However, contrary to this, her Honour found at J[2517] that "by reason of S&P's rating of AAA alone, LGFS reasonably believed ... that S&P had assessed the CPDO notes as having a default probability of less than 0.728%". In addition, Mr Hilder (a) did not identify [ABN Amro] as the source of his understanding that there was a 0.728% chance of default; (b) did not refer to that understanding at all in his affidavit evidence; and (c) did not identify that understanding as a decisive consideration in LGFS's purchase of the Rembrandt 2006-3 notes. Accordingly, Mr Hilder's references "to Rembrandt having a 0.728% chance of default" were not capable of proving LGFS's reliance on any of the ABN Representations.

That submission (and the subsequent paragraphs) were wrong and are rejected. ABN Amro's submission ignores aspects, some might say critical aspects, of the evidence entirely and misconstrues the evidence referred to.

925. The facts surrounding LGFS' purchase of the Rembrandt notes have been addressed in Part 5, Section 1.2.3. The evidence disclosed that the only explanation to LGFS of the rating being expressed in terms of a percentage or numerical possibility of default was the explanation that ABN Amro gave LGFS in, and by speaking to, the Surf Presentation: see Part 5, Section 1.2.3 especially at [813] above. As the primary judge found at J[3175], Mr Hilder's understanding was derived from ABN Amro's statements to LGFS about the rating. That evidence, taken as a whole, supports the finding that ABN Amro's written and oral explanations directly influenced Mr Hilder and, no less importantly, supports the finding of reliance on one or more of the ABN Representations: see [71] above. No other conclusion was open.

926. ABN Amro submitted that the primary judge's finding at J[3175] was inconsistent with her Honour's earlier finding at J[2517] which read:

> For these reasons I accept that, by reason of S&P's rating of AAA alone, LGFS reasonably believed that in S&P's opinion the capacity of the CPDO notes to meet their financial commitments was extremely strong and that S&P had assessed the CPDO notes as having a default probability of less than 0.728%.

At that point in the judgment, her Honour was addressing S&P's case on the meaning of an S&P credit rating. Read carefully, and in context, her Honour was addressing LGFS' belief in S&P's opinion and the basis for that belief. Her Honour was not addressing the position of ABN Amro. Indeed, that finding is consistent with ABN Amro's position on appeal that it was possible for LGFS to have relied on both S&P and ABN Amro.

927. The first question was whether ABN Amro's conduct was, in all the circumstances, including both what ABN Amro said and what it left unsaid about the rating, misleading: *Demagogue Pty Limited v Ramensky* (1992) 39 FCR 31 at 32. The answer was yes: see [906] above. The ABN Representations were made (see [903] above) and were misleading (see [906] above). The next question was whether LGFS suffered loss "by" that conduct. LGFS did suffer loss because, in reliance on the rating and the information about the rating as communicated by ABN Amro, LGFS subscribed for and caused StateCover to subscribe for Rembrandt notes: see Part 2 , Sections 4 and 6, Part 3 and [813] above.

928. Two further matters should be noted about the second of those conclusions. It is not surprising. As the factual analysis demonstrates (see [813] above), the conduct of ABN Amro and S&P was not relevantly separated or severable. ABN Amro:

1. Created the CPDO, of which the Rembrandt notes were each a "vanilla issue": see [37] and [38] above and Part 3, Section 1.2 above. ABN Amro had a special knowledge of the notes, the characteristics of the notes, how the notes were designed to perform and the particular vulnerabilities of the notes and the deficiencies in the modelling process;

2. Engaged S&P, for a substantial fee, to rate the Rembrandt notes because it knew that the rating was essential to its marketing: see [39] and [41] above;

3. Sought a AAA rating: see [39] and [86] above;

4. Was involved in the rating process and knew how S&P had formed its opinion expressed by the rating: see Part 3, Sections 1.3-1.8 above. The rating of the notes was as much a product of ABN Amro's assessment and pressure as it was of S&P's analysis: J[3090]- [3091] and J[95]ff;

5. Knew (and the Mandate Letter made clear) that it was a precondition of LGFS' purchase of the notes that they obtain a AAA rating: see [60], [62], [75] and [86] above;

6. Marketed the Rembrandt notes to LGFS on the basis that the notes had the "high degree of security" that ABN Amro knew LGFS required: see [60]-[63] above and J[3088];

7. Deployed information (including the rating) in its marketing of the notes: see [61]-[63], [65]-[69], [92] and [94] above;

8. Was able to, and did, provide to LGFS information about the Rembrandt notes and the rating: see [71]-[73], [80], [87]-[88] and [91] above; and

9. Explained the rating to LGFS in the Surf Presentation, orally and in other communications: see [61]-[63], [71], [92] and [94] above.

Each step in ABN Amro's interaction with LGFS was linked to, or dependent upon, S&P's rating. Contrary to ABN Amro's contentions, it is impermissible to ignore S&P's rating when considering the ABN Representations and the fact that LGFS relied on those representations.

929. Second, causation and reliance can be proved (and often must be proved under s 5D(3)(b) of the *Civil Liability Act*) not through a formula of words as to what a witness with hindsight says he or she would have done in a hypothetical world, but by reference to the objective probabilities and an analysis of the relevant decision maker's state of mind. As we have noted, that is what the primary judge correctly did: see [779]-[784] above.

3.2.2 Finding that LGFS did not need to prove reliance on any of the ABN Representations

930. ABN Amro submitted on appeal that the primary judge held that LGFS did not need to prove reliance on any of the ABN Representations in order to establish causation.

931. In particular, ABN Amro submitted that the primary judge's reasoning in J[3174] (from the third sentence of that paragraph) was as follows:

1. ABN Amro's knowledge of the flaws in S&P's AAA rating was such that, unless it disclosed those flaws, it could not have deployed the rating without engaging in misleading conduct;

2. Accordingly, for causation purposes, the relevant counterfactual was what would LGFS have done had ABN Amro, when it provided the rating to LGFS, also disclosed to LGFS the flaws of which it was aware in the rating; and

3. Had that occurred, LGFS would not have purchased the Rembrandt 2006-3 notes.

ABN Amro submitted that reasoning was incorrect and wholly inconsistent with the basic principle of causation that the impugned conduct must be shown to have been at least one of the decisive considerations in LGFS purchasing the notes.

932. Again, ABN Amro misconstrued the primary judge's reasons. The point made by the primary judge at J[3174] was that in the circumstances of ABN Amro's use of the rating and explanation of it (see [813] above), it was likely that LGFS relied on both the rating and the ABN Representations. The point made by the primary judge at J[3174] was that LGFS had to prove that it relied on both the rating (a fact ABN Amro accepted was proved) and on the ABN Representations, but that once reliance on the rating was established, it was readily established, by the probabilities and Mr Hilder's evidence, that LGFS also relied on the ABN Representations relating to the rating. In the circumstances, that conclusion was not only open but inevitable.

933. The two stage enquiry described in Part 4 , Section 3.1 above – factual causation and scope of liability – was satisfied.

3.3 Alternative Universe Contention

934. ABN Amro submitted that to establish causation on each of its claims against it, including the Second Duty, LGFS also had to prove, on the balance of probabilities, that, absent ABN Amro's impugned conduct, it would have taken some other, more beneficial course of action than purchasing the Rembrandt 2006-3 notes. At trial, the primary judge rejected ABN Amro's submission that LGFS had failed to prove this: J[3177].

935. We reject ABN Amro's contentions for the reasons set out at [786]- [790] above.

4. CONTRACTUAL CLAIMS OF LGFS AGAINST ABN AMRO

4.1 Introduction

936. This section of the judgment concerns the Mandate Letter: see [83]-[84] above. The Mandate Letter was relevant to the Rembrandt 2006-3 notes, not the Rembrandt 2006-2 notes. LGFS'

contractual claim was made by way of cross-claim against ABN Amro in the Bathurst Proceedings. However, by its nature, it is an independent cause of action.

937. The primary judge held that, by s 12ED of the *ASIC Act* , three terms were to be implied into the Mandate Letter: J[3220]-J[3236]. ABN Amro appealed against that finding, contending that two of the terms should not have been implied, that ABN Amro did not breach any of the implied terms and, finally, that ABN Amro's alleged breaches of the implied terms did not cause loss to LGFS: ABN Amro Appeal Grounds Matrix Rows 98D-98G.

938. The terms which the primary judge (at J[3220]-J[3227]) found to be implied into the Mandate Letter by s 12ED of the *ASIC Act* were that:

1. ABN Amro would render its services with due care and skill;

2. ABN Amro would structure and arrange the notes so that they would be reasonably fit for the purpose of being held by LGFS or the Councils to whom LGFS might sell the notes as investments with a high degree of security commensurate with a AAA rating; and

3. ABN Amro would structure and arrange the Rembrandt 2006-3 notes so that they might reasonably be expected to have a degree of security commensurate with a AAA rating.

ABN Amro accepted that the Mandate Letter contained the first implied term. It challenged the statutory implication of the other two terms by the operation of s 12ED(2) of the *ASIC Act* .

4.2 Legislation

939. Sections 12ED(1) and (2) of the *ASIC Act* provides:

> (1) In every contract for the supply of financial services by a person to a consumer in the course of a business, there is an implied warranty that:
>
> (a) the services will be rendered with due care and skill; and
>
> (b) any materials supplied in connection with those services will be reasonably fit for the purpose for which they are supplied.
>
> (2) If:
>
> (a) a person supplies financial services to a consumer in the course of a business; and
>
> (b) the consumer, expressly or by implication, makes known to the person:
>
> (i) any particular purpose for which the services are required; or

(ii) the result that he or she desires the services to achieve;

there is an implied warranty that:

(c) the services supplied under the contract for the supply of the services; and

(d) any materials supplied in connection with those services;

will be reasonably fit for that purpose or are of such a nature and quality that they might reasonably be expected to achieve that result, except if the circumstances show that the consumer does not rely, or that it is unreasonable for him or her to rely, on the person's skill or judgment.

940. It was not disputed that LGFS was a "consumer" for the purposes of s 12ED of the *ASIC Act* and that the other requirements of the section were satisfied. ABN Amro's position at trial and on appeal was that the second and third terms should not have been implied.

4.3 ABN Amro's contentions on appeal and analysis

941. The basis of ABN Amro's submission that the second and third terms should not have been implied into the Mandate Letter was that:

> LGFS made [it] known to [ABN Amro] that it required the notes to be rated AAA by S&P. However, …, it does not follow from this that LGFS made [it] known to [ABN Amro] that the purpose for which [ABN Amro's] modelling and structuring services were required, or the result LGFS desired the services to achieve, was to ensure that the notes had a degree of security commensurate with any AAA rating S&P gave them.

942. In other words, by the Mandate Letter (see [83]-[84] above), the services provided by ABN Amro were limited to what might be described as mechanical or perfunctory aspects of causing the notes to be issued and, second, the purpose of ABN Amro's services did not relevantly include creating a note having a degree of security commensurate with a AAA rating. We reject those contentions.

943. First, ABN Amro's alleged "limited" scope of its services was inconsistent with the proper construction of the Mandate Letter: see [83]-[84] including, in particular, the title to the Mandate Letter, the chapeau, and cl 1.2.1, and [845]-[851] above. ABN Amro's role was not simply to produce a CPDO with defined features, one of which was that it was expected to be rated AAA by S&P. ABN Amro promised to "model and structure" the "Transaction", which included both the creation of the Rembrandt 2006-3 notes and the issue of the notes. The services promised by ABN Amro were all the services required to create the notes. The (or at least a) substantial purpose of the services was the creation of the notes with a degree of security commensurate with a AAA rating, as required by LGFS.

944. ABN Amro's contention that the purpose for which its services were required, or the result they were to achieve, was *not* to ensure that the Rembrandt 2006-3 notes had a sufficient

degree of security to obtain that rating was, as the primary judge stated, "illusory": see J[3227], [813] and [846] above. LGFS made it plain to ABN Amro that it required a product (and thus services to structure a product) which had a AAA rating. LGFS did not require a label, it required a product with certain characteristics, in particular a risk of loss commensurate with a AAA rated product: J[1167]. LGFS made known to ABN Amro the matters referred to in s 12 ED(2)(b). That is consistent with the term sheet attached to the Mandate Letter, which described the notes as "expected to receive a full AAA rating from S&P".

945. The primary judge was correct to conclude that all three terms were implied.

4.4 Breach of contractual obligations

946. ABN Amro submitted that the primary judge made two errors in finding that ABN Amro breached the implied terms: ABN Amro Appeal Grounds Matrix Rows 98H. The first error depended on acceptance of ABN Amro's construction of the services it promised to provide LGFS. ABN Amro's construction was not accepted: see section 4.3 above. Consequently ABN Amro's first argument fails.

947. ABN Amro's second argument in relation to breach was that, because of S&P's AAA rating of the notes, ABN Amro had reasonable grounds to believe that the notes possessed a degree of security commensurate with a AAA rating. That argument fails for two reasons. First, ABN Amro's belief as to the adequacy of S&P's rating or of the security of the notes is irrelevant to the inquiry whether the implied terms have been breached. The implied terms are breached if (a) ABN Amro reasonably believes that the services were fit for purpose (to use a shorthand expression) but (b) the services were not fit for purpose. Section 12ED is directed to the fact of lack of fitness not to the supplier's state of mind. Second, for the reasons set out in Part 3 above, ABN Amro knew or ought reasonably to have known that the rating was unreliable.

4.5 Loss and Damage

948. On appeal and for the first time, ABN Amro submitted that the principles to be applied in determining whether LGFS had proved loss or damage in its contract case were different from those in tort or under the statutory provisions: see [437] above. The fact that this was raised for the first time on appeal reflected "the fact that the argument on this issue at trial was somewhat misdirected as a result of both parties' failure to identify the correct starting point".

949. The starting point for assessing damages in relation to LGFS' contract claim was not in dispute – what would have happened if ABN Amro had performed the terms of the Mandate Letter: *Wenham v Ella* (1972) 127 CLR 454 at 460 and 471 and *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64 at 80, 98, 117, 134, 138 and 161.

950. Two questions arise. First, what was the correct counterfactual and, second, having identified the correct counterfactual, what was the proper assessment of damages?

951. ABN Amro's case on appeal was that LGFS failed to prove what would have happened if ABN Amro had performed the terms of the Mandate Letter: ABN Amro Appeal Grounds Matrix Row 98H. ABN Amro submitted that had it performed the Mandate Letter in accordance with its terms, it would have modelled and structured the Rembrandt 2006-3 notes so that they had a level of security commensurate with a AAA rating (or, at least, so that ABN Amro had reasonable grounds for believing they had such a level of security). To illustrate its

point, it contended that the counterfactuals may have involved the notes having lower leverage, or a reduced coupon, or both. Or it may have involved them having some other combination of modified features. ABN Amro submitted that the evidence did not disclose what LGFS would have done had the notes been in some modified form and did not disclose how the notes, with those features, would have performed during the global financial crisis (**GFC**). ABN Amro's point was that a AAA rating was and is no guarantee of success, and even notes with a degree of security commensurate with such a rating may have failed in the hostile market conditions of that time.

952. These contentions are rejected. The correct counterfactual is that the notes would not have been issued because it was impossible to structure a CPDO which justified a AAA rating. The modelling runs showed that with stressed (or historically based) assumptions the notes had a much greater risk of default than commensurate with a AAA rated instrument: see [216] above and J[174], J[184] and J[334]. The probability of default was further increased once the other errors were taken into account, including the assumed roll down benefit: see [505] and [558] above. If the notes were not rated AAA, then LGFS would not have bought the notes or suffered a loss, and ABN Amro likely would not have marketed the notes. The primary judge properly assessed LGFS' loss and damage as the difference between the price it paid for the Rembrandt 2006-3 notes less the amount it received when it sold them to LGSS on 20 March 2008: see [969] below.

953. The other possible counterfactual is that ABN Amro structured a note with a probability of default commensurate with a AAA rating. That was improbable: see Part 3 above. In any event, if ABN Amro had structured such a note, it would have had different characteristics from the Rembrandt notes, including, at very least, a lower coupon. The evidence does not suggest that such a product would have been attractive to LGFS or the Councils.

PART 6: LGFS AGAINST ABN AMRO AND S&P FOR LOSSES ON LGFS' RETAINED NOTES

1. INTRODUCTION

954. There were two purchases of notes by LGFS – Rembrandt 2006-2 and Rembrandt 2006-3: see Part 2 , Sections 6-8 above. The matters considered in Parts 4 and 5 were relevant to both purchases. Part 6 deals with Appeal Grounds raised by both ABN Amro and S&P that relate to the LGFS Retained Notes – some $26 million of the Rembrandt 2006-3 notes not sold to the Councils but which LGFS sold to LGSS on 22 March 2008. Part 7 will deal with Appeal Grounds raised by both ABN Amro and S&P that relate to the Rembrandt 2006-2 notes issued to StateCover.

2. APPEAL GROUNDS

955. ABN Amro and S&P raised three matters on appeal against LGFS:

1. To establish causation on each of its claims, LGFS had to prove on the balance of probabilities that, absent the impugned conduct, it would have taken some other more beneficial course (the **Alternative Universe Contention**): ABN Amro Appeal Grounds Matrix Rows 85A-85D and S&P Appeal Grounds Matrix Rows 50A-50B;

2. LGFS' claim on the LGFS Retained Notes infringed the "rule" in *Potts v Miller* (1940) 64 CLR 282: ABN Amro Appeal Grounds Matrix Rows 89A-89B and S&P Appeal Grounds Matrix Rows 47A, 48A, and 51A; and

3. LGFS was contributorily negligent in connection with its loss on the LGFS Retained Notes.

956. The Alternative Universe Contention was addressed at [786]-[790] and [934]-[935] above. It is rejected for those reasons.

957. We turn then to the remaining Appeal Grounds.

3. *POTTS v MILLER*

3.1 Introduction

958. At trial and on appeal, ABN Amro and S&P submitted that LGFS failed to prove its loss because it had adopted an alternative approach to the "rule" in *Potts v Miller*. In particular, each submitted that LGFS had impermissibly claimed its loss was the difference between the price it paid for the Rembrandt 2006-3 notes less the amount it received when it sold them to LGSS on 20 March 2008 (see [955] above) without establishing that this would not result in it being overcompensated. The primary judge concluded that LGFS had not failed to prove its loss: J[3452]-J[3463].

959. ABN Amro and S&P contended that there were two findings which underpinned the primary judge's reasoning. First, that the extreme spread widening which accompanied the GFC and led to the Rembrandt 2006-3 notes cashing out was *not* a supervening or extraneous event (J [3454]-J[3458]) and, second, that as a consequence of the impugned conduct of ABN Amro and S&P, LGFS was effectively "locked in" to the purchase of the notes until it cashed out by sale to LGSS: J[3459]-J[3462]. ABN Amro and S&P challenged these findings on appeal.

3.2 Analysis

960. **Following paragraph cited by:**

Stav Investments Pty Ltd v Taylor (09 March 2022) (Ward CJ in Eq)
In the matter of Mediation & Online Dispute Resolution Operating Network Pty Ltd (23 February 2022) (Rees J)
DIF III - Global Co-Investment Fund LP v Babcock & Brown International Pty Limited (13 May 2019) (Ball J)

268. However, as the defendants recognise, the rule in *Potts v Miller* is not an inflexible one. In assessing the true value as at the date of acquisition, the Court may take into account subsequent events which shed light on the true value as at that date: *HTW Valuers (Central Qld) Pty Ltd v Astonland Pty Ltd* (2004) 217 CLR 640; [2004] HCA 54 at [38]-[39]. Moreover, in some cases it may be more appropriate to assess damages at the date of trial, such as where the asset is not readily saleable: see *ABN AMRO Bank NV v Bathurst Regional Council* (2014) 224 FCR 1; [2014] FCAFC 65 at [

960] ff; *Wyzenbeek v Australasian Marine Imports Pty Ltd (No 2)* [2018] FCA 1517 at [224] ff per Derrington J.

The Appeal Grounds fail. ABN Amro and S&P's contentions are inconsistent with both applicable legal principles and the facts. It is important to understand that neither ABN Amro nor S&P contended that different principles were to be applied in determining whether LGFS had proved loss or damage in tort or under the statutory provisions and neither contended that a different result would or should have followed if the proper principles were applied. Rather, in the circumstances of the current appeal, it is sufficient to observe that the "true measure" of LGFS' loss is the amount which represents the prejudice or disadvantage suffered by LGFS as a result of it altering its position in reliance on the misleading representations of each of ABN Amro and S&P: *HTW Valuers (Central Qld) Pty Limited v Astonland Pty Limited* (2004) 217 CLR 640 at 656-659 [35]-[40] and *Gates v City Mutual Life Assurance Society Limited* (1986) 160 CLR 1 at 12.

961. We have stated the "true measure" of LGFS' loss in those terms because it reflects, accurately, the position LGFS found itself in as a result of the impugned conduct of ABN Amro and, separately, the impugned conduct of S&P. It is important to understand why that proposition was stated in those terms and where it sits with the so-called "rule" in *Potts v Miller* .

962. The position was explained by the High Court in *HTW Valuers* . In that case, the argument on appeal was that the correct measure of damages, apart from consequential losses, was to deduct the value of the asset acquired at the date of acquisition from the purchase price and in assessing that value to bear in mind post-acquisition events. The Court's response to that argument (at 656-659 [35]-[40]) was and remains important:

> 35. [(1)] The approach of subtracting value from price is commonly employed where the acquisition of land, chattels, businesses or shares is induced by deceit. It has also been commonly employed under s 82 of the [TPA]. It is sometimes described as the rule in *Potts v Miller* . [(2)] Even in the areas in which that approach is often applied, and even apart from cases in which consequential losses have been recovered, the "rule" is not universal or inflexible or rigid. This perception is not novel. It has existed at least since the judgment of Dixon J in *Potts v Miller* and has been quite plain since that of Gibbs CJ in *Gould v Vaggelas*. Even Jordan CJ, who called the rule "well settled", acknowledged that it was only a "rule of practice". The flexibility of the rule can be seen by reference to a number of its characteristics.
>
> 36. One key qualification of the rule which prevents it from being inflexible is that the test depends *not* on the difference between price and "market value", but price and "real value" or "fair value" or "fair or real value" or "intrinsic" value or "true value" or "actual value" or what the asset was "truly worth" or "really worth" or "what would have been a fair

price to be paid ... in the circumstances ... at the time of the purchase". This distinction is sometimes difficult to draw, but it is old and fundamental.

37. A second qualification flows from the first. The distinction between a value which answers one of the tests just stated and market values means that market values – the prices actually obtainable in market sales - may be disregarded if they are "delusive or fictitious" because they are the result of "a fraudulent prospectus, manipulation of the market or some other improper practice on the part of the defendant". There are other reasons why the law does not limit recovery by reference to market value – the amount for which the plaintiff might have sold the assets acquired. One is that, subject to mitigation issues, the plaintiff is "not bound to sell them". Another is that there may not be a market. Another is that the market is mistaken on some basis other than manipulation. It is common to speak of shares being undervalued (or overvalued) by the market.

…

39. In the same way, in *Kizbeau Pty Ltd v W G & B Pty Ltd* this Court pointed out that, in many fields of law, assessments of compensation or value at one date are commonly made taking account of all matters known by the later date when the court's assessment is being carried out. … The limpid words of Lord Macnaghten about the duty of an arbitrator in determining compensation are far too well known to escape repetition:

> Why should he listen to conjecture on a matter which has become an accomplished fact? Why should he guess when he can calculate? With the light before him, why should he shut his eyes and grope in the dark?

The significance of *Kizbeau Pty Ltd v W G & B Pty Ltd* is that it endorsed that approach in relation to s 82 of the [TPA] when the court is assessing damages by comparing the price and the real value of the asset at the date of the acquisition.

40. Finally, although the court is entitled to take into account events after the date of acquisition, it must distinguish among possible causes of the decline in value of what has been bought. "If the cause is inherent in the thing itself, then its existence should be taken into account in arriving at the real value of the shares or other things at the time of the purchase. If the cause be 'independent', 'extrinsic', 'supervening' or 'accidental', then the additional loss is not the consequence of the inducement".

(Material in brackets and emphasis added. Footnotes omitted).

963. **Following paragraph cited by:**

Stav Investments Pty Ltd v Taylor (09 March 2022) (Ward CJ in Eq)

Addenbrooke Pty Ltd v Duncan (No 2) (16 May 2017) (Dowsett, Gilmour and White JJ)

664. Secondly, s 12GM of the ASIC Act (like its counterpart, s 237 of the Australian Consumer Law (*Competition and Consumer Act 2010* (Cth), Sch 2)) is not confined by the common law principles concerning causation of loss and recovery of damages. It vests the Court with flexible powers to craft an appropriate remedy. As was observed by the Full Court in *ABN AMRO* at [963] :

> 963. A number of matters are worth stating. … subject to the loss being proved, the approach to assessment must be flexible and "best adapted to give the injured claimant an amount which will most fairly compensate for the wrong suffered" provided that it works no injustice: *Ingot Capital Investments* at [171] ; *Henville v Walker* (2001) 206 CLR 459 at [131] and *HTW Valuers* at [65] . … causation and damages are closely linked: *Ingot Capital Investments* at [172] . … no less importantly, where property has been acquired in reliance on misrepresentations, there will be many cases where the losses are *not* represented by the difference between the price and the value of the asset *at the time of purchase*: see *HTW Valuers* at [35]-[40] ; *Ingot Capital Investments* at [176]-[180] and [190] ; and *Smith New Court Securities Ltd v Citibank NA* [1997] AC 254 at 266. The circumstances in which that last group of cases might arise are not closed.

(Emphasis in the original)

Choo v Zhang (05 August 2016) (McColl and Basten JJA, Sackville AJA)

A number of matters are worth stating. First, LGFS had the burden of proving its loss or damage. Second, subject to the loss being proved, the approach to assessment must be flexible and "best adapted to give the injured claimant an amount which will most fairly compensate for the wrong suffered" provided that it works no injustice: *Ingot Capital Investments* at 684 [171]; *Henville v Walker* (2001) 206 CLR 459 at 502 [131] and *HTW Valuers* at 667 [65] . Third, causation and damages are closely linked: *Ingot Capital Investments* at 684 [172]. Fourth, and no less importantly, where property has been acquired in reliance on misrepresentations, there will be many cases where the losses are *not* represented by the difference between the price and the value of the asset *at the time of purchase*: see *HTW Valuers* at 656-659 [35]-[40] ; *Ingot Capital Investments* at 685-686 [176]-[180] and 688 [190] and *Smith New Court Securities Ltd v Citibank NA* [1997] AC 254 at 266. The circumstances in which that last group of cases might arise are not closed.

964. It is against that background that it is necessary to address the submissions of ABN Amro and S&P. First, they described the "rule" in *Potts v Miller* as being that where a plaintiff has been induced by deceit to purchase an asset, the *proper measure* of the plaintiff's loss is the difference between the price the plaintiff paid for the asset and its true value *at the time of purchase* (*HTW Valuers* at 656-657 [34]-[35]) and then submitted that the *rule* is appropriate for the assessment of damages under s 82 of the TPA (and its analogues) where misleading

conduct has induced a person to purchase an asset: *HTW Valuers* at 656-657 [35] . Second, although commonly employed, the "rule" in *Potts v Miller* is not "universal or inflexible or rigid": *HTW Valuers* at 656-657 [35] . Third, under provisions such as s 82 of the TPA , other approaches to the assessment of damages are permissible, provided they will not result in the plaintiff being overcompensated: *HTW Valuers* at 666-667 [63] and 667-668 [65] .

965. Fourth, a primary reason for the common adoption of the so-called "rule" in *Potts v Miller* was to separate out losses resulting from extraneous factors in the later history of the asset: *HTW Valuers* at 667-668 [65] . In support of that contention, they referred to Gleeson CJ's statement in *Henville* at 471-472 [24]-[25] that:

> [24] Although there has been some discontent with its apparent rigidity, a primary reason for the general principle that damages in deceit, where there has been a fraudulent inducement to acquire shares in a company, are measured by the difference in the value of the shares at the time of acquisition and the price paid for them, is the need to separate out losses resulting from extraneous factors in the later conduct of the company's business. *Peek v Derry* [(1887) 37 Ch D 541] was a case concerning shares in a tramway company that were taken up on the faith of a false prospectus. Cotton LJ said [at 592]:
>
>> Neither can the Plaintiff get the benefit of any loss or depreciation in the shares which was occasioned by subsequent acts. If the company at the time was a good company and the shares had an intrinsic value, then no fact which subsequently occurred, as for instance, some Act of Parliament being passed to prevent such tramways from using steam-power, or anything else, ought to add to the damages to be paid by the Defendants ...
>
> [25] Later, his Lordship referred to "events injurious to the company, which occurred not from intrinsic defects in it, but from events which happened after the purchase", which "cannot be taken into account" [at 593].
>
> (Some footnotes omitted.)

966. The contention was that losses resulting from extraneous events were to be separated out because they were not the reasonable consequence of the impugned conduct and so the defendant should not be held liable for them. So much may be accepted. As Dixon J said in *Potts v Miller* at 298 :

> The reason given for the rule is that, if, after the date of purchase, the thing which the plaintiff was induced to buy loses in value owing to accidental or extrinsic causes, that loss is not the reasonable consequence of the inducement. "It is not enough to say that but for the misrepresentation or fraud the purchaser would never have bought, and therefore would not have lost the thing bought. To recover back the whole price, if the thing had any value when bought, he must be in a condition to rescind the bargain and replace it, which here the plaintiff is not, as it is not in his power to make the company take back the shares, or in the power of the company to resume them.

If a man is induced by misrepresentation to buy an article and while it is still in his possession it becomes destroyed or damaged, he can only recover the difference between the value as represented and the real value at the time he bought. He cannot add to it any further deterioration which has arisen from some other supervening course" (per *Cockburn* CJ in *Twycross v Grant* [(1877) 2 CPD at 544]).

967. Fifth, ABN Amro and S&P asserted that another reason for adopting the "rule" in *Potts v Miller* was that its application required a difficult distinction to be drawn between causes of loss or diminution in the value of the relevant asset which are extraneous, and those causes which are inherent in the asset itself. And, that in drawing that distinction, assistance is to be gained by bearing in mind that what underlies it is the notion that diminution in the value of an asset from inherent causes can properly be taken into account in assessing the asset's true value as at the date of its acquisition, whereas diminution in value from extraneous causes cannot: *Kizbeau Pty Ltd v WG & B Pty Ltd* (1995) 184 CLR 281 at 291.

968. Finally, ABN Amro and S&P asserted that, as a separate exercise, it was and remained necessary to separate out losses or diminution in the true value of the asset resulting from extraneous events, even where the purchaser retained the asset as a result of the impugned conduct (e.g., because there was no market for it).

969. **Following paragraph cited by:**

Re DCA Enterprises Pty Ltd (23 January 2023) (Black J)
Stav Investments Pty Ltd v Taylor (09 March 2022) (Ward CJ in Eq)
In the matter of Mediation & Online Dispute Resolution Operating Network Pty Ltd (23 February 2022) (Rees J)
Addenbrooke Pty Ltd v Duncan (No 2) (16 May 2017) (Dowsett, Gilmour and White JJ)

Each of these propositions repays careful analysis. The premise which underpins each appears to be that the "rule" in *Potts v Miller* is the default position or starting point. If that is the premise, we reject it. Labelling it a "rule" is unhelpful and dangerous. It is unhelpful and dangerous because inevitably the wrong question is asked: namely is the "rule" in *Potts v Miller* satisfied rather than asking the more fundamental questions – what are the facts, do those facts establish a compensable loss and if so, what was its true measure? Put at its highest, *Potts v Miller* points to considerations which *may*, *not must*, bear upon the assessment of that "true measure". In the present appeal, the onus was and remained on LGFS to prove its loss: *Banque Bruxelles Lambert S.A. v Eagle Star Insurance Co Ltd* [1997] AC 191 at 218D-F (Lord Hoffmann). In the circumstances of this case, the "true measure" of LGFS' loss was the amount which represented the prejudice or disadvantage suffered by LGFS as a result of it altering its position in reliance on the misleading representations of each of ABN Amro and S&P, namely the amount paid by LGFS for the notes less the amount received when it sold the LGFS Retained Notes to LGSS.

970. Next, the distinction that ABN Amro and S&P would have the Court draw between the "true value" or "real value" of the asset, as distinct from its "market value", as at the time of

purchase (see [964] above) is inapposite. At the heart of this contention was the submission that focus on the "true value" or "real value" of the asset preserved the flexibility of the "rule" in *Potts v Miller* , and meant that it remained an appropriate measure of loss even in circumstances where the market value of the asset is "delusive or fictitious" (as such market values may be disregarded) or there is no market for the asset at all: *HTW Valuers* at 657-658 [36]-[37] . That submission does not assist. The focus on "true" or "real" value *at the time of purchase* is interesting but irrelevant in answering the more fundamental questions in assessing LGFS' loss or damage.

971. **Following paragraph cited by:**

In the matter of Mediation & Online Dispute Resolution Operating Network Pty Ltd (23 February 2022) (Rees J)

113. Ipp JA referred at [178] (citing *Smith New Court Securities Ltd v Citibank NA* [1997] AC 254 at 266 (Lord Browne-Wilkinson) to the rationale for the departure from the rule as *inter alia* necessary to give adequate compensation for the wrong done to the plaintiff, in particular where the fraud continues to influence the conduct of the plaintiff after the transaction is complete or where the result of the transaction induced by fraud is to lock the plaintiff into continuing to hold the asset acquired. Further, in *ABN AMRO* at [971] , [983] , the Full Court observed that *Potts v Miller* has no application where the misrepresentations have and continue to have operative effect. The plaintiffs submitted that these principles were applicable here. Their damages should be assessed as the difference between what they paid for their investments and the value of the investments following the failure of the Company.

The true comparator was between the price paid and the "real value" of the notes. The real value of the notes was what was paid on cash out (or sale to LGSS) because no-one knowing the true creditworthiness of the notes would have paid any more than that amount. And the fact that the loss is measured at that time (the time when the notes cashed out or sold and not at the time of purchase) is necessary because the decline in value was attributable to the notes themselves, not to an extrinsic event. That analysis demonstrates two further reasons why the so-called "rule" in *Potts v Miller* is inapposite in assessing the true measure of LGFS' loss. It would assess the measurable loss at the wrong date and would direct attention to an extrinsic event which did not exist thereby ignoring a loss inherent in the thing bought. As to the date, the correct point of comparison of the "true value" was when the representations ceased to have operative effect – here, the sale of the notes to LGSS. Next, the cause of the loss. Any assessment of the true measure of loss or damage requires identification, precise identification, of the losses or diminution in the true value of the asset and the events from which those identified losses or diminution in value were said to have resulted. Here, the questions posed by *Potts v Miller* are inapposite because, as we have explained when assessing the "scope of liability" or normative assessment of causation, the loss was caused by the inability of the notes, inconsistent with a AAA rating, to survive relatively rapid credit spread widening without mean-reverting in the short to medium term. That loss was attributable to the characteristics of the notes themselves (and the characteristic of the notes to which the negligent and misleading statement made by each of ABN Amro and S&P was directed), not an extraneous event: J[3417], J[3427] and J[3455]- [3456]. The primary judge was correct to conclude that in those circumstances, the true measure of LGFS' loss is the amount paid by LGFS for the notes less the amount it received on the notes being sold to LGSS: J[3462].

972. What then of these so-called "extraneous factors" referred to by ABN Amro and S&P? The submission was that where a plaintiff has been induced by misrepresentation to purchase an asset, an alternative to the so-called "rule" in *Potts v Miller* is to measure the plaintiff's loss as the difference between the price it paid for the asset and the benefit left in the plaintiff's hands at trial but that that alternative was not likely to be an appropriate approach (because it will result in the plaintiff being overcompensated) where the value of the asset has been diminished by extraneous factors and/or where the plaintiff has not been locked into the asset by the continuing effect of the misrepresentation or the asset not being saleable: *HTW Valuers* at 667-668 [65]-[66] . As we have just said, in the circumstances of this appeal, that analysis is inapposite. LGFS' loss was attributable to the characteristics of the notes themselves (and the characteristic of the notes to which the negligent and misleading statements made by each of ABN Amro and S&P was directed), not an extraneous factor.

973. However, it is necessary to address the so-called "extraneous factors", relied on by ABN Amro and S&P and providing the basis for their Appeal Grounds.

3.3 Extreme spread widening accompanying the GFC

974. The primary judge concluded at J[3454] that "it cannot be accepted that the GFC, which from the point of view of the performance of the notes was simply an example of sustained spread widening being a risk central to the assessment of the creditworthiness of the notes, may be ... characterised [as a supervening or extraneous event]": see also J[3417] and J[3427].

975. ABN Amro and S&P submitted that the finding was incorrect for four reasons:

1. The basal reason for the finding – that the extreme spread widening which accompanied the GFC and led to the Rembrandt 2006-3 notes cashing out was simply an example of sustained spread widening which was central to S&P's assessment of the creditworthiness of the notes – was factually incorrect.

2. The primary judge was in error to conclude (at J[3455]), in relation to the spread widening which accompanied the GFC, that "[t]his is an example of the principles discussed in *HTW Valuers* at [658-659] [38]-[40] that the real value of an asset may be assessed having regard to subsequent events if those subsequent events do no more than expose what was inherent in the asset in the first place".

3. The primary judge was also in error to conclude (at J[3456]-J[3458]) that the losses sustained by LGFS on the downgrade and cash out of the Rembrandt 2006-3 notes were causally related "to S&P's and [ABN Amro's] negligent misrepresentations" in a way which went beyond the mere fact that, absent those misrepresentations, LGFS would not have purchased the notes.

4. The primary judge was incorrectly influenced (at J[3452], J[3453] and J[3458]) by a belief that the duties of care of ABN Amro and S&P were in some way analogous to that of the valuer in *Kenny & Good Pty Limited v MGICA (1992) Limited* (1999) 199 CLR 413.

976. In the context of the LGFS Retained Notes, none of these matter because LGFS' loss was occasioned by the intrinsic defects in the notes, defects which both ABN Amro and S&P represented to be otherwise. LGFS suffered the loss that it did because the notes were not as represented. The event which brought home the inaccuracies of those representations is properly not described as an independent extraneous event causing LGFS' loss. It was, as the primary judge said, "an example of the principles discussed in *HTW Valuers* at [38]-[40] that the real value of an asset may be assessed having regard to subsequent events if those subsequent events do no more than expose what was inherent in the asset in the first place". That event was not the GFC. That event was the inability of the notes, inconsistent with a AAA rating, to survive relatively rapid credit spread widening without mean-reverting in the short to medium term. That loss was attributable to the characteristics of the notes themselves, not an extraneous event.

977. Further, in any event, LGFS sold the LGFS Retained Notes on 20 March 2008 to LGSS: see [958] above. Although what was the start of the GFC is the subject of much debate, when LGFS sold the LGFS Retained Notes, the collapse of Lehman Brothers on 15 September 2008 was still six months away.

3.4 LGFS effectively "locked in"?

978. That leads to the second alleged "error" relied upon by ABN Amro and S&P, namely that the primary judge erred in finding that, as a consequence of the impugned conduct of ABN Amro and S&P, LGFS was effectively "locked in" to the purchase of the notes until they cashed out by sale to LGSS: J[3459]-J[3462].

979. The primary judge held that LGFS was "locked in" to its purchase of the Rembrandt 2006-3 notes for two reasons – first, because ABN Amro's (and S&P's) impugned conduct as to the creditworthiness of the notes continued to operate until shortly before LGFS sold them to LGSS (see J[3419], J[3422]-J[3424] and J[3459]) and, second, because even if that conduct was negatived at an earlier point in time, the notes were not a readily marketable asset: see J [[3426], J[3428] and J[3460]-J[3461]. On appeal, ABN Amro and S&P challenged each reason: ABN Amro Appeal Grounds Matrix Rows 89A-89B and S&P Appeal Grounds Matrix Row 53A.

3.5 Impugned conduct did not continue to operate

980. ABN Amro and S&P contended that their impugned conduct did not continue to operate on LGFS until shortly before it sold the Rembrandt 2006-3 notes to LGSS. First, they contended that the impugned conduct never had any effect on LGFS. That contention has been addressed earlier at [774]-[800] and [916]-[935] and is without foundation.

981. Next, they contended that, even if this was not so, any continuing effect of ABN Amro's impugned conduct on LGFS had come to an end by late February or early March 2007 when ABN Amro informed Mr Hilder that S&P was reviewing how it rated CPDOs, and that, accordingly, ABN Amro would not issue any further Rembrandt 2006-3 notes to LGFS. ABN

Amro contends that it ought to have been plain to Mr Hilder, from the fact that ABN Amro was declining to issue any further Rembrandt 2006-3 notes, that S&P's review at least called into question the reliability of its earlier AAA rating of the notes. The primary judge refused to accept this on the basis that Mr Hilder was not told, in terms, that S&P's original rating had been negligent or misleading: J[3424].

982. ABN Amro and S&P contended that in framing the issue that way, the primary judge misdirected herself. Instead, ABN Amro and S&P stated that what mattered was whether LGFS continued to rely on S&P's rating (since, if it did not, LGFS could not have been relying on ABN Amro's impugned conduct). In support of that contention, ABN Amro submitted that:

> Mr Hilder did not need to be told that the rating was negligent or misleading in order to stop relying on it. He was an experienced participant in financial markets, who knew that credit ratings addressed creditworthiness at a particular point in time and could change. To stop relying on S&P's rating, therefore, all Mr Hilder needed to know was that the rating had changed or was likely to change. The fact that [ABN Amro] was refusing to issue any more of the notes because of S&P's rating review was sufficient to convey this to him.

The "irresistible inference" they contend the primary judge should have drawn was that Mr Hilder (and by extension LGFS) did not rely on S&P's AAA rating (and, therefore, could not have relied on ABN Amro's impugned conduct) after late February or March 2007.

983. As we have explained at [971] above, *Potts v Miller* has no application where the misrepresentations have and continue to have operative effect. ABN Amro's and S&P's submission fails because LGFS not only relied on both the ABN Representations and the S&P Representations but both sets of representations had a continuing effect on LGFS: see [980] above. That leaves the facts set out at [981] above. There are two fundamental problems with the submission based on those facts. The submission misapplies *Potts v Miller* and it is factually inaccurate and incomplete.

984. ABN Amro told LGFS, in early 2007, that S&P was reviewing how it rated CPDOs: see [981] above. That is not in dispute. However, that statement must be considered in context, not in isolation. What then was the context? It included that (a) the rating of the Rembrandt notes had not been downgraded and remained AAA at the time of ABN Amro's statement and thereafter (see [142] above) (b) ABN Amro did not disclose what it knew about the rating (see [981] above) (c) ABN Amro did not suggest the rating was unreliable (see [981] above) and (d) ABN Amro did not challenge on appeal the primary judge's finding at J[3420] that the events before the downgrade did not affect LGFS' ongoing belief that the rating was reliable.

985. Put simply, *Potts v Miller* had no application because LGFS did not know the representations were misleading.

986. S&P adopted a different position about the so-called end point in relation to the continuing representations: S&P Appeal Grounds Matrix Rows 55A-56A. It contended that the primary judge erred in failing to find that the AAA rating operated as a continuing representation only until the Rembrandt 2006-3 notes were (a) placed on "CreditWatch Negative" or (b) downgraded to BBB+. Two matters should be noted. The substance of S&P's complaint is the same as ABN Amro's. S&P simply adopted two alternative end points. Second, in

support of these alternative end points, it relied upon ABN Amro's submissions. It is dismissed for the same reasons: see [980]-[985] above.

3.6 LGFS able to sell to ABN Amro

987. The other matter relied upon by ABN Amro and S&P was that LGFS was able to sell the Rembrandt 2006-3 notes to ABN Amro. It was common ground that, pursuant to the Rembrandt 2006-3 term sheet, ABN Amro was obliged to repurchase the notes from LGFS, if it so required, at a price which reflected supply and demand: see [84] above. There is a short answer to this contention. ABN Amro's promise to buy back was at market value: see [84] above. There is no reason to think that in an informed market the notes had any greater value than the price at which LGFS sold them (immediately following the downgrade).

988. Accordingly, for those reasons, ABN Amro and S&P's Appeal Grounds that the primary judge should have concluded that LGFS: (a) had not proved any loss in accordance with the "rule" in *Potts v Miller* and (b) had not established that it would not be overcompensated if its alternative approach were applied, fail.

4. CREDIT FOR INTEREST OR COUPON PAYMENTS?

989. That leaves the last contention that in assessing LGFS' "true measure" of loss, LGFS should give credit for the interest payments or coupon payments it received: ABN Amro Appeal Grounds Matrix Row 89C and S&P Appeal Grounds Matrix Row 49A. That contention is rejected. Contrary to S&P's contentions, labelling LGFS' claim as a "no transaction case" again obscures the more fundamental questions: see [969]-[971] above. LGFS suffered loss when it sold the notes. That was a loss of principal invested. There was no requirement to give credit for interest or coupon payments received before that date because those payments reflect a cost of money which LGFS would have earned, to some degree, in any event (e.g, if paid into a term deposit LGFS would have earned interest).

5. NOTICES OF CONTENTION – LGFS AND COUNCILS

990. By Notices of Contention, both LGFS and the PA Councils submitted that:

1. The Court should find that the principles for assessing and quantifying damages in *Potts v Miller* do not apply to LGFS' and the PA Councils' claim for damages against ABN Amro, S&P and LGFS (in the case of the PA Councils) because LGFS and the PA Councils would never have acquired an investment in the Rembrandt notes had the notes not been assigned a AAA rating by S&P: LGFS Appeal Grounds Matrix Row 127 and PA Councils Appeal Grounds Matrix Row 134; and]

2. In the alternative, if the Court finds that the principles in *Potts v Miller* apply, the Court should find that as at the date of acquisition, the Rembrandt notes had no value or a nominal value and damages should be calculated as the difference between zero and the purchase price paid by LGFS and the Councils, plus interest: LGFS Appeal Grounds Matrix Row 128 and PA Councils Appeal Grounds Matrix Row 135.

991. For the reasons at [954]ff, we reject the submissions.

6. LGFS CONTRIBUTORILY NEGLIGENT?

992. This is addressed in Part 13 below.

PART 7: LGFS' CLAIMS AGAINST ABN AMRO AND S&P IN RELATION TO SETTLEMENT WITH STATECOVER

1. INTRODUCTION

993. LGFS sued both ABN Amro and S&P on account of its payment to StateCover to discharge StateCover's claims against LGFS, ABN Amro and S&P arising from the Rembrandt 2006-2 notes, which were purchased by LGFS on StateCover's behalf: [SAF1]. The relevant facts are summarised at [76]- [78] above.

994. At trial, the primary judge found that:

1. S&P and ABN Amro had breached a duty of care owed to LGFS in relation to the Rembrandt 2006-2 notes: J[2993], J[2741]-J[2825], J[2925]-J[2956] and J [3179]-[3200];

2. S&P and ABN Amro had engaged in misleading conduct against LGFS in relation to the Rembrandt 2006-2 notes in contravention of ss 1041E and 1041H of the *Corporations Act* and s 12DA of the *ASIC Act* : J[2993] and J[3088]-J [3104];

3. LGFS suffered loss and damage as a result of S&P's and ABN Amro's breach of duty and contravention of ss 1041E and 1041H of the *Corporations Act* and s 12 DA of the *ASIC Act* : J[2837]-J[2882], J[2959]-J[2975], J[2984], J[2920]-J[2922], J[2993] and J[3167]-J[3178]; and

4. S&P and ABN Amro were liable to make equitable contribution to LGFS for LGFS' settlement of the StateCover proceedings: J[2991]-J[2992], J[2994] and J [3722].

995. S&P and ABN Amro appealed against these findings.

996. It is necessary to note certain aspects of the Rembrandt 2006-2 transaction. The term sheet for the Rembrandt 2006-2 transaction indicated that the characteristics of, and disclaimers applicable to, the Rembrandt 2006-2 notes were the same as for the Rembrandt 2006-3 notes with minor exception. Further, the primary judge found that the Mandate Letter did not apply to the Rembrandt 2006-2 notes: J[3234]. That finding was not challenged on appeal.

2. LIABILITY OF ABN AMRO TO LGFS

2.1 Tort Claims: ABN Amro Appeal Grounds Matrix Rows 59A, 77B and 78B

997. The primary judge found that ABN Amro owed LGFS a duty to exercise reasonable care and skill in providing to LGFS information and advice about the Rembrandt 2006-2 notes: J[3179]

-J[3200]. That duty was the same duty which ABN Amro owed to LGFS in relation to the Rembrandt 2006-3 notes. The primary judge found that ABN Amro breached its duty of care: J[3201]-J[3214].

998. ABN Amro challenged the primary judge's finding of the existence of a duty on the same bases as it did with respect to the Rembrandt 2006-3 notes: see [805]-[806] above. The nature of the differences between the Rembrandt 2006-2 transaction and the Rembrandt 2006-3 transaction meant that there were some subtle differences between ABN Amro's submissions in respect of the two but those differences do not materially alter the analysis. We therefore reject that challenge for the reasons at [807]-[838] and [852]-[860] above.

999. Similarly, and subject to one exception, ABN Amro's challenge to the primary judge's finding that it breached its duties also mirrored the arguments it made in relation to the Rembrandt 2006-3 notes: see [878] above. That exception was its submissions that there was no breach because "it cannot be doubted that the [Rembrandt 2006-2] notes, which had the new rebalancing method, would have rated AAA using either [15% or 25%] volatility" and that the Rembrandt 2006-2 notes "could have rated AAA at a starting spread as low as 28 bps (well below the level of around 32 bps which prevailed when the notes were issued". We have dealt with these submissions at [374]- [424] above. We reject ABN Amro's challenge to the primary judge's finding that it breached the duties it owed to LGFS in relation to the Rembrandt 2006-2 notes for the reasons at [879]-[906] above.

2.2 **Statutory Claims:** ABN Amro Appeal Grounds Matrix Row 60A

1000. The primary judge found that ABN Amro had engaged in misleading conduct in contravention of ss 1041E and 1041H of the *Corporations Act* and s 12DA of the *ASIC Act* for the same reasons as she had found it had done so in relation to the Rembrandt 2006-3 notes: see [913] -[915] above. ABN Amro challenged that finding for the same reasons it deployed in its challenge to the finding in relation to the Rembrandt 2006-3 notes: see [913]-[915] above. We reject that challenge for the reasons at [913]- [915] above.

2.3 **Causation:** ABN Amro Appeal Grounds Matrix Rows 64B, 79B and 81C

1001. The primary judge's findings on causation in relation to the claims brought by LGFS against ABN Amro applied to both the Rembrandt 2006-2 and the Rembrandt 2006-3 notes: see Part 5 , Section 3 above. ABN Amro challenged those findings on the same bases as it did with respect to the Rembrandt 2006-3 notes: see [916] above. In particular, ABN Amro submitted that:

1. LGFS failed to prove that, if it had not caused StateCover to purchase the Rembrandt 2006-2 notes, it would have caused StateCover to purchase an alternative product which would not have exposed LGFS to the same liability; and

2. LGFS' unlawful conduct was the real and essential cause of its liability to StateCover.

1002. We reject ABN Amro's challenge for the reasons at [916]-[935] and Part 4 , Section 1.1.4.4 above.

3. LIABILITY OF S&P TO LGFS

3.1 Tort Claims: S&P Appeal Grounds Matrix Rows 1A, 10B, 12E, 12G and 12I

1003. The primary judge found that S&P owed LGFS a duty to exercise reasonable care in forming, and to have reasonable grounds for, the opinion expressed by the rating: see J[2993] and [566] above. That duty was the same duty which S&P owed to LGFS in relation to the Rembrandt 2006-3 notes. The primary judge found that S&P breached that duty: J[2993].

1004. Subject to one exception, S&P challenged the primary judge's finding of the existence of a duty on the same bases as it did with respect to the Rembrandt 2006-3 notes: see [567] above. The exception was S&P's submission that the finding of a duty was "unsupported by the facts about the Rembrandt 2006-2 notes (as opposed to the Rembrandt 2006-3 notes)". S&P did not elaborate on this submission beyond directing the Court to its submissions with respect to LGFS and the PA Councils and stating that its submission was effectively that "it has not been proven on the balance of probabilities that the relevant indicia for imposition of a duty of care in relation to Rembrandt 2006-2 exist". We disagree and reject S&P's challenge to the primary judge's finding of the existence of a duty for the reasons at Part 4 , Section 1.1 above.

1005. Consistently with its position in relation to the Rembrandt 2006-3 notes, S&P did not appeal against the primary judge's finding that the rating was incorrect and, as a result, it had breached its duty.

3.2 Statutory Claims: S&P Appeal Grounds Matrix Rows 12B, 14B, 15B, 17B, 22B-22E, 23B, 26B, 27B and 30B

1006. The primary judge found that S&P had engaged in misleading conduct in contravention of ss 1041E and 1041H of the *Corporations Act* and s 12DA of the *ASIC Act* for the same reasons as she had found it had done so in relation to the PA Councils: see [1304] below. S&P challenged that finding for the same reasons it deployed in its challenge to the finding in relation to the PA Councils: see [1304]-[1308] below. We reject that challenge for the reasons at [1304]- [1308] below.

3.3 Causation: S&P Appeal Grounds Matrix Rows 31B, 32B and 38B

1007. The primary judge's findings on causation in relation to the claim brought by the PA Councils against S&P applied equally to LGFS in the StateCover proceedings: see J[2837]-J[2882], J [2959] and [1309] below. S&P challenged those findings for the same reasons as it did with respect to the PA Councils: see [1309] below. We reject that challenge for the reasons at [1309] below.

3.4 Loss and Damage: S&P Appeal Grounds Matrix Row 47B

1008. On appeal S&P raised the same issues and pressed the same arguments in relation to loss and damage as it did with respect to the PA Councils: see [1311]-[1312] below. We reject S&P's arguments for the reasons at [1311]- [1312] below.

4. EQUITABLE CONTRIBUTION

1009. The primary judge found that ABN Amro and S&P were each liable to make equitable contribution to LGFS for LGFS' settlement of the StateCover proceedings: J[2991]-J [2992]. Her Honour accepted that the principles which governed the question whether LGFS was entitled to equitable contribution were those expressed by the High Court in *HIH Claims Support Limited v Insurance Australia Limited* (2011) 244 CLR 72 at 87-90 [36]-[48] :

> [36] In [*Albion Insurance Co Ltd v Government Insurance Office (NSW)* (1 969) 121 CLR 342], Kitto J said the basic concept of contribution was longstanding and was "accepted by both law and equity as one of natural justice", expressed by ensuring equality between persons obliged in respect of a common obligation; although his Honour recognised that "the doctrine of equality operated more effectually in a court of equity". He described the basic principle thus: "persons who are under co-ordinate liabilities to make good the one loss … must share the burden pro rata".
>
> [37] The rationale for equitable contribution was explained by Eyre LCB in *Dering v Earl of Winchelsea*. Obligors (such as co-sureties) severally bound by different instruments in respect of the same liability, who may not even know of each other, have "a common interest, and a common burthen". It is because the charging of one surety in respect of the common obligation discharges the other that "each therefore ought to contribute to the *onus*". The equity of contribution does not apply between obligors where one of them is, in fact, a surety for a surety rather than a co-surety. The nature or quality of the obligations is critical although the quantum of liability between co-obligors may vary.
>
> [38] Co-ordinate liabilities are not limited to circumstances involving co-sureties, or to double insurance where two insurers each have a secondary liability in respect of the same risk; in the latter case "the two policies of insurance are treated as one insurance".
>
> [39] Given that natural justice, exemplified by equality, underpins the duty to contribute in respect of co-ordinate liabilities, the search for a common obligation "should not be defeated by too technical an approach". It is possible to have a common obligation where the obligation of each of two obligors has a different source, such as statute and contract, as occurred in *B P Petroleum Development Ltd v Esso Petroleum Co Ltd*, provided the obligations can be characterised as "of the same nature and to the same extent".
>
> [40] By way of contrast, the obligation of an indemnifier under a contract of services, and the obligation of an insurer which may cover the same event, have been held not to be obligations "of the same nature and to the same extent" because, as explained in *Caledonia*, liabilities incurred in tort, deceit or contract are generally primary whereas the liability of an indemnity insurer to an injured party is generally secondary.
>
> [41] In the Inner House decision upheld by the House of Lords in *Caledonia* , Lord Sutherland explained the rationale: "Contribution …. is a two way

exercise. You cannot have contribution from one without contribution from the other."

[42] As the requirement of co-ordinate liabilities is essential for the operation of the doctrine of equitable contribution between obligors, the duty to contribute is not based on "some general principle of justice, that a man ought not to get an advantage unless he pays for it".

[43] In *Burke v LFOT Pty Ltd* , a purchaser of retail premises suffered loss arising out of misrepresentations made by the vendor which were actionable under the *Trade Practices Act 1974* (Cth) , and also loss arising from the negligence of one of the directors of the purchaser who acted as the solicitor in relation to the purchase. The vendor and one of its directors failed to obtain contribution from the solicitor because the liabilities were not, as in *BP Petroleum*, "of the same nature and to the same extent". Accordingly, they were not co-ordinate liabilities in respect of a common obligation. The repayment to the purchaser by the vendor and its director of the difference between the price received and the true value of the premises did not command equity's intervention.

[44] The equitable doctrine that a duty to contribute applies where obligors are under a common burden or common obligation was restated by this Court in the plurality judgment in *Friend v Brooker*:

> "With a claim to contribution, as is the position generally with the intervention of equity to apply its doctrines or to afford its remedies, the plaintiff must show the presence of 'an equity' founding the case for that intervention. The 'natural justice' in the provision of a remedy for contribution is the concern that the common exposure of the obligors (or 'debtors') to the obligee (or 'creditor') and the equality of burden should not be disturbed or be defeated by the accident or chance that the creditor has selected or may select one or some rather than all for recovery …
>
> The equity to seek contribution arises because the exercise of the rights of the obligee or creditor ought not to disadvantage some of those bearing a common burden; the equity does not arise merely because all the obligors derive a benefit from a payment by one or more of them. As explained in United States authority, contribution is an attempt by equity to distribute equally, among those having a common obligation, the burden of performing it, so that without that common obligation there can be no claim for contribution."
>
> (Footnotes omitted.)

[45] The plurality went on to prefer the wider term "co-ordinate liabilities" said to subsume the expression "common obligation", and confirmed that "the doctrine is not enlivened merely because the claimant's payment operates to the financial benefit or relief of the other party".

[46] In that case, the first respondent, a director of a company, had claimed equitable contribution from a co-director in respect of loans he had made to the company, on the basis that the directors were parties to a common design to achieve a common end. The appellant successfully resisted the claim on the basis that the doctrine of equitable contribution should not be extended to "a common design" which would have the effect of "outflank [ing] the consequences of the selection by the parties of the corporate structure" for their business, which "brought with it the attendant legal doctrines of corporate personality and limited personal liability". The result confirms that equity will not intervene in the absence of a common legal burden or co-ordinate liabilities.

[47] The authorities show that no court has departed from the requirement that the equity to contribute depends on obligors bearing a common burden, the basis for co-ordinate liabilities in respect of the one loss. A proposition upon which the appellant wishes to rely – namely, that equity looks to substance rather than form – has never been invoked successfully to achieve a departure from, or modification of, that requirement.

[48] In terms of the abovementioned authorities, it was argued for the appellant that the facts of this case justified a "controlled departure" from Lord Sutherland's conception that contribution "is a two way exercise", since the plurality in *Friend v Brooker* concentrated upon equity addressing the "disadvantage" an obligee might cause to an obligor. However, as the passages quoted above show, the reference to "disadvantage" in *Friend v Brooker* is predicated on obligors bearing a common burden.

(Footnotes omitted.)

1010. The primary judge identified that the basal question in a claim for equitable contribution was whether the parties' liabilities were "of the same amount and to the same extent". That question was directed to identification of "the existence of a common obligation" and should not "depend on an overly technical approach": J[2992]. The primary judge found that the liabilities of LGFS, ABN Amro and S&P to StateCover were "co-ordinate" in the sense that StateCover "suffered but one loss": J[2992]. While the parties' liability was differently sourced, it was "for the same amount, the same extent and of the same nature": J [2992]. LGFS settled the claim and "in so doing the liability of S&P and ABN Amro was discharged": J[2992].

1011. ABN Amro and S&P appealed against that finding: ABN Amro Appeal Grounds Matrix Rows 94R and 94S and S&P Appeal Grounds Matrix Rows 58C and 58D.

1012. ABN Amro challenged the primary judge's finding that the parties' liabilities were "co-ordinate" or that they shared a "common obligation" to "make good the one loss": *Burke v*

LFOT Pty Ltd (2002) 209 CLR 282 at 292-293 [15]-[16] and *HIH Claims* at 87-90 [36] -[48]. ABN Amro submitted that there was “no suggestion that StateCover was directly mislead by or relied on [ABN Amro’s] impugned conduct”. It further submitted that LGFS’ case at its highest was that “[ABN Amro] mislead LGFS, and that this led LGFS to breach its contractual and other obligations to StateCover”. LGFS’ liabilities to StateCover were not, therefore, “of the same nature and to the same extent” as ABN Amro’s liabilities.

1013. S&P submitted that the primary judge erred because she treated LGFS’ liability as arising in contract from the settlement agreement it entered into with StateCover whereas S&P’s liability was “founded in various contraventions of the statutory prohibitions of misleading or deceptive conduct or negligence”. ABN Amro made a like submission in the course of oral argument. Those two sources of liability were said to be “fundamentally different in the obligations that they impose and cannot properly be described as being of the same nature or to the same extent”: *Burke* at 298-299 [38] . S&P further argued that a co-ordinate liability does not arise “merely because two obligations are owed to the same party or connected in time or circumstance or merely because one party’s payment has benefitted or relieved the other party financially”: *Burke* at 301 [43]-[44] . What is required is “a common design between the purported contributors to a common end”: *Burke* at 303 [48] .

1014. We reject these submissions. They misstate the nature of the primary judge’s findings. The primary judge found that the parties’ liabilities were co-ordinate in the sense that StateCover suffered “but one loss”. That aspect of her Honour’s reasoning was not challenged. We reject ABN Amro’s submission that its liability to StateCover was different from LGFS’ liability to StateCover. ABN Amro and LGFS shared a common liability. Both parties had (or would have been found to have had) a liability to exercise care in the provision of information to StateCover about the Rembrandt notes: cf J[2991]. Further, we reject S&P’s argument that the fact that its liability to StateCover had a different source to LGFS’ liability to StateCover (if that were to be accepted) pointed against a common obligation. As the Court stated in *HIH Claims* (at 88 [39]), a difference in the source of liability does not preclude the finding of a common obligation. S&P’s submissions adopt precisely the overly technical approach to the identification of a common obligation that the Court warned against in *HIH Claims* . No error has been identified in the primary judge’s findings and, in our view, none could be identified.

1015. LGFS, ABN Amro and S&P were common obligors to StateCover. LGFS’ settlement with StateCover was expressly stated to cover S&P’s and ABN Amro’s liability with respect to StateCover’s investment losses: J[2992]. LGFS’ settlement of the StateCover proceedings discharged that common obligation. Equity requires ABN Amro and S&P to make equitable contribution to LGFS. Indeed, “a community of obligation” will make it inequitable for the party against whom the contribution is sought to keep the benefit which arises from the claimant discharging its obligations: *QBE Insurance (Australia) Ltd v NSW Self Insurance Corporation* [2013] NSWSC 1841 at [28] (Hammerschlag J).

5. LGFS CONTRIBUTORILY NEGLIGENT?

1016. This is addressed in Part 13 below.

PART 8: PA COUNCILS’ PURCHASE OF 2006-3 NOTES: LGFS

1. INTRODUCTION

1017. The PA Councils' claims against LGFS were in tort, for breach of contract and misleading and deceptive claims under statute. The Appeal Grounds relevant to those claims will be dealt with in that order.

2. TORT AND EQUITABLE CLAIMS

2.1 Introduction

1018. The PA Councils maintained three separate claims. A claim in negligence, a claim for negligent misstatement and a claim for breach of fiduciary duty. Each claim succeeded. LGFS has appealed. This section of the judgment will address the factual findings and then consider the Appeal Grounds – the appeal against the finding that LGFS breached its fiduciary obligations to the PA Councils and then turn to consider the negligence and negligent misstatement claims together.

2.2 Factual Analysis

1019. For this section of the judgment, a number of matters should be noted. First, some of the relevant factual matters have already been addressed in Part 2 , Sections 1, 2 and 7 above. Next, the primary judge made numerous factual findings about the relationship, and dealings, between LGFS and the PA Councils which were not appealed by LGFS. To the extent necessary, it will be sufficient to identify some of those in summary terms, cross referenced to the trial judgment. During the course of argument, LGFS identified seven challenges it made to the primary judge's factual findings. After addressing the summary of factual findings, each of the seven specific challenges made by LGFS will be dealt with in turn.

1020. The primary judge's analysis of the relationship, and dealings, between LGFS and the PA Councils was extensive and, to the extent necessary, included the findings that follow at [1021] -[1035]. For the sake of convenience, they are addressed under the following headings:

1. Nature of the relationship;
2. Representations made by LGFS to the PA Councils;
3. The context in which the representations were made;
4. Distinction between RB Councils and NRB Councils.

2.2.1 Nature of the relationship

1021. LGFS had a lengthy history of interactions with councils in New South Wales and wanted the councils to "feel a strong relationship" with it, acting as a sounding board by providing advice on an ongoing but informal (unpaid) basis: see [29] above and J[1259(1)].

1022. LGFS' corporate strategy, explained by its staff, was to develop a relationship of trust and confidence with councils in New South Wales so as to become their trusted adviser and "confidant": see [29] above and J[1259(1) and (2)].

1023. The primary judge found that LGFS was in an advisor relationship with the PA Councils: J [2324], J[2262], J[1406] and J[1378]-J[1379]. LGFS was not a mere salesman: J[2262]. In particular, the primary judge found that:

1. An analysis of the historical relationship between LGFS and the PA Councils generally, and by reference to each of the PA Councils, demonstrated LGFS was acting as an adviser to each PA Council: J[1259]-J[1289], J[1306]-J[1372] and J [1476]-J[2116];

2. The fact that some PA Councils had invested in CDOs prior to their acquisition of the Rembrandt notes did not establish that those PA Councils were not conservative investors or understood complex structured products such that they were not reliant on LGFS' advice with respect to the Rembrandt notes: J[1477] and J[1402];

3. The fact that some PA Councils had made investments with other financial advisers or sought investment advice from third parties concerning other investments did not preclude the existence of an informal advisory relationship with LGFS, either generally or more specifically with respect to the sale of the Rembrandt notes: J[1480]. As the primary judge said, "[a] council may have more than one trusted adviser": J[1660].

1024. LGFS knew that all councils were bound by the relevant Ministerial Order (see [29] above) and the Investment Guidelines (see [21]-[24] above) including the prudent person approach: J [1642]. LGFS knew also that all councils, when investing, were dealing with public money that would ultimately be required for public purposes: J[1642]. As a result, LGFS knew that councils in New South Wales were all conservative investors and had to give priority to preserving capital over rates of return when the two were in material conflict: J[1642], J [1937] and J[1996]. Whilst in some cases LGFS expected a council to consider whether it had the funds available to invest, LGFS expected, or it was objectively reasonable for it to expect, that the council would treat the advice from LGFS as a recommendation that they in fact invest in the product subject only to the availability of surplus funds: J[2149]. LGFS' recommendation was not merely a recommendation to "take another look" or the like: J [2150], see also J[2148]. In the context of the relationship between LGFS and the PA Councils, both historically and by reference to the evidence of officers from each PA Council, the effect of LGFS offering the Rembrandt notes to the PA Councils was a recommendation that they buy it: J[1381], J[1384] and J[2161]-J[2165].

2.2.2 Representations made by LGFS to PA Councils

1025. The primary judge reviewed the evidence of Mr Hilder and Mr Tischler (at J[1135]-J[1243]) and drew conclusions as to what was said by Mr Tischler and Mr Michell to the PA Council officers in marketing the Rembrandt notes: J[1325]-J[1333]. Her Honour accepted the evidence of the PA Council officers to the extent there was any conflict with the evidence of Mr Hilder and Mr Tischler: J[1264], J[1325], J[1671], J[1759], J[1794] and J[1891]-J[1892].

1026. The primary judge found (at J[2147]) that LGFS represented to the PA Councils that, for example, Rembrandt 2006-3 was:

1. One of the best products that had come across LGFS’ desk for a long time: Eurobodalla and Deniliquin (J[2147(1)]).

2. Designed/tailored specifically for local Councils or with Councils in mind: Corowa, Orange, Moree, Oberon, Deniliquin, Murray, Cooma, Narromine and Ryde (J[2147(10)]).

3. Fully supported by LGFS/LGFS fully supports the product/LGFS will buy back at market value/guaranteed 24 hour liquidity/LGFS guarantee liquidity /money back whenever the Council needs it: Eurobodalla, Parkes, Corowa, Orange, Oberon, Deniliquin, Narrandera, Murray, Cooma, Moree and Ryde (J [2147(16)]).

4. A very robust product: Eurobodalla, Corowa and Moree (J[2147(2)]).

5. A good/suitable product for the Council: Parkes, Oberon, Murray and Ryde (J [2147(3)]).

6. A great/fantastic/terrific/perfect product or opportunity for the Council: Corowa, Moree and Deniliquin (J[2147(4)]).

7. Secure, safe and liquid: Oberon and Deniliquin (J[2147(5)]).

8. A safe product and a sound investment: Bathurst and Ryde (sound investment) (J[2147(6)]).

9. Extremely risk averse: Cooma (J[2147(7)]).

10. Suitable for a conservative Council: Oberon and Ryde (J[2147(8)]).

11. Higher returns than term deposits but low risk: Ryde (J[2147(9)]).

12. Put together by LGFS and so will sit well with the councillors: Bathurst (J [2147(11)]).

13. Designed/built to cash in and become a risk free investment in six or seven years: Eurobodalla, Orange and Moree (J[2147(12]).

14. Likely to cash in in six or seven years and then become risk free: Eurobodalla, Parkes (seven years) and Narrandera (J[2147(13)]).

15. Conservative in structure/defensive structure and takes as little risk as possible: Parkes, Corowa (takes the minimum risk possible to achieve the stated coupon), Moree and Ryde (J[2147(14)]).

16. As to cash out the likelihood was very remote/very low/very unlikely: Eurobodalla, Moree and Narrandera (J[2147(15)]).

2.2.3 The context in which the representations were made

1027. The context in which those representations were made is important.

1028. Mr Tischler marketed the Rembrandt notes by providing the PA Councils with some or all of the LGFS Community Income Notes Brochure (see [131] above), the Pre-Sale and/or the Post-Sale Report (see [131] above) and the ABN Amro term sheet (see [131] above) and "left them to it": J[1212], J[1338] and J[1389]-J[1391]). This method was not how Mr Hilder directed his staff to market the Rembrandt notes although he conceded that he had left it to them to determine what the Councils "wanted to know": J[1218]-J[1221], J[1224] and J[1335]-J [1337].

1029. The primary judge found that:

1. Given the nature of the Pre-Sale and Post-Sale Reports and the ABN Amro term sheet, LGFS' knowledge of the fact that Council officers did not understand CDOs and the lack of any questions based on the Pre-Sale Report or Post-Sale Report or term sheet, LGFS could not have believed that the PA Councils read either document before deciding to invest, nor that Council officers actually understood the product or its risks from those documents: J[1348].

2. Reading the LGFS Community Income Notes Brochure, the Pre-Sale and/or Post-Sale Report and ABN Amro term sheet would not have assisted the PA Councils to identify the risks as (J[1637]):

    2.1 The LGFS Community Income Notes Brochure did not disclose the risks – "it was a wholly one sided description of the potential benefits of investing in a product said to have been arranged by LGFS without any accompanying disclosure of the potential risks which LGFS itself knew about";

    2.2 The Pre-Sale or Post-Sale Report also did not disclose all of the risks of which LGFS was aware and did not purport to be a summary of the product suitable to be given to the PA Councils for the purpose of explaining the nature of and risks associated with the product; and

    2.3 The ABN Amro term sheet did not identify the risks of the Rembrandt notes.

3. Eurobodalla was in the same position as the other PA Councils despite receiving the Surf Presentation: J[2198].

4. LGFS knew that the Council officers would not have understood the material they had been provided: J[1343], J[1348], J[1395], J[1451], J[1566(2)] and J [1682].

5. LGFS was fully aware (or ought to have been aware) of the lack of financial sophistication of the PA Councils and that they would not understand the complex nature of the product: see J[1282].

6. It was apparent from the PA Councils' witnesses' evidence that "they did not know what they did not know" and thus could never have asked the right questions to obtain the relevant information from Mr Tischler: J[1620] and J [1639].

7. Had LGFS turned its mind to its disclosure obligations, it would have appreciated from its knowledge of local councils that their officers were not capable of formulating meaningful questions about the Rembrandt notes: J[1639].

8. LGFS was leveraging off the rapport it had established with councils over the years as a platform for the sale to them of the Rembrandt notes: J[996], J[1157], J [1178], J[1290], J[1514], J[1645], J[1671], J[1682], J[1684], J[1743], J[1823], J [1910], J[2018], J[2144], J[2167], J[2843], J[2845] and J[3319].

9. LGFS did not want the PA Councils to get advice from anyone else about the product as that would be contrary to its business plan and purpose in marketing the Rembrandt notes exactly as it did: J[1371].

1030. The position was best summarised by the primary judge at J[2265]:

> Given the unique history of LGFS, its unique status under the Ministerial [O]rder, its marketing of itself… and the beliefs [which] all of these factors engendered in the [C] ouncils about LGFS the [C]ouncils were peculiarly vulnerable to LGFS … Their degree of reliance on LGFS was high. Moreover, LGFS knew that to be the case both because of what LGFS knew about the limited capacities of [C]ouncils to understand structured financial products but also because of what LGFS knew about the high degree of trust the [C]ouncils placed in LGFS. … The category of relationship between LGFS and the [C]ouncils in respect of the product was investment adviser and client. …

1031. LGFS challenged three of these findings (1029(1), (4) and (5)) in the context of the statutory claims. These challenges are addressed and dismissed in Part 9, Section 3 below.

1032. The primary judge concluded that it was apparent from the overall circumstances, and course of dealings, between each Council and LGFS over many years, that LGFS expected and intended that, in making a decision to invest, the Councils would rely on LGFS' advice that the Rembrandt notes were suitable for Councils, were safe, secure, robust and sound: J[2150].

2.2.4 Distinction between RB and NRB Councils?

1033. There were two categories of Council. The first category comprised the **RB Councils** – Corowa and Cooma (see [116] above) – who had a contractual relationship (in the form of the Right Balance Agreement (see [112]-[115] above) with LGFS. That contractual relationship required LGFS to give advice when required on the portfolio of those Councils, and the recommendations LGFS made to the RB Councils for the purchase of the Rembrandt 2006-3 notes was made in the course of such a portfolio report. The other category comprised those Councils who had not entered into a Right Balance Agreement with LGFS – the **NRB Councils**.

1034. The relevant findings by the primary judge included that:

1. The relevant officers of Deniliquin, Moree, Parkes and Ryde did not recall LGFS offering to them the Right Balance Service and accordingly, there cannot have been any change in the reliance which those Councils placed on LGFS for investment advice: J[1289].

2. The other Councils which were aware of the Right Balance Service did not subscribe for the service because they perceived they had been receiving that service from LGFS for many years and for free: J[1289], see also, for example, the primary judge's finding in relation to Narrandera at J[1847];

3. Nothing in LGFS' marketing materials regarding the Right Balance Service or subsequent dealings with the NRB Councils suggested that the fact that they had not taken up the Right Balance Service impacted in any way upon their continuing relationship with LGFS: J[1289].

2.2.5 LGFS' challenges to factual findings

1035. Against that background, we turn to consider LGFS' seven challenges to the factual findings made by the primary judge. A number of matters of general application should be noted at the outset.

1036. Each of LGFS' challenges is rejected. The passages referred to by LGFS are incomplete and taken out of context. As the preceding section of this Part demonstrates, the primary judge made numerous factual findings which have not been challenged. That is unsurprising. As the primary judge said (at J[1247]):

> I accept that in cases involving disputed facts from years ago contemporaneous or near contemporaneous documents, where available, are invaluable and often more revealing of the true position than flawed attempts at recollection by those with an interest in the outcome of the litigation. I do not accept, however, that I should simply put to one side the affidavits of the [C]ouncil officers because they were demonstrated to be incorrect in some respects. It is true that the affidavits of the [C]ouncil officers contained formulaic evidence, errors and omissions. It is not true that "few if any of them had any real recollection of their dealings with LGFS concerning Rembrandt or the Councils' internal deliberations leading to the purchase", as LGFS submitted. It is also not true that "the Council officers who dealt with LGFS were not the decision makers". Although this was the case with respect to some [C]ouncil officers, the generalisation is too broad and fails to take account of the fact that all relevant officers involved in the decision-making processes gave evidence describing their involvement.

These observations and findings cannot, and should not, be ignored.

2.2.5.1 Challenge 1: Whether the witnesses were the decision makers and the availability of other potential advisers

1037. The primary judge made a finding that the Council officers, being those persons with whom LGFS dealt, did not have a high level of financial expertise (a fact that was known to LGFS) and instead had a general understanding of the investment products that they were authorised to invest in and relied upon LGFS' advice to assist them in making their investment decisions: J[1259(3)].

1038. LGFS challenged this finding. Its challenge was specific. LGFS submitted that the people that it was dealing with were not always the decision makers and that LGFS was not the only available source of advice for the Councils. LGFS summarised its argument as follows:

> LGFS was also dealing with the Councils as institutions. LGFS was not privy to the Council's internal deliberations concerning [the Rembrandt notes]. LGFS did not necessarily know what experience the decision maker(s) had. And even when LGFS might have suspected that all the relevant Council officers lacked knowledge or experience of structured products, LGFS had no way of knowing whether outside assistance had been brought to bear in making the decision.

1039. The challenge fails generally and specifically. First, the passages of the trial judgment referred to by LGFS in support of its challenge are incomplete and taken out of context. LGFS does not challenge the finding (at J[1247]) that "all relevant officers involved in the decision-making processes gave evidence describing their involvement". In fact, LGFS accepted the truth of that statement but went on to contend that not all of the decision maker witnesses in fact dealt with LGFS. Again, that statement conceals more than it reveals.

1040. The first witness identified was Mr Brian Matthews, who, until his retirement in 2008, was the Director of Corporate Services at Parkes. Mr Matthews did not discuss the Rembrandt notes with LGFS. However, Mr Robert Bokeyar from Parkes did discuss the Rembrandt notes with Mr Tischler of LGFS. The evidence disclosed that Mr Bokeyar had contact with Mr Tischler through at least two separate discussions (J[1541], J[1542] and J[1546]) and through the provision of the Pre-Sale Report by Mr Tischler to Mr Bokeyar: J[1545]. The evidence disclosed that, on at least two occasions after his discussions and communications with Mr Tischler, Mr Bokeyar would discuss the Rembrandt notes with Mr Matthews, his superior: J [1543], J[1544], J[1548] and J[1549]. None of those facts were challenged by LGFS.

1041. Similar complaints were made by LGFS in relation to Mr Tony Burgoyne at Bathurst and Ms Jane Redden at Narromine. In relation to Bathurst, Mr Michell of LGFS visited Bathurst and discussed the Rembrandt notes with a Mr Campion. He gave Mr Campion the LGFS Community Income Notes Brochure and, in response to a concern expressed by Mr Campion, stated that Rembrandt 2006-3 was not a CDO and not like a CDO. On the same day, Mr Tischler sent Mr Campion an email attaching the Pre-Sale Report and the ABN Amro term sheet. Mr Campion forwarded the email and gave the LGFS Community Income Notes Brochure to his superior, Mr Burgoyne (J[1814]), who then discussed the proposed investment with his own superior, Mr Roach (J[1824]). The position at Narromine was not dissimilar. Mr Michell dealt with Ms Corderoy and she discussed the Rembrandt notes with her superior, Ms Redden (J[2046]). None of these facts were challenged by LGFS.

1042. The next PA Council identified was Oberon. LGFS submitted that two of its decision makers – Mr John Chapman and Mr Bruce Fitzpatrick – did not discuss the Rembrandt notes with LGFS and that the primary judge did not make any specific findings in relation to Oberon's relationship with LGFS. Again, LGFS omitted to refer to the fact that Mr Michell of LGFS discussed the Rembrandt notes with Ms Amanda McGrath, the Finance Manager at Oberon. At J[1694], the primary judge addressed this contention directly and stated: "Mr Chapman did not have discussions directly with LGFS. He relied on what Ms McGrath told him LGFS had said in that regard". It must be recalled that her Honour made further unchallenged factual findings (at J[1690]) that Ms McGrath reported to Mr Chapman and that, according to Mr Chapman, Ms McGrath was in 2006 primarily responsible for analysing investment options for the Council and providing him with relevant information. LGFS did not challenge any of these findings. The primary judge did not leave the position there. Her Honour also made an unchallenged finding (at J[1697]) that:

> The fact that Mr Chapman relied on LGFS (in this case) having determined that the product was a suitable one for [C]ouncils, and thus Oberon, to invest in does not mean that Mr Chapman exercised no judgment at all about investments and he did not give evidence to that effect. The [C]ouncil still had to consider its own position including whether it had the funds available to invest and whether such a long-term investment was appropriate at the time given its funding obligations. The [C]ouncil did not rely on LGFS to make those decisions for it (although, as it turns out, in the case of Oberon it was LGFS which identified that the [C]ouncil had two investments with LGFS which were about to mature and funds from which could be reinvested in [the Rembrandt notes]). But it did rely on LGFS having determined that the product was a suitable one for any [C]ouncil, including Oberon, to invest in.

This analysis demonstrates that LGFS' contention that the primary judge made *no* findings specific to Oberon's relationship with LGFS is wrong.

1043. LGFS then referred to Ryde where two members of its investment committee – Mr Michael Whittaker and Mr Roy Newsome – did not deal with LGFS. Again, that statement conceals more than it reveals. Mr Michell dealt with Mr Richard Nankivell, the third member of the committee (J[2070]) and also with Mr Barry Gibb (Mr Nankivell's assistant). Mr Tischler also dealt with Mr Nankivell in relation to the Rembrandt notes: J[2083]-J[2085]. Mr Nankivell was primarily responsible for assessing proposed investments: J[2075]. Mr Gibb was also a member of the investment committee: J[2073]. In addition, Mr Nankivell received the [CPDO] letter from Mr Hilder of LGFS attaching the LGFS Community Income Notes Brochure: J[2088]-J[2089]. Mr Nankivell reported to Mr Newsome and the investment committee and did so in relation to the Rembrandt 2006-3 notes: J[2092]-J[2093]. In addition, Mr Gibb provided assistance to Mr Nankivell and prepared a memorandum about the Rembrandt notes for the investment committee: J[2090] and J[2094]. None of these facts were challenged by LGFS.

1044. Finally, LGFS referred to Eurobodalla and Moree in support of its contention that LGFS was not the only available source of advice for the Councils. Mr Tischler had had involved discussions with a representative from Eurobodalla and had informed Eurobodalla that it was unlikely that it would lose capital because of the Rembrandt notes' "cash in" and "self cleansing" features: J[1481]. The primary judge made findings that although both Eurobodalla (J[1480]) and Moree (J[1660]) referred to and relied upon another body for advice, that fact alone did not establish that each Council could not have relied upon LGFS when it came to investing in Rembrandt 2006-3 notes. As the primary judge said (at J[1674]), a Council may have more than one trusted adviser. LGFS' contention on appeal was that the existence of more than one advisor did not mean that the relevant Council did not rely on what LGFS told it but did show that the Council was not reliant on LGFS. For our purposes, that is a distinction without a difference. Each Council was found to rely on what LGFS told it: Eurobodalla at J[1482] and Moree at J[1664]. LGFS does not challenge those findings or the facts upon which those findings were made.

2.2.5.2 Challenge 2: Relevance of Right Balance Agreements

1045. The primary judge considered the relevance of the Right Balance Agreement at J[1271] as follows:

> Contrary to LGFS's submission I do not find it at all unconvincing that all but two of the [C]ouncils which were aware of the Right Balance [S]ervice refused it on the basis that they believed that LGFS was already offering the same service free of charge. It is true that the [C]ouncils must have known that they were not receiving the reporting services offered as part of the Right Balance [S]ervice. But the point is this – by LGFS' s own prior invitation the [C]ouncils had access to LGFS's expertise free of charge as and when they required it to act as the [C]ouncils' sounding board and financial markets confidant because LGFS enjoyed a unique and long-standing association with local government which ensured that it would act in the best interests of the [C]ouncils. The Right Balance [S]ervice seems to have failed precisely because LGFS had always offered the same service – albeit without the formal reporting – free of charge. …

1046. LGFS' challenged what it described as "the primary judge's finding that the Right Balance Service offered by LGFS was the same or substantially the same as the ad hoc advice LGFS provided to the Councils". There are a number of answers to that contention. First, the Right Balance Agreement provided a different legal basis for LGFS' relationship with the RB Councils as distinct from the NRB Councils. In considering the position of the NRB Councils, that fact alone did not provide an answer, let alone a complete answer, to the nature of the relationship between LGFS and the NRB Councils. The nature of the relationship between LGFS and the NRB Councils had to be addressed by reference to the unchallenged factual findings at [1021]- [1024] above. Those findings were independent of the Right Balance Agreement. LGFS' contention proceeds on a false premise – that the existence of the Right Balance Agreement somehow altered the nature of the relationship between LGFS and the NRB Councils. It did not and that was the finding of the primary judge: J[1287]-J[1289]. Indeed, at least four NRB Councils (Deniliquin, Moree, Parkes and Ryde) could not recall being offered the Right Balance Service: J[1289]. Other Councils decided not to take up the Right Balance Service because they considered they had been receiving the same service from LGFS for many years without the fees imposed by the Right Balance Agreement: J[1289] and J[1269].

1047. There were other factual findings that should not be overlooked in this context. Those findings include that the distinction between the RB Councils and the NRB Councils did not seem to have existed in anyone's mind at LGFS at the time or, if it did exist, it had no effect on the information which LGFS provided to the Councils: J[1349]. So, for example, the RB Councils received no more information from LGFS than any of the NRB Councils: J[1349].

2.2.5.3 Challenge 3: Whether the Councils would have understood that LGFS would prefer its own interests over those of the Councils

1048. LGFS challenged the following italicised sentence of the primary judge's findings at J[1272]:

> The fact is that LGFS's own marketing material and documents are sufficient to found the inference that LGFS deliberately and over many years fostered a belief in the [C]ouncils that LGFS not only had the necessary skill, experience, qualifications and expertise to be able to provide financial information and advice tailored to the particular needs and requirements of [C]ouncils but also that as a trustworthy and reliable source of such information and advice, the interests of which were closely aligned with those

> of [C]ouncils, LGFS would ensure its information and advice was provided with a view to the best interests of the [C]ouncils. *In other words, the whole of LGFS's relationship with [C]ouncils in New South Wales was to the effect that LGFS would not prefer its own interests to those of the [C]ouncils.* This was LGFS's crucial point of distinction with other providers of financial advice and services to [C]ouncils in New South Wales.
>
> (Emphasis added.)

1049. The passage in italics is just one sentence. As the sentence makes clear ("in other words"), it was the primary judge's restatement of the factual findings which preceded the sentence. None of those factual findings were challenged by LGFS. The sentence must be read in the context in which it sits. It is only by divorcing the sentence from its context that LGFS could assert, as it did, that the primary judge put the relationship between the parties too highly. The argument must be rejected. The unchallenged findings by the primary judge stated the nature and relevant consequences of LGFS' relationship with the PA Councils accurately: see also, by way of example, J[1141], J[1147], J[1148] and J[1157], and [1021]-[1024] above.

2.2.5.4 Challenge 4: Whether the Councils were reliant on LGFS

1050. LGFS challenged the primary judge's finding that the PA Councils were reliant on LGFS when it came to understanding whether the Rembrandt 2006-3 notes were a suitable investment for them: J[1259(4)]. Her Honour stated that there was "ample evidence" to support that general finding. We agree: see, for example, J[1475], J[1684], J[2324] and J[2151] and the factual findings set out at [1021]-[1024] and [1029]-[1030] above. During the course of argument, LGFS referred to passages of the trial judgment it relied upon in relation to Challenges 1, 3 and 5. The problems with that material apply equally to Challenge 4.

1051. LGFS' argument must be rejected. The PA Councils were reliant upon LGFS when it came to understanding whether the Rembrandt 2006-3 notes were a suitable investment for them: see [1021]-[1024] and [1029]-[1030] above.

2.2.5.5 Challenge 5: Findings concerning LGFS' beliefs in J[1371]

1052. Paragraph J[1371] of the trial judgment was entitled "*If LGFS not giving investment advice*" and it read:

> … [A]gain, as the [C]ouncils submitted in their alternative case, LGFS did not inform any of the [C]ouncils that: – (i) LGFS had not considered whether an investment by them in the Rembrandt notes was suitable or appropriate for them; (ii) LGFS was not recommending they invest in the Rembrandt notes, or (iii) they should obtain financial advice about whether to invest in the product. I consider that LGFS did not inform the [C]ouncils to this effect for one obvious reason – because *LGFS knew the [C]ouncils believed that: – (i) LGFS had considered whether an investment by them in the Rembrandt notes was suitable or appropriate for them; (ii) LGFS was recommending they invest in the Rembrandt notes, and (iii) they need not obtain financial advice about whether to invest in the product because LGFS was advising them to do just that.* More over, LGFS intended that the [C]ouncil officers should believe these things. *LGFS did not want the [C]ouncil officers to get advice from anyone else about the product.* That would have been contrary to LGFS's business plan and purpose in marketing the

> product to the [C]ouncils in the way it did. LGFS cannot complain now that the [C] ouncils acted precisely as LGFS in fact intended at the time by relying on LGFS.
>
> (Emphasis added.)

1053. LGFS' argument was that the findings in italics were unsupported by evidence and were directly contradicted by emails sent to Narromine and Ryde.

1054. Again, this argument conceals more than it reveals. First, these findings were addressing the PA Councils' alternative case run at trial (i.e, if LGFS was found *not* to be giving investment advice). The primary judge found that LGFS was giving investment advice: see [1021]-[1024] and [1029]-[1030] above.

1055. Second, the findings in italics were supported by evidence: see [1021]-[1024] and [1029]-[1030] above. Third, LGFS' argument that the emails to Narromine and Ryde contradicted those findings is rejected. The emails stated that LGFS was "happy to provide any further information to you or your adviser". These two emails do not contradict the finding. Selectively quoting part of one sentence from two emails to support a contention that a finding was incorrect is impermissible. The contents of emails (here, part of a sentence), absent other evidence, do not and cannot conclusively establish LGFS' state of mind. LGFS' argument is rejected.

2.2.5.6 Challenge 6: Relevance of the speed of the Councils' decision to acquire the Rembrandt notes

1056. As we have seen (see [1029] above), the primary judge made a finding that given the nature of the Pre-Sale Report, the Post-Sale Report and the ABN Amro term sheet, LGFS' knowledge of the fact that Council officers did not understand CDOs and the lack of any questions based on either the Pre-Sale or Post-Sale Report or the term sheet, LGFS could not have believed that the PA Councils read either document before deciding to invest, nor that Council officers actually understood the product or its risks from those documents: J[1348]. That factual finding was not challenged.

1057. There was, however, another related aspect to this finding at J[1348]. That was a finding that, except for Cooma, it was difficult to accept that LGFS did not notice how quickly many of the PA Councils made their decisions after first being contacted about the product and having been sent the documents by LGFS to which reference has just been made. These findings were and remain interrelated.

1058. Moreover, the finding was not made in a vacuum. It was preceded by other significant and unchallenged factual findings. For example, the primary judge made the following factual findings (at J[1347(c)]):

> Mr Tischler [of LGFS] knew he had taken two months of immersion to understand the product but LGFS never appears to have been surprised by the swiftness of the decisions some of the [C]ouncils communicated to LGFS measured against receipt of the [Pre-Sale Report] (including possible weekends – about four days for Eurobodalla, zero days for Parkes, three days for Corowa, maybe a week or two for Orange or less but not more, a week for Moree, for Oberon the report was received a week after the decision was communicated to LGFS, 10 days for Deniliquin, eight days for Bathurst,

nearly four weeks for Narrandera, seven days for Murray, three weeks for Narromine and four days for Ryde). The only Council that had the [Pre-Sale Report] for any lengthy period before investing was Cooma – but Cooma invested in response to a specific LGFS recommendation six months after the [Pre-Sale Report] was emailed.

1059. These findings were not challenged by LGFS. Instead, it contended that there was no "[C]ouncil-specific case" or "[C]ouncil-specific" cross examination of Mr Tischler about these matters. There are a number of problems with that contention. This was a conclusion about reliance, not understanding, in *all* the circumstances. Selective criticism of just one circumstance identified by the primary judge is neither permissible nor appropriate. In any event, the inference was open to the primary judge. LGFS' challenge must be rejected.

2.2.5.7 Challenge 7: Price volatility and whether the Rembrandt notes were suitable for any Council at any time

1060. The primary judge found that LGFS should have known that an investment that might be highly volatile was not a suitable investment for any Council to make at any time: J [2164]. LGFS challenged two propositions – (1) that a potentially volatile investment was unsuitable for any Council at any time and (2) if that was so, LGFS knew Rembrandt 2006-3 to be sufficiently "highly volatile" to be unsuitable.

1061. This challenge is rejected for the reasons set out in Part 8, Section 2.4.4.2 under the heading "Suitability of Rembrandt for local councils": see [1136]-[1152] below.

2.2.6 Conclusion

1062. It is against that factual background that we turn to consider LGFS' Appeal Grounds.

2.3 Fiduciary duty claim: LGFS Appeal Grounds Matrix Rows 101-108

2.3.1 Introduction

1063. The primary judge found that LGFS was in a fiduciary relationship with each PA Council. In relation to the RB Councils, LGFS accepted on appeal that it had a contractual relationship (in the form of the Right Balance Agreement) (see [112]-[115] above) with each of the RB Councils which required it to give advice when required on the portfolio of those Councils and that the recommendations it made for the purchase of the Rembrandt 2006-3 notes was made in the course of such a portfolio report. LGFS accepted that in those circumstances it owed fiduciary obligations to each of the RB Councils: LGFS Appeal Grounds Matrix Row 102.

1064. On appeal, LGFS challenged the primary judge's finding that LGFS was in a fiduciary relationship with the NRB Councils and further contended that, if such a relationship did exist, it did not breach any fiduciary obligations it owed to the NRB Councils: LGFS Appeal Grounds Matrix Rows 101, 103 and 104.

1065. This section of the judgment will consider whether LGFS' relationship with each of the NRB Councils was a fiduciary relationship and then turn to consider whether LGFS breached the fiduciary obligations it owed the NRB Councils.

2.3.2 Applicable legal principles – fiduciary relationship

1066. **Following paragraph cited by:**

R and N Hunter Pty Ltd ATF the Hunter Family Superannuation Fund v Count Financial Limited (27 May 2025) (Halley J)

180. There is no generally agreed and unexceptionable definition of who is a fiduciary: ***Grimaldi*** *v Chameleon Mining NL (No 2)* (2012) 200 FCR 296; [2012] FCAFC 6 at [177] (Finn, Stone and Perram JJ). The characteristics which define a fiduciary relationship cannot be exhaustively defined: ***ABN AMRO*** *Bank NV v Bathurst Regional Council* (2014) 224 FCR 1; [2014] FCAFC 65 at [1066] (Jacobson, Gilmour and Gordon JJ) .

R and N Hunter Pty Ltd ATF the Hunter Family Superannuation Fund v Count Financial Limited (27 May 2025) (Halley J)
R and N Hunter Pty Ltd ATF the Hunter Family Superannuation Fund v Count Financial Limited (27 May 2025) (Halley J)
In the matter of 1derful Pty Limited (08 November 2024) (Black J)
Troiano v Voci (17 December 2021) (Delany J)
Re: Porter & Anor v Mulcahy & Co Accounting Services Pty Ltd & Ors (13 September 2021) (Delany J)
Oliver Hume South East Queensland Pty Ltd v Investa Residential Group Pty Ltd (01 September 2017) (Dowsett, Greenwood and White JJ)
Riva NSW Pty Limited v Official Trustee in Bankruptcy (03 March 2017) (Perry J)
Investa Properties Pty Ltd v Nankervis (No 7) (10 September 2015) (Collier J)

For the purposes of this appeal, the applicable principles *may* be summarised as follows:

1. The "critical feature is that the fiduciary undertakes or agrees to act for or on behalf of or in the interests of another person": *Hospital Products Pty Ltd v United States Surgical Corp* (1984) 156 CLR 41 at 96-97 ; *Pilmer v Duke Group Ltd* (2001) 207 CLR 165 at 196-197 [70]-[71] and *Australian Securities and Investments Commission v Citigroup Global Markets Australia Pty Ltd (No 4)* (2007) 160 FCR 35 at 76 [270]-[275] and 77 [283] .

2. It is the element of undertaking (from the point of view of the fiduciary) or obligation (for and on behalf of the beneficiary) that has the consequence that equity insists that the principal must act in the "interests of" or "for the benefit of" the beneficiary rather than in the principal's own interests: *Breen v Williams* (1996) 186 CLR 71 at 113, approved in *Pilmer* at 196-198 [70] and [74] .

3. Whether a fiduciary relationship exists in a particular case, and if so, the scope of that fiduciary relationship, are matters which depend critically upon the particular circumstances of the case: *In Re Coomber* [1911] 1 Ch 723 at 728-729, approved in *Hospital Products* at 102 ; see also *Pilmer* at 198-199 [77]-[78] and *Citigroup* at 76 [285], 78 [287]-[288] .

4. The characteristics which define a fiduciary relationship cannot be exhaustively defined. It is inappropriate to treat the existence of a fiduciary obligation as being dependent upon whether the principal and beneficiary fall into a particular status relationship: James Edelman, 'The Role of Status in the Law of Obligations: Common Callings, Implied Terms and Lessons for Fiduciary Duties' (Paper presented at the University of Alberta, 18 July 2013, and DePaul University conference, Chicago, 19-20 July 2013).

5. Similarly, whether a fiduciary relationship has come into existence does not depend upon the motivation or desire of one party to establish a relationship of trust or confidence. What matters is whether there is a relationship involving the requisite undertaking, determined as a matter of objective characterisation, rather than by having regard to the subjective expectations of the parties: *Beach Petroleum NL v Kennedy* (1999) 48 NSWLR 1 at 45 [188] and 46 [194] ; P D Finn, *Fiduciary Obligations* (Law Book Company, 2nd ed, 1977), par 14ff; James Edelman 'The Importance of the Fiduciary Undertaking' (2013) 7 *Journal of Equity* 128 (see also, James Edelman 'When Do Fiduciary Duties Arise' (2010) 126 *Law Quarterly Review* 302) and, in the context of a contractual relationship, *Citigroup* at 77 [281] .

2.3.3 LGFS' submission on appeal

1067. Against that background, it is necessary to address the relationship between LGFS and each of the NRB Councils. LGFS submitted that:

> The relationships between LGFS and the NRB Councils were different. … [I]t was not correct to describe any of those relationships as one of "investment adviser'", whether "informal" or not. There is a clear distinction between LGFS's dealings with those Councils and Patrick Partners' dealings with Dr Daly which were the subject of *Daly v Sydney Stock Exchange* . Dr Daly had a particular sum of money to invest and entrusted the task of advising on how to invest that sum to Patricks. It was in that context that Patricks recommended that the money be deposited with it. The relationship was one where, of its nature, the giving of investment advice and the making of investment recommendations was a matter exclusively for Patricks.
>
> There was no equivalent relationship between LGFS and the NRB Councils. None of those Councils entrusted their portfolios, or any particular part of their portfolios, for LGFS to advise upon. At most, those Councils which used LGFS as a "sounding board" sought its "advice" (in the form of information and opinions about particular products) as and when it suited them, and made their decisions on the basis of that and other information without further reference to LGFS. Nor was this relationship in any way exclusive to LGFS. The Councils dealt with a number of different financial institutions depending on the nature of the proposed investment. When LGFS set out to market Rembrandt [2006-3] to the NRB Councils, it did not do so under cover of complying with any pre-existing obligation or request for advice. Rather, LGFS made a "cold call". LGFS would have been entitled to assume that the Councils would have treated this approach in the same way in which they had treated approaches from vendors of other products: that is, by asking any questions they had of LGFS, considering the material which LGFS provided for them (and, in the case of

Eurobodalla, which it already had), and quite possibly by seeking information and opinions from competitors and other third parties, as in fact two of them did. There was nothing in any of this which amounted to an undertaking by LGFS to act in the Council's interests rather than its own.

These contentions fail. That statement requires further explanation.

2.3.4 Did a fiduciary relationship exist between LGFS and the NRB Councils?

1068. The primary judge found (at J[2322]-J[2324]) that LGFS was in a fiduciary relationship with each of the NRB Councils for the following reasons:

1. LGFS held itself out as an entity on which the Councils could and should rely to satisfy themselves that LGFS had brought its expertise to bear and evaluated the product as a suitable investment for each Council. In so doing LGFS moved beyond the role of a mere salesman and acted as an investment advisor and thereby attracted to itself fiduciary duties to avoid conflicts of interest or duties to disclose and obtain consent to such conflicts": J[2324] and J[2300]-J[2323];

2. In introducing the Rembrandt 2006-3 notes to the Councils, LGFS did not act as a mere salesman. LGFS knew the Councils perceived LGFS as acting in their interests and not LGFS' sole interests and LGFS did not disabuse the Councils of that belief: J[2324]; and

3. LGFS traded on that belief (that the Councils perceived LGFS as acting in their interests and not LGFS' sole interests), a product of the relationship that LGFS' fostered and cultivated over many years with the Councils, to achieve its own commercial objectives: J[2323]-J[2324].

1069. Her Honour described LGFS as an "informal investment adviser" to each Council: J[2322]-J[2324]; see also Part 2 , Sections 1, 2 and 7 above and [1021]-[1030] above. That description was, and is, not inaccurate.

1070. LGFS' contention (at trial and on appeal) that it did not owe fiduciary obligations to each NRB Council is untenable. First, LGFS would have the Court ask the wrong question. As the summary of applicable legal principles illustrates, the question is *not* whether LGFS "fits" into the facts of a decided case and, in particular, *Daly v Sydney Stock Exchange* (1986) 160 CLR 371. The question was and remains whether the facts disclose the existence of a fiduciary relationship. It is that question which identifies LGFS' second error – its analysis and assessment of the facts was incomplete and inaccurate.

1071. **Following paragraph cited by:**

R and N Hunter Pty Ltd ATF the Hunter Family Superannuation Fund v Count Financial Limited (27 May 2025) (Halley J)

The characteristics which define a fiduciary relationship *cannot* be exhaustively defined. Contrary to LGFS' contention on appeal, the facts were sufficient to constitute a fiduciary relationship in which LGFS undertook to act in the NRB Councils' interests rather than its own: see [1021]-[1030] above. The existence of such a duty followed analysis of the history of the relationship between LGFS and each of the NRB Councils, including how LGFS marketed itself to the PA Councils: see Part 2 , Section 7 above and [1028]-[1030] above.

2.3.5 Conflict of interest and therefore disclosures required by LGFS?

1072. A party owing fiduciary obligations to another is bound "to avoid being in a position of conflict between its interests and duties, and between its duties to other persons" and "not to obtain any unauthorised benefit from its position": *Breen v Williams* at 113. The identification of the relevant conflict informs the required disclosures by the fiduciary and the analysis of whether the fiduciary has breached those requirements.

1073. The primary judge found that LGFS breached its fiduciary duty to avoid conflicts of interest, or to disclose and obtain fully informed consent to such conflicts: J[1373]-J[1374] and J [2311]-J[2324]. The issue was addressed by her Honour in two separate passages of the judgment.

2.3.5.1 Failure to disclose potential risks and ramifications faced by LGFS in holding $40 million of notes

1074. In the first passage (at J[1373]-J[1374]), her Honour dealt with LGFS' alleged conflict of interest in the following terms:

> After its purchase of all of the Rembrandt notes issued under the Rembrandt 2006-3 transaction, LGFS held $40,000,000 of the notes (to which $5,000,000 was added in January 2007). LGFS recognised that this fact had consequences for it identified as potential risks and ramifications. As disclosed in its board papers for October 2006, LGFS was aware that LGFS could end up holding inventory with no available purchaser (the asset would be suitable for LGFS's balance sheet operations but would prevent new issues as there would be no room for holding long-term assets).
>
> LGFS's consciousness of these risks and ramifications, as well as its own commercial [imperative] to address the impact of CDO's on its balance sheet, placed it in a position of conflict of interest …

1075. These findings were unsurprising. They are consistent with, and reflect, the position that LGFS found itself in: see [90] above. At best, one Council (Orange) knew that LGFS had purchased notes valued at $40 million: J[2301]. No Council was told of the potential risks and ramifications faced by LGFS in holding that amount of notes, including LGFS' commercial imperative of addressing the impact of those notes on its balance sheet. As it was described elsewhere in the trial judgment, LGFS acquired the entire tranche of the Rembrandt notes from ABN Amro in the amount of $40 million and had an interest in liquidating a portion or a substantial portion of its own holdings because:

1. To the extent LGFS was not able to sell the Rembrandt notes, it was exposed to the risks of losses on those notes it continued to hold; and

2. Those risks included certain risks associated with the Rembrandt notes (see Part 3 above) which were not disclosed at the time LGFS marketed the notes to the PA Councils.

1076. LGFS' duty was not to be in a position of conflict of duty and interest. It breached that duty. LGFS was in a position of conflict between its interests and duties, and between its duties to the PA Councils. LGFS did not disclose to the PA Councils the potential risks and ramifications faced by LGFS in holding the amount of Rembrandt notes it held, including LGFS' commercial imperative of addressing the impact of those notes on its balance sheet.

1077. Indeed, LGFS accepted that if it was in a fiduciary relationship as "investment advisor" with the PA Councils (and it was) then a "potential conflict of interest" arose from the fact that LGFS would profit from the sale of the Rembrandt notes to the PA Councils. However, LGFS submitted that the Councils knew that fact: J[2319]. So much may be accepted. However, LGFS' argument that the PA Councils were aware that LGFS was the vendor of the Rembrandt notes or otherwise stood to gain financially from their purchase of the notes goes to issues of informed consent, not questions of conflict and disclosure.

1078. The PA Councils did not know, and were not told by LGFS, of the commercial pressures LGFS faced and which made its sale of the notes commercially imperative. Its motivation for selling the notes was itself a conflict, a substantial conflict, which was required to be disclosed and was not: cf *Pilmer* at 199-201 [79]-[83] . LGFS accepted that it was, and remains, the fiduciary's obligation to disclose the conflict and to permit the beneficiary to make a free and fully informed decision on whether to proceed. That did not occur. And, contrary to LGFS' submissions, the fact that LGFS was obliged to disclose the commercial pressures it faced was not and is not unworkable.

1079. That leads to the form of the disclosure. LGFS raised two complaints: LGFS Appeal Grounds Matrix Row 105. First, LGFS contended that the primary judge overstated the significance of the Rembrandt notes to the viability of LGFS' business. LGFS submitted that this meant that even if LGFS had a duty to disclose its commercial imperatives, the duty would have been satisfied by a less stark disclosure than the primary judge considered necessary. The second complaint was that the primary judge's formulation of what LGFS had to disclose was different from that pleaded by the PA Councils. LGFS submitted that as the PA Councils did not mount an evidentiary case as to what they would have done if they had known of the "conflict", it did not have an opportunity to meet the relevant disclosure. These contentions fail.

1080. The PA Councils did not know, and were not told by LGFS, of the commercial pressures LGFS faced and which made its sale of the notes commercially imperative. The significance of the Rembrandt notes to the viability of LGFS' business was not and cannot be overstated: see [90], [98]-[108], [116]-[119] and [124] above. Even if we are wrong to reject that contention, LGFS was obliged to disclose the significance of the Rembrandt notes to the viability of LGFS' business and it did not. That failure placed it in an immediate position of conflict. Its duty was not to be in a position of conflict of duty and interest. It breached that fiduciary duty.

1081. The next limb in LGFS' argument – that the PA Councils did not mount an evidentiary case as to what they would have done if they had known of the "conflict" – is addressed below in section 2.3.6 of this Part of the judgment.

2.3.5.2 LGFS information

1082. The second passage of the judgment addressed the conflict of interest issue in wider terms by reference to what was defined in the trial judgment as the "LGFS information". It was defined to mean:

> 1. LGFS was entitled to earn a substantial fee or commission on the sale of Rembrandt to the [C]ouncil;
>
> 2. LGFS was under a mandate with ABN [Amro] to assist in the promotion of the product;
>
> 3. LGFS had arranged the structuring and creation of Rembrandt by ABN [Amro] for LGFS to sell to local [C]ouncils as it was concerned that it was losing market share of [C]ouncils' invested funds by not offering higher yielding financial products similar to those offered by LGFS' competitors such as collateralised debt obligations (CDOs) to local [C]ouncils.
>
> 4. LGFS had acquired the entire tranche of Rembrandt from ABN [Amro] in the amount of $40,000,000 and had an interest in liquidating a portion or a substantial portion of its own holdings because;
>
> (a) to the extent LGFS was not able to sell Rembrandt, it was exposed to the risks of losses on those [n]otes it continued to hold;
>
> (b) those risks included certain risks associated with Rembrandt that have been identified in these proceedings, but which were not disclosed at the time LGFS marketed Rembrandt to the [C]ouncil;
>
> 5. LGFS had received a report prepared by Grove Research and Advisory which identified substantial risks associated with Rembrandt which were not disclosed to the [C]ouncil officers by LGFS;
>
> 6. LGFS held the view that Rembrandt was a grotesquely complicated product;
>
> 7. LGFS was aware that in the period prior to LGFS's marketing of the product to the [C]ouncils there had been negative movements in the credit spreads in the two indices which was likely to have an adverse effect on the future performance of Rembrandt;

> LGFS may have had a conflict of interest in Rembrandt by reason of the matters referred to in 1 to 7 above.

1083. The primary judge addressed the conflict of interest issue in the context of the LGFS information at J[2311]-J[2312]:

> … [T]he LGFS information created a conflict between LGFS's interests and those of the [C]ouncils. In the context of the fiduciary relationship between LGFS and the [RB Councils] the attempts by LGFS to isolate and diminish the significance of each piece of the LGFS information should be resisted. As a whole the circumstances described disclose the existence of a conflict of interest. The [C]ouncils' interest was to invest only in products that were suitable for [C]ouncil investment in the sense described. In respect of the Rembrandt CPDO LGFS's interest was to establish itself as a player in the financial products market in order to overcome the substantially deleterious effect that the sale of CDOs had on LGFS's profitability. The conflict is not removed by LGFS's belief that the product was not a "dog" (as LGFS put it, a belief which LGFS did hold), could be held on LGFS's balance sheet if not sold entirely to [C]ouncils albeit with some risk, and was suitable for [C]ouncils given its AAA rating and good return. In fact, LGFS's apparent beliefs support the existence of the conflict of interest which it submitted either did not exist or was too remote or insubstantial to have any effect on the discharge of any fiduciary obligations.
>
> The point can be explained this way. The essence of the LGFS information, evaluated in the context set by the evidence, is that LGFS's business was under serious threat from CDOs, it wanted a product to compete, it entered into a deal with ABN Amro about the CPDO which enabled it to compete, it bought as much of the product as it could intending to sell it to [C]ouncils to increase (probably, more to the point, establish) its position as a structured product provider to [C]ouncils, it knew things about the product that in fact made it unsuitable for [C]ouncils, but implemented strategy by selling as much of the product as it could to [C]ouncils and proceeded to do so without telling the [C]ouncils any of this information. It is not an answer to this case to say that LGFS believed the product to be suitable for [C]ouncils.

1084. For our part, we are not persuaded that each limb of the "LGFS information" placed LGFS in a position of conflict that necessitated the disclosure of each limb to each of the PA Councils. At the very least, the PA Councils did not know, and were not told by LGFS, of the commercial pressures it faced and which made its sale of the notes commercially imperative. That failure placed LGFS in an immediate position of conflict. Its duty was not to be in a position of conflict of duty and interest. That was sufficient to constitute a breach of LGFS' fiduciary duty: see Part 8, Section 2.3.4 above.

2.3.6 Factual causation

1085. This section of the judgment will consider factual causation in relation to the claims for equitable compensation for breach of fiduciary duty.

1086. Having dismissed LGFS' Appeal Grounds in relation to the fiduciary duty findings (see [1067]-[1084] above), LGFS' next contention was that the primary judge erred in holding that, but for LGFS' breaches of duty, the PA Councils would not have invested in the Rembrandt notes: LGFS Appeal Grounds Matrix Row 117.

1087. LGFS' argument at trial and on appeal was that:

> The direct and immediate cause of the Councils' losses was the cash-out of their [n] otes. This in turn was the result of deficiencies in Rembrandt's structure which led to its robustness being over-estimated and over-represented by ABN [Amro] and S&P. In a real and practical sense, these were the causes of the Councils' losses. … [N]one of the misrepresentations and non-disclosures alleged against [LGFS], individually or collectively, was a cause of those losses in the relevant sense.

That argument was rightly rejected at trial.

1088. LGFS had further complaints. It submitted that on causation, the primary judge said that it was "sufficient to say that I do not accept that [the RB Councils] would not have acted any differently if LGFS had disclosed its conflict of interest and sought [their] consent to its conflicted position" (J[2321]) but did not give any further reasons, or identify any specific factual findings on which she relied for this conclusion. LGFS further contended that the primary judge did not expressly address the question of causation as it applied to the NRB Councils. In addition, LGFS contended that the Councils did not mount an evidentiary case as to what they would have done if they had known of the "conflict".

1089. It is necessary to keep a number of points at the forefront of consideration. First, LGFS made a gain from its dealings in the Rembrandt notes where its duty to the Councils and its personal interests conflicted. Second, the Councils' informed consent to that dealing was not obtained. Third, because the Councils invested in the notes, they lost a substantial part of their investment.

1090. **Following paragraph cited by:**

> City Garden Australia Pty Ltd (in administration) as trustee for the Ming Tian City Garden Unit Trust v Meng Dai (05 December 2023) (Rees J)
> Vanguard Financial Planners Pty Ltd v Ale (14 March 2018) (Black J)

Fourth, the principles of causation in relation to a claim for equitable compensation for breach of fiduciary duty are distinct. The court must identify "criteria which supply an adequate or sufficient connection between the equitable compensation claimed and the breach of fiduciary duty": *Maguire v Makaronis* (1997) 188 CLR 449 at 473 and *O'Halloran v R T Thomas & Family Pty Ltd* (1998) 45 NSWLR 262 at 276-277 . What constitutes an adequate or sufficient connection is not predetermined or formulaic. Each case requires a precise focus on both the nature of the obligations and the nature of the breach: *Beach Petroleum* at 90 [431] and *Maguire* at 472-473 . Any question of "direct" or "immediate cause" is a red herring. The required focus is the nature of the obligations and the nature of the breach because different obligations and breaches may raise different criteria that supply the necessary connection. So, for example, "several matters appropriately will be taken into account when there falls for consideration, in an action against the fiduciary arising *other than out of breach of trust*, the criteria which supply an adequate or sufficient connection between the equitable compensation claimed and the breach of fiduciary duty" which may not be relevant in breach of trust cases (emphasis added): *Maguire* at 473.

1091. Indeed, as Spigelman CJ stated in *O'Halloran* , "[i]n the case of a trustee dealing with trust property, the law has proceeded beyond the invocation of the formulaic "common sense" approach to causation, by adopting a stringent test to the selection of those events preceding loss which are to be taken as causing the loss": at 276-277 . Spigelman CJ's reference to the "common sense" approach to causation was to the oft-stated proposition that a court will only make good losses that on a common sense view of causation were caused by the breach of fiduciary duty: *Beach Petroleum* at 90 [432] ; *Watson v Ebsworth & Ebsworth (a firm)* (2010) 31 VR 123 at 173 [160] ; *O'Halloran* at 272-273 ; *Ganson Enterprises Ltd v Boughton & Co* (1991) 85 DLR (4th) 129 at 163 and *Target Holdings Ltd v Redferns* [1996] 1 AC 421 at 439. So much may be accepted.

1092. Finally, the compensation payable for "breaches of fiduciary duty is assessed based on loss at the time of the trial with the full benefit of hindsight": *Wingecarribee Shire Council* at 260-261 [995] ; *Canson Enterprises Ltd v Boughton & Co* [1991] 3 SCR 534 at 555 applied in *Youyang Pty Ltd v Minter Ellison Morris Fletcher* (2003) 212 CLR 484 at 499 [35] ; see also *Parker, In the matter of Purcom No 34 Pty Limited (In Liq) (No 2)* [2010] FCA 624 at [23] .

1093. In this appeal, the criteria which supply the adequate or sufficient connection between the equitable compensation claimed and the breach of fiduciary duty is not reliance upon a misrepresentation. Here, the connection was established by LGFS' non-disclosure of material facts which the Councils were entitled to know in connection with their purchase of the notes and, in breach of which, LGFS sold the notes to the Councils: see [1080] above and *Maguire* at 472-473 .

1094. A question which then arises is whether, in light of that breach, LGFS was entitled to maintain the contention that "the disclosure would not have altered the [Councils'] decision to proceed with the transaction ...": *Maguire* at 471 and *Brickenden v London Loan & Savings Co* [1934] 3 DLR 465 at 469 ; see also *Hydrocool v Hepburn (No 4)* (2011) 279 ALR 646 at 711-714 [443]-[466] and the authorities there cited. LGFS submitted that the Court needed to be satisfied that the purchase of the Rembrandt notes was caused by an actionable non-disclosure on the part of LGFS, that the Councils would *not* have purchased the notes if the relevant disclosure had taken place *and* that the onus of proving this lay on the Councils: *Beach Petroleum* at 90-91 [432]-[433] and 94 [449]-[450] and *Watson v Ebsworth & Ebsworth* at 173 [160]-[162].

1095. A starting point for consideration of this contention is the observations of Lord Thankerton in *Brickenden* at 469, that:

> When a party, holding a fiduciary relationship, commits a breach of his duty by non-disclosure of material facts, which his constituent is entitled to know in connection with the transaction, he cannot be heard to maintain that disclosure would not have altered the decision to proceed with the transaction, because the constituent's action would be solely determined by some other factor, such as the valuation by another party of the property proposed to be mortgaged. Once the Court has determined that the non-disclosed facts were material, speculation as to what course the constituent, on disclosure, would have taken is not relevant.

These observations were cited with approval in *Commonwealth Bank of Australia v Smith* (1991) 42 FCR 390 at 394-395 ; *Wan v McDonald* (1992) 33 FCR 491 at 511 and 520-521 ; *Gemstone Corporation of Australia Ltd v Grasso* (1994) 62 SASR 239 at 243 and 252-253 and *Australian Securities and Investments Commission v Adler (No 3)* (2002) 20 ACLC 576 at 707. This passage has also been the subject of criticism: see, for example, *Maguire* at 489-492 .

1096. In this appeal, LGFS' contention fails. First, given the nature of the obligations and the nature of the breach, enquiries into whether the Councils' would have given informed consent were fruitless and irrelevant: see, by way of example, *Brickenden* at 469 and *Hydrocool* at 711-714 . That conclusion is not surprising. Unlike breach of trust cases, "[t]he consequences of such a conflict (the non-disclosure of material facts) are not discoverable. Both justice and policy are against their investigation": *Furs Ltd v Tomkies* (1936) 54 CLR 583 at 592 ; cf *Youyang* at 500-502 [38]-[44] .

1097. Second, contrary to LGFS' contention, *Beach Petroleum* at 90-91 [432]-[433] and 94 [449]-[450] and *Watson v Ebsworth & Ebsworth* at 173 [160]-[162] are not authority for the proposition that the onus lay on each Council to establish that it would *not* have purchased the Rembrandt notes if the relevant disclosure had taken place. On the contrary, as the Court of Appeal stated in *Watson v Ebsworth & Ebsworth* at 173 [161]-[162], "[t]he [C]ourt was entitled, with the full benefit of hindsight, not to speculate *against* the interests of the [Councils]", in respect of whom there was a breach of fiduciary duty. Here, LGFS was the defaulter. Its default was non-disclosure of material facts which the Councils were entitled to know in connection with their purchase of the notes and, in breach of which, LGFS sold the notes to the Councils. The Councils were obliged to establish "adequate or sufficient connection between the equitable compensation claimed and the breach of fiduciary duty". The Councils discharged that duty: see [1067]-[1084] above. If LGFS wished to contend otherwise, as a matter of fact, it should have adduced evidence or cross examined the Councils' witnesses. It did not.

1098. In this context, it must be recalled that the primary judge was satisfied that the Councils would not have purchased the notes if LGFS had disclosed its conflict: J[2321]. Given the views we have formed, that finding was unnecessary but nevertheless open on the evidence: see [1085]-[1097] above.

2.3.7. Contributory negligence / indemnity / apportionment in relation to fiduciary duty claim

1099. This is addressed in Part 13 below.

2.4 Negligence and negligent misstatement

2.4.1 Introduction

1100. Given our rejection of LGFS' Appeal Grounds in relation to fiduciary duty, this section of the judgment is arguably unnecessary. However, given the positions adopted by the various parties, it is appropriate to address these Appeal Grounds.

1101. The primary judge found that LGFS owed to the NRB Councils a duty which included a duty to exercise reasonable care and skill in: (a) analysing investments being considered on behalf of the NRB Councils and identifying the risks associated with the investment; (b) only recommending investments that were suitable for the NRB Councils and (c) properly providing the NRB Councils with all material information about the investment that might reasonably be considered as bearing upon the investment decision: J[2263]-J[2265].

1102. LGFS appealed. It again drew a distinction between the RB Councils and the NRB Councils. It did *not* dispute that it owed the duties identified in [1101] above to the RB Councils. In relation to the NRB Councils, LGFS did *not* dispute that:

1. In marketing the Rembrandt notes to the Councils, it owed a duty of care in relation to what it said to the Councils about the notes: *Tepko* at 16-17 [46]-[47] ;

2. It owed a duty to exercise reasonable care that any statements of fact were correct to the best of its knowledge: *South Australia Asset Management Corp v York Montague Ltd* [2007] AC 191 at 214 ; and

3. It also owed a duty to take reasonable care that any statements of fact or opinion derived from the application of its experience or other expertise reflected opinions that were honestly held and which were based on reasonable grounds: *Tipperary Developments Pty Ltd v State of Western Australia* (2009) 38 WAR 488 at 525 [162] .

1103. However, LGFS did contend on appeal that the primary judge erred in finding that it owed the duties identified in [1101] above to the NRB Councils and in holding that LGFS breached those duties of care: LGFS Appeal Grounds Matrix Rows 112-114. Those Appeal Grounds are rejected. In advising and recommending to the NRB Councils that they invest in the Rembrandt notes, LGFS undertook, or at the very least, in the circumstances objectively undertook, the obligations identified in [1101] above to each of the NRB Councils.

2.4.2 Factual analysis

1104. The finding at trial that LGFS owed the duties identified in [1101] to the NRB Councils followed analysis of the history of the relationship between LGFS and each of the Councils, including how LGFS marketed itself to the PA Councils. That analysis has been addressed in Part 8, Section 2.2 and Part 2 , Section 7 above.

2.4.3 Duty of care

1105. Were the duties identified in [1101] above owed to the NRB Councils? The answer is yes. First, the factual findings. LGFS was in an advisory relationship with the NRB Councils. It was not a mere salesman: see Part 8, Section 2.2 above.

1106. Second, the legal analysis. The primary judge's identification of the duties owed by LGFS to each of the NRB Councils was consistent with established principles relating to duties of care in circumstances where the parties are in a relationship of investment advisor and client. As the primary judge accepted (at J[2251]):

1. The core obligation of a financial advisor is to warn the investor of the "material risks" of a potential investment: *NMFM Property Pty Ltd v Citibank Ltd (No 10)* (2000) 107 FCR 270 at 366 [427]-[428] . A "material risk" is a risk to

which the investor would attach significance: *NMFM Property* at 366 [427]-[428] citing *Rogers v Whittaker* (1992) 175 CLR 479 at 490.

2. An investor is entitled to be warned of the fact that projected rates of return and growth might not be achieved and that there is an element of commercial risk-taking involved for which the investor must be prepared to take responsibility: *NMFM Property* at 365-366 [425] ; see also, *Paige v FPI Limited* [2001] NSWSC 627 at [193] .

3. Where an investor has suffered a loss because the investment was "unsuitable" for them, such that no financial advisor would have made an unqualified recommendation in the circumstances, the advisor will be liable to put the investor back in the position they would have been in had they not invested: *NMFM Property* at 375 [468] .

LGFS did not identify any error in these factual findings or the legal analysis.

1107. Instead, on appeal, LGFS identified two "errors" in support of its contention that the primary judge erred in finding that LGFS owed the duties identified in [1101] to the NRB Councils. First, LGFS submitted that the primary judge's finding that LGFS owed those duties based upon LGFS' status as a financial advisor would "cut across the statutory regime applicable to such parties" under the *Corporations Act* . Second, LGFS submitted that such a duty could only be found to exist if LGFS undertook, or was taken in the circumstances to have objectively undertaken, to perform those obligations to each of the NRB Councils (which LGFS submits it did not undertake to do). Both these so called errors are rejected.

2.4.3.1 Conflict with LGFS' statutory duties as investment advisor?

1108. On appeal, LGFS submitted that the fact that LGFS sought to sell, and succeeded in selling, the Rembrandt 2006-3 notes to the NRB Councils could not justify the imposition of the duties identified in [1101] above. As we have said, the basis for this submission was that the primary judge's finding that LGFS owed those duties based upon LGFS' status as a financial advisor would "cut across the statutory regime applicable to such parties" under the *Corporations Act* .

1109. These contentions fail for a number of reasons. First, at trial, LGFS did not contend that the *content* of these duties of a financial advisor was inconsistent with the statutory regime in the *Corporations Act* regulating the conduct of financial advisors. The alleged inconsistency was only relied on by LGFS if LGFS was found to be a mere salesman. The primary judge correctly rejected the contention that LGFS was a mere salesman: see [1023]- [1024] above and J[2262].

1110. Second, the factual and legal bases for LGFS' contention that the duties would "cut across the statutory regime applicable to such parties" under the *Corporations Act* is wrong. At a factual level, LGFS was not a salesman, it was a financial adviser: see [1023]-[1024] above.

1111. Legally, there is *no* disconformity between the statutory provisions identified by LGFS and the content of the duties identified in [1101] above: *Ingot Capital Investments Pty Ltd v Macquarie Equity Capital Markets Ltd (No 6)* (2007) 63 ACSR 1 at 140 [540(7)] and 148 cf [588]. That last statement requires further explanation.

1112. It is first necessary to understand the reason for the "disconformity principle". The fundamental issue is the coherence of the law. The law recognises that "[t]here are cases ... where to find a duty of care would so cut across other legal principles as to impair their proper application and thus lead to the conclusion that there is no duty of care of the kind asserted: *Sullivan v Moody* (2001) 207 CLR 562 at 580 [53] . So, for example, a common law duty of care "should not be found if that duty would not be compatible with other [statutory] duties which the respondents owed": *Sullivan* at 581 [55] . Therefore, a "common law duty of care cannot be imposed on a statutory duty if the observance of such common law duty of care would be inconsistent with, or have a tendency to discourage, the due performance by the local authority of its statutory duties": *X (Minors) v Bedfordshire County Council* [1995] 2 AC 633 at 739 and *Sullivan* at 574 [30] . Here, the duties imposed by the primary judge in no way impair the application of the existing statutory regime, are not inconsistent with the other duties LGFS owed under the *Corporations Act* and do not discourage the performance of those obligations.

1113. Second, and in any event, *Ingot (No 6)* at 140 [540(7)] and 148 [588] does not support LGFS' submission. *Ingot (No 6)* at 140 [540(7)] is authority for the uncontroversial principle that the relevant statutory and common law context is relevant to the determination whether a duty of care should be imposed in a particular case. The finding at 148 [588] that "[w]here the legislature has seen fit to prescribe rights and liabilities ... , the courts should be slow to engraft their own scheme of protection, ... [t]hey should be slow to find gaps where the legislature has created a self-contained and detailed scheme of protection" is not applicable in the current circumstances.

1114. LGFS referred to two specific aspects of the *Corporations Act* which it submitted conflicted with the duties identified in [1101] above: (1) the fact that there are no statutorily implied terms governing the *sale* of financial products comparable to those for the sale of goods and (2) to the extent that any duty might be thought to arise out of LGFS' status as a "financial advisor", LGFS referred to s 912A and what it termed the "limited" disclosure obligations in ss 941A, 944A and 949A .

1115. The fact that there are no statutorily implied terms governing the *sale* of financial products comparable to those for the sale of goods is interesting but irrelevant. LGFS was not a salesman, it was a financial adviser: see [1023]-[1024] above.

1116. The other provisions do not assist LGFS. The statutory obligations of the holder of an AFSL are identified in s 912A . The fact s 912A does not contain a duty in the terms or of the character identified in [1101] above is again interesting but irrelevant. The section, headed "General Obligations", requires a holder of an AFSL, among other things, to "do all things necessary to ensure that the financial services covered by the [AFSL] are provided efficiently, honestly and fairly". The imposition of a duty in the terms or of the character identified in [1101] above is neither inconsistent with, nor cuts across, these general obligations.

1117. The next set of provisions referred to by LGFS was the statutory disclosure obligations imposed on LGFS by ss 941A, 944A and 949A of the *Corporations Act* . LGFS accepted that none of these statutory disclosure obligations were engaged. And the fact that the provisions existed and, further, were not engaged is again interesting but irrelevant. They are interesting but irrelevant because the disclosure obligations in relation to advice provided to wholesale investors is not prescribed by statute.

1118. LGFS' contention (as we best understood it) that, in the absence of statutory provisions regulating such conduct, the legislature intended that no duty of care would arise in relation to wholesale investors is without foundation. As a matter of legal and commercial sense, it is unsurprising that the *Corporations Act* does not impose blanket disclosure obligations in relation to wholesale investors, but that common law obligations may be owed to particular wholesale investors in circumstances where the salient features giving rise to a duty of care are present.

2.4.3.2 LGFS undertook, or was to be taken to have undertaken, to perform those obligations to each of the NRB Councils?

1119. LGFS submitted that finding was not open to the primary judge. We disagree. The primary judge found that the salient features giving rise to a duty of care were present (see [1068] -[1069] above and J[2265]) and, in the circumstances, found it appropriate to impose a duty of disclosure: see [1074]-[1075] above and J[2262].

1120. LGFS undertook, or is to be taken in the circumstances of the case to have undertaken, the particular obligations in question in relation to *each* NRB Council. In this context, it is necessary to recall that whilst in some cases LGFS expected a NRB Council to consider whether it had the funds available to invest, LGFS expected, or it was objectively reasonable for it to expect, that the NRB Councils would treat the advice from LGFS as a recommendation that they in fact invest in the product subject only to the availability of surplus funds: see [1024] and J[2149]-J[2150].

2.4.4 Breach of duty: J[2157]-J[2169]

1121. LGFS challenged the primary judge's finding that LGFS breached each of the duties (see [1101] above) that it was held to owe to each of the PA Councils: LGFS Appeal Grounds Matrix Row 114.

1122. On appeal LGFS identified three "errors":

1. The primary judge's findings as to LGFS' commercial objectives in selling the Rembrandt notes overstated the importance of the Rembrandt transaction to LGFS' business, such that the primary judge erred in finding that LGFS was blinded to any deficiencies in the product by its need to sell the notes;

2. There was no "obvious justification" for the primary judge's finding that investment in the Rembrandt notes was not suitable for any local council at any time. According to LGFS, there were some investors including some local councils for whom the Rembrandt notes were an appropriate investment and whether the notes were suitable for the PA Councils required a council-by-council analysis; and

3. With respect to the RB Councils, LGFS' duty to those councils would not have been breached unless LGFS could not reasonably have held the view that the Rembrandt notes were appropriate to those councils' circumstances and the evidence did not justify such a conclusion.

It is important to understand that, except for these three "errors", LGFS made no other complaints about the approach adopted by the primary judge.

1123. It is therefore necessary to understand what the primary judge in fact did. Her Honour made critical findings that by "offering the [PA Councils] this unsuitable product [the Rembrandt notes] and/or failing to properly identify the risks associated with a repurchase by ABN Amro from LGFS (and thus LGFS from the [PA Councils]) .... and not properly providing the [PA Councils] with information material to their investment decisions, LGFS breached its duty of care to the [PA Councils]": J[2272].

1124. Those findings were not made in a vacuum. The primary judge supported each finding by detailed reasons, reasons which were clearly open on the evidence: see Part 2 , Section 7 and Part 8, Section 2.2 above.

1125. First, LGFS believed that the Rembrandt notes were a "grotesquely complicated" financial instrument but failed to disclose this to the PA Councils: see [90] above. As a result, the PA Councils did not appreciate "that they were investing in something unlike anything they had ever invested in before": J[2268]. And the fact that the product was extremely complicated was a factor that the PA Councils would have taken into account in assessing their willingness to invest in the Rembrandt notes: see, for example, [103]- [104] above and J[2268].

1126. Second, LGFS failed to disclose to the PA Councils that the Rembrandt notes could be highly volatile: see [128]-[130] above. The primary judge observed that "[g]iven the nature of local government it should have been obvious to LGFS, as experts in local government financial markets, that although councils might intend to hold an investment for the term it was possible, even likely, that they would be subject to contingencies which might require an investment to be liquidated": J[2269]. The duty LGFS owed to the PA Councils required LGFS to disclose to the PA Councils that there was a high likelihood that the Rembrandt notes could trade significantly below par and that if the PA Councils wanted to sell the notes prior to maturity they may be forced to sell the notes substantially below their par value. As the primary judge noted, "[i]n circumstances where LGFS was offering to repurchase at market value on 24 hours' notice, the [PA Councils] needed to know that the product could be highly volatile": see [128]-[130] above and J[2269].

1127. Next, LGFS failed to disclose to the PA Councils the "performance and modelling risk" of the Rembrandt notes. LGFS knew that the performance of the Rembrandt notes was highly path dependent (see [129] above) and therefore "LGFS understood not only that the product could be highly volatile but why it could be highly volatile": see [129] above and J[2270]. LGFS also understood that "S&P's rating was based on modelling of the performance of the product assuming multiple different spread paths and that ... there was a risk that past performance may not be representative of future performance, current modelling assumptions are unlikely to be consistent with actual performance of the CPDO, and key modelling assumptions were as set out in S&P's base case assumptions": see [62] above and J[2270]. Again, by reason of the duty LGFS owed to the PA Councils, the primary judge found that the PA Councils were reasonably entitled to rely on LGFS disclosing the performance and modelling risk associated with the Rembrandt notes, but LGFS failed to disclose this risk: see, for example, [128]- [130] above and J[2270]. No other conclusion was open.

1128. Finally, the primary judge identified a number of material matters relevant to the PA Councils' investment decision which the PA Councils needed to know about and reasonably relied on LGFS to ensure that they did in fact know about but which LGFS failed to disclose or adequately disclose to the PA Councils. Those matters were listed at J[2271] as follows:

> (a) the product was not designed, developed or tailored for councils but was created for wholesale investors who, as ABN Amro put it, wished to diversify their current structured credit portfolio (a description which, by definition, excluded Bathurst, Narrandera and Murray): [see [62] and [65] above];
>
> (b) LGFS was promising only to repurchase the notes at market value on 24 hours' notice by a back-to-back arrangement with ABN Amro so that the amount LGFS would pay any council as so-called market value would be the same as the amount ABN Amro paid to LGFS in circumstances where that amount would not necessarily be the same as and may be lower than the net asset value of the note at the time having regard to ABN Amro's assessment of supply and demand: [see [84] and [130] above];
>
> (c) the performance of the product, including its volatility, depended on the evolution of credit spreads on the two indices over the term: [see [62] above];
>
> (d) the tightening of credit spreads which was occurring immediately before the issue of Rembrandt 2006-3 could be adverse to the performance of the product given its dependence on the evolution of credit spreads: [see [62] above]; and
>
> (e) for those councils which invested after 22 March 2007, S&P had issued its CPDO Evaluator which disclosed that S&P would use a different approach to rating instruments such as the product in the future so that, if the product had been issued later, it would not have obtained a rating of AAA from S&P: [see [366] and [368] above].

The references in brackets identify the evidentiary bases for these findings.

1129. It is therefore unsurprising, that, having regard to these matters (taken separately or cumulatively), the primary judge was satisfied that LGFS' dealings with the PA Councils involved breaches of its duty of care to them to: (a) properly analyse any investment being considered on behalf of a client and identify the risks associated with the investment; (b) only recommend investments that are suitable for the client and (c) to properly provide the client with all material information about the investment that might reasonably be considered as bearing upon the investment decision.

1130. As the primary judge said (at J[2272]):

> In offering the [PA Councils] this unsuitable product and/or failing to properly identify the risks associated with a repurchase by ABN Amro from LGFS (and thus LGFS from the councils) – namely that ABN Amro would determine the price having regard to

> supply and demand and not necessarily the net asset value of the notes at the time – and not properly providing the council with information material to their investment decisions LGFS breached its duty of care to the [PA Councils].

1131. It is against that background that the three "errors" identified in [1122] above must be considered.

2.4.4.1 LGFS' commercial objectives

1132. LGFS' contention on appeal was that the primary judge's findings as to the importance of the Rembrandt transaction to LGFS' business were not supported by the evidence. This contention is rejected. The evidence did support the findings. Moreover, given the nature and significance of the other findings of non-disclosure, the contention goes nowhere.

1133. First, the evidence. We reject the contention that the primary judge's findings as to the importance of the Rembrandt transaction to LGFS' business were not supported by the evidence: see Part 2 , Sections 6 and 7 at [90], [98]-[108] and [118]-[124] above and at Part 8, Section 2.2, especially at [1021]-[1024] and [1029]-[1030] above.

1134. Next, the futility of the contention. It must be recalled that LGFS' "commercial objectives" were addressed in the context of the PA Councils' claims for breach of fiduciary duty. The PA Councils did not know, and were not told by LGFS, of the commercial pressures LGFS faced and which made its sale of the notes commercially imperative. That failure placed it in an immediate position of conflict: see Part 8, Sections 2.1-2.3 above.

1135. The essential elements of LGFS' breach of fiduciary duty were the non-disclosures identified in Part 8, Section 2.3 above, especially at [1074]-[1078]. However, the legal significance of the non-disclosures did not stop with the fiduciary duty claims. The non-disclosures to the PA Councils necessarily had an effect on LGFS' performance of its other legal obligations. The findings (see [1128]) above identified deficiencies in LGFS' marketing material. It was the consequences of those deficiencies that were assessed in deciding whether the duty found to be owed was breached. The so-called "importance" of the Rembrandt transaction to LGFS' business is a red herring. Regardless of the level of its "importance", LGFS was obliged at least to disclose the matters identified at [1074] above. It did not. Those non-disclosure findings existed independently of any assessment of the significance of the Rembrandt notes to the viability of LGFS' business. As we have said, those non-disclosure findings identified deficiencies in its marketing of Rembrandt to the PA Councils.

2.4.4.2 Suitability of Rembrandt for local councils

1136. LGFS submitted that the primary judge's finding (at J[2164]) that the Rembrandt notes were not suitable for any council at any time was wrong. LGFS submitted that:

> The fact that an investment in the CPDO would expose a council to the additional risk, beyond the risk of default, of suffering a capital loss should it be required to sell in adverse circumstances was a factor to be taken into account but did not of itself mean that the CPDO should be off limits. Whether or not the CPDO was unsuitable for a particular council would depend on various factors, including the size and structure of the Council's investment portfolio, its perceived cash flow and liquidity requirements, etc.

1137. LGFS' contention goes nowhere. LGFS' selection of one sentence from a lengthy and detailed judgment, out of context, is inappropriate. LGFS' contention ignores critical findings. Those critical findings extend to the following matters. First, the representations made by LGFS to the PA Councils: see Part 8, Section 2.2.2 above, especially at [1026], and J [2147]. These were LGFS' oral recommendations to the PA Councils. Those recommendations were made in a particular context: Part 8, Section 2.2.3 above.

1138. It is therefore unsurprising that the primary judge found (at J[2148]) that each of those matters constituted an opinion intended to induce the council officers to invest in the product and that, considered in context, many of them constituted a recommendation to invest in the product. As we have said (at [1120]) above, it was apparent from the overall circumstances and course of dealings between each of the PA Councils and LGFS over many years that LGFS expected and intended that the PA Councils would rely on its advice that the Rembrandt notes were suitable for the PA Councils and were safe, secure, robust and sound in making a decision to invest: J[2150].

1139. That leads us to the second basis for rejecting LGFS' contention. As the primary judge said (at J[2164]), "[i]f it is assumed that LGFS in fact held the opinion that the investment was suitable for a council (that is, any council which had the available funds) to make then, nevertheless, … the opinion was not based on reasonable grounds and was not the product of the exercise of due care and skill. LGFS should have known that an investment that might be highly volatile was not a suitable investment for any council to make at any time".

1140. The primary judge's finding that LGFS' opinion that investment in the Rembrandt notes was suitable for a council was *not* based on reasonable grounds and was *not* the product of the exercise of due care and skill was correct. Two important aspects of the Rembrandt notes demonstrate why this finding was open and correct.

1141. First, the liquidity of the Rembrandt notes. Liquidity of an investment was an important factor to the PA Councils (apart from Ryde) who may have needed the funds invested for public purposes: see [130] above. That fact was known to LGFS: see [130] above. Indeed, LGFS emphasised the "next day liquidity" of the Rembrandt notes in its marketing material: see [130] above. However, the council officers were not told that there was no secondary market for the Rembrandt notes or that the market value of the notes may not be the face value and substantially below par if they chose (or were forced) to sell them before maturity: see [90] and [130] above. This was a major risk of investing in the Rembrandt notes which affected the suitability of the product as an appropriate investment for the PA Councils.

1142. Second, the volatility of the Rembrandt notes. LGFS knew that the Rembrandt notes were not just volatile but "highly volatile" (see [129] above) and that this was a factor which was highly material to its suitability as an investment for the PA Councils: see [129] above. This aspect had nothing to do with the rating: see [130] above. LGFS knew that the PA Councils needed to be able to liquidate investments as it knew the 10 year term of the Rembrandt notes would be an "eyebrow raiser": see [130] above. LGFS' statement about volatility was in the fine print of the LGFS Community Income Notes Brochure (see [128] above), which was drafted to emphasise LGFS' 24-hour liquidity promise instead: see [128]-[130] above. In short, LGFS knew that the high volatility of the notes was an important factor and LGFS chose to emphasise its liquidity promise without any corresponding emphasis about the potential for high volatility: see [128]-[130] above.

1143. LGFS submitted that the primary judge's finding that the Rembrandt notes were not suitable for any council at any time was "contrary to the view of market participants in 2006". LGFS did not pursue a defence at trial that the recommendation of the Rembrandt notes to the PA Councils was reasonable by reference to standard industry practice. The PA Councils did not adduce evidence in relation to this issue. LGFS should not be permitted to raise this contention on appeal: *Coulton* at 7-8 . In any event, the contention is not substantiated by the evidence: see, for example, [135] and [139] above. LGFS' submission referred to a fragment of advice from Grange Securities Ltd to Moree: see [139] above. That fragment must be read in context. That statement was not an endorsement of the product. In fact, the statement was given in limited terms in the context of the prior disclosure that the investment was likely to be suitable for investors "[a]ble to cope with a high level of potential volatility in NAV" and "[a]ble to invest for a 10-year period – while intended liquidity arrangements through making a market appear reasonable, *there is no guarantee of liquidity in all market conditions*": see [135] above. No, less significantly, as the primary judge noted, the fact that Grove Research and Advisory sold the Rembrandt notes to three unidentified "clients" did not establish that it held the view that the investment was suitable for councils: J[1113].

1144. The final aspect of LGFS' complaint under this heading was that the primary judge was required to undertake a council-by-council analysis to assess the suitability of the product and that her Honour failed to do so. LGFS submitted that "[t]he proper conclusion was that Rembrandt was not for everyone but there were some investors (including *some* local councils) for whom it was an appropriate investment to include in their portfolio" (emphasis added). LGFS addressed the RB Councils and the NRB Councils separately.

1145. In relation to the RB Councils, LGFS accepted that, in recommending Rembrandt 2006-3, it owed a duty to take reasonable care to ensure that it was a suitable product for each of them. However, LGFS submitted that its obligation to the RB Councils was only to take reasonable care, such that it will only have breached its duty if it could not reasonably have held the view that the Rembrandt notes were suitable for the RB Councils. There are three answers to that contention. First, LGFS could not reasonably have held the view that the Rembrandt notes were appropriate to those Councils' circumstances. They were not: see [1141]- [1142] above.

1146. Second, whether LGFS breached its obligation to the RB Councils to take reasonable care to ensure that the Rembrandt notes were a suitable product is *not* answered by simply enquiring whether LGFS could reasonably have held the view that the Rembrandt notes were suitable for the RB Councils. It ignores the more extensive duties LGFS owed to the RB Councils: see [1101] above. LGFS breached those duties: see [1121]-[1131] above.

1147. Third, even if in assessing whether LGFS breached its obligation to the RB Councils to take reasonable care to ensure that the Rembrandt notes were a suitable product, it was sufficient to simply enquire whether LGFS could reasonably have held the view that the notes were suitable for the RB Councils (a view we do not accept), the material referred to on appeal by LGFS did not support such a finding. So, for example, LGFS submitted that it discharged that duty because:

> Corowa was a long-term and enthusiastic investor in structured products, including CDOs. It had clearly adopted the practice of holding a significant proportion of its portfolio in such products. Although Cooma's track record was shorter, it too had a portion of its portfolio in long-term and structured products. On the face of it, both Councils met Grove's criteria for investors for whom Rembrandt would be suitable.

1148. The "Grove criteria" which LGFS referred to as indicative of the suitability of the Rembrandt notes to Cooma and Corowa were merely "Indicative Investor Profiles" (see [135] above) which indicated the types of investors to whom the product *might* be suitable to offer. That statement was unsurprising. As the Grove Report itself stated, "[y]our Grove advisor can recommend whether these notes fit into your portfolio strategy": see [135] above. We therefore reject LGFS' contention that it was reasonable for it to recommend the Rembrandt notes to the RB Councils because it now considers that they fit "on their face" into Grove Research and Advisory's indicative criteria for investors who could consider the investment.

1149. LGFS owed the RB Councils a duty to investigate and only recommend investments which it concluded were suitable to those Councils in the circumstances. Whether or not Cooma and Corowa fit "on their face" into Grove Research and Advisory's indicative criteria for investors, unsurprisingly, was not an issue at trial. And it was not an issue at trial because even if they did fit the criteria, the criteria are no more than indicative. In other words, even if the RB Councils did fit the criteria (about which there was no evidence and no findings), that fact alone would not establish that it was reasonable for LGFS to recommend the Rembrandt notes as a suitable investment.

1150. Of course, even if LGFS had reasonable grounds to believe the Rembrandt notes were suitable to Cooma and Corowa (a view we do not hold), that would not discharge LGFS' common law and contractual duty to disclose all material facts relevant to the decision to invest, which, for the reasons outlined at [1132]- [1135] above, LGFS did not do.

1151. LGFS complained that the RB Councils did not attempt to demonstrate that some other product was more suitable for them and that LGFS could have and should have recommended that product. That contention is, at best, misguided. There was no obligation on the RB Councils to establish what LGFS should have done so as *not* to be negligent or in breach of its contractual obligations. The RB Councils were obliged to establish that by recommending the Rembrandt notes to the RB Councils, LGFS was in breach of the duties of care it owed to them. The primary judge correctly found that LGFS breached those duties: see [1121]-[1131] above.

1152. That leaves the NRB Councils. Their position is addressed at [1024] above. LGFS did not have reasonable grounds to believe the Rembrandt notes were suitable for those Councils.

2.4.5 Other representations and non-disclosures

1153. LGFS accepted that it owed duties of care in what it said when marketing Rembrandt notes to the PA Councils. The issue of breach of duty will be addressed in the context of the statutory claims for misleading or deceptive conduct in Part 8, Section 3 below.

3. STATUTORY CLAIMS

3.1 Introduction

1154. LGFS was found to have contravened ss 1041H(1) and 1041E(1) of the *Corporations Act* and s 12DA of the *ASIC Act* . In particular, LGFS was found to have engaged in misleading and deceptive conduct, and, in one respect, the publication of information or a statement false in material particulars, and otherwise found to have made negligent misrepresentations to the PA Councils about the Rembrandt 2006-3 notes. It was also found to have breached its AFSL in advising the PA Councils about, and selling to them, the Rembrandt notes because the notes were not a debenture and thus not a security but a derivative under the *Corporations Act* in which LGFS was not licensed to deal. LGFS appealed: LGFS Appeal Grounds Matrix Rows 118 and 119.

3.2 Section 1041H of the *Corporations Act*

1155. Under s 1041H of the *Corporations Act* , "[a] person must not, *in this jurisdiction*, engage in conduct, in relation to a financial product or a financial service, that is misleading or deceptive or is likely to mislead or deceive" (emphasis added): see [724] above.

1156. The statutory question was whether LGFS engaged in conduct in relation to a financial product (the Rembrandt notes) or a financial service which was misleading or deceptive. The primary judge concluded that it had. The primary judge's conclusions that the PA Councils' acquisition of the Rembrandt notes from LGFS involved the acquisition of a financial product and LGFS' conduct in selling the Rembrandt notes to the PA Councils was dealing in a financial product and providing a service, including giving financial product advice, were not challenged by LGFS: J[2119]-J[2132]. Significantly, none of the findings depended on LGFS being in an advisor relationship with the PA Councils. That question does not arise on the proper construction and application of s 1041H of the *Corporations Act* .

1157. What then was the misleading or deceptive conduct? There were two separate groups of findings. The first was that LGFS represented to each of the PA Councils that the Rembrandt notes were a suitable investment. These representations were conveyed by LGFS orally and in its various promotional statements: see, by way of example, [125] above. The primary judge found that the representations were misleading or deceptive because Rembrandt 2006-3 was not a suitable investment for the PA Councils and LGFS should have known this to be so: J [2160]-J[2164]. The factual bases for these findings are the same as those addressed in Part 8, Section 2.4 above, especially at Part 8, Section 2.4.4. LGFS' appeal against those findings is dismissed for the same reasons.

1158. The second group of findings related to discrete misrepresentations or non-disclosures by LGFS. The findings may be summarised as follows:

1. Representing (to Bathurst) that Rembrandt 2006-3 was "not a CDO or like a CDO" and otherwise failing to properly disclose the nature of the product as a "highly complex structured credit derivative": J[2174], J[2182]-J[2185] and J [2271(a)] and [1041] above;

2. Representing that Rembrandt 2006-3 had been designed or tailored by LGFS for local councils when it had not: J[2172] and J[2271(a)] and [131] above;

3. Representing that Rembrandt 2006-3 was a good or sound investment, without properly disclosing the notes' potential NAV volatility, and in particular its dependence on the evolution of credit spreads, and implications of the then current low spread environment: J[2171], J[2186]-J[2187], J[2189]-J[2190], J[2198], J [2269]-J[2270], J[2271(c)] and J[2271(d)]), and [125]-[130] above;

4. Representing that LGFS would buy the product back, without properly disclosing that LGFS' undertaking to repurchase the product at "market value" did not mean NAV: J[2188] and J[2271(b)], and [90] and [130] above;

5. Failing to disclose the disclaimer in the Surf Presentation concerning "modelling risk": J[2199]-J[2200] and J[2270] and [125]-[130] above (with the exception of Eurobodalla, the Rembrandt 2006-3 notes were not marketed on the basis of the Surf Presentation);

6. Failing to disclose to the Councils considering the purchase of Rembrandt 2006-3 notes after March 2007 that S&P had developed a new CPDO Evaluator for rating future CPDO issues: J[2207(a)], J[2209] and J[2271(e)], and [142] above;

7. Representing that a cash out was very unlikely and Rembrandt 2006-3 was very robust: J[2175] and [1044] above; and

8. Representing that Rembrandt had been designed, or was likely, to cash in early: J[2175].

1159. LGFS did not appeal against the first finding. It appealed against each of the other findings on the grounds that: (1) some of the findings of misrepresentation and non-disclosure should not have been made on the facts; (2) some findings as to what LGFS knew or should have known acting reasonably went too far and (3) the PA Councils did not demonstrate that any misconceptions about Rembrandt 2006-3 which they may have had, or the misjudgements they may have made in investing "were the responsibility of LGFS".

1160. None of these submissions have merit. The primary judge found that LGFS contravened s 1041H(1) of the *Corporations Act* and s 12DA of the *ASIC Act* in marketing and selling the Rembrandt 2006-3 notes to the PA Councils. The primary judge said (at J[2232]):

> LGFS engaged in misleading and deceptive conduct in relation to a financial product and in providing a financial service in the manner proscribed by each provision. The councils were misled by and as a result of LGFS's conduct about many material aspects of the investment as identified. They invested in reliance on their erroneous beliefs induced by LGFS's conduct. I am also satisfied that LGFS's contravening conduct, at least on a prima facie basis, materially contributed to the loss and damage the councils suffered when the investment cashed out even though the councils also relied on the mere fact of the AAA rating on interest and principal by S&P which LGFS was, as it is said, passing on to the councils as S&P's representation rather than its own.

1161. That conclusion was preceded by a detailed analysis of the pleaded case and the evidence, both generally and in respect of each of the Councils. LGFS' challenge to that analysis was largely undirected. It fell under five headings – (1) the "conservatism" of the Councils; (2) LGFS' perception of the Councils' understanding of structured products; (3) oral presentations to the Councils; (4) the nature of the product and (5) challenges to specific representations. It is necessary to address each.

3.2.1 'Conservatism' of Councils

1162. The significance of the matters under this heading to a challenge to the primary judge's finding that LGFS had engaged in conduct in contravention of s 1041H of the *Corporations Act* was not readily apparent. The primary judge made a finding that each Council was "conservative": J[1642], J[1937] ("[i]n common with all of the councils Murray was a conservative and risk averse investor") and J[1996]. (As to the Councils individually: J[1500]-J[1501], J[1504], J[1533] and J[1573] (Parkes); J[1629]-J[1630] and J[1641]-J[1642] (Orange); J[1662] and J[1665]-J[1666] (Moree); J[1698], J[1709] and J[1714(3)] (Oberon); J[1754] and J[1777] (Deniliquin); J[1849], J[1854]-J[1855], J[1857], J[1861] and J[1867] (Narrandera); J[1936]-J[1938], J[1944], J[1949], J[1963]-J[1964] and J[1973] (Murray); J[1996] (Cooma); J[2038], J[2041]-J[2042] and J[2056] (Narromine) and J[2083], J[2087] and J[2104] (Ryde)).

1163. LGFS challenged the primary judge's description of Eurobodalla as a "conservative" investor: J[1477]. In support of that finding, the primary judge identified that Eurobodalla operated well inside the Ministerial Order and Investment Guidelines and saw the security of its funds as very important. LGFS submitted that findings that it was aware of Eurobodalla's "conservative" requirements (see, for example, J[1482(a)] and J[1477]) had to be understood in context. LGFS' complaint was that even if Eurobodalla was relatively conservative compared with other investors, it needed to be recognised that the label ("conservative" investor) was being applied to a local council which was investing a significant proportion of its assets in structured products (including CDOs) which were not principal protected, could fluctuate in value and for which there was no ready market if they needed to be sold to raise cash. LGFS submitted that a similar analysis applied to other Councils.

1164. As LGFS put it:

> Not all of [the Councils] invested in complex structured products to the same extent as Eurobodalla (although Corowa, Parkes, Ryde and Moree did). But none of the Councils which did invest in CDOs apparently regarded such investments as detracting from their status as risk-averse investors concerned above all with the protection of capital. Even the Councils which had not previously invested in structured products invested in higher-yielding and lower rated FRNs without considering that they were being anything other than "conservative".

1165. The relevance of these matters was not and is not apparent. Moreover, LGFS' submission was wrong. It inaccurately summarised the PA Councils' investment portfolios and ignored the primary judge's findings concerning LGFS' knowledge of local government investment requirements (see [1024] above) and the PA Councils' individual investment strategies. For present purposes, it is sufficient to take Eurobodalla by way of example: see J[1476]-J[1495]. As the PA Councils submitted, Eurobodalla had a historical preference for term deposits. Eurobodalla's 2002 and 2005 investment policies specified that "[t]he order of priorities are first, the preservation of capital, second the maintenance of liquidity and third, maximum return on investment". Its investments in CDOs increased substantially after November 2005 when it entered into an Individually Managed Portfolio (or IMP) Agreement with Grange Securities Ltd under which Grange traded CDOs "by default" on Eurobodalla's behalf: J[1480]. Eurobodalla's draft investment policy, sent to LGFS sometime in 2003, stated that "[t]here is an emphasis on capital protection and risk reduction rather than an aggressive approach to high earnings/growth". Eurobodalla was bound by, and complied with, the Ministerial Order. None of these facts support a finding that it was reasonable for LGFS to conclude that Eurobodalla was anything other than a conservative investor. A similar analysis may be applied to the other PA Councils.

1166. There are, however, more basic flaws in LGFS' argument. The fact that a Council increased its investment in CDOs (or an equivalent product) does not support a finding that that Council was not conservative. It merely suggests that the composition of that Council's portfolio changed over time. Change was inevitable as the application of the relevant ministerial orders changed from time to time, including the reference to permitted investments in products with S&P credit ratings of A or above: see [19] above. Finally, and no less significantly, LGFS' submission ignores the evidence of council officers, including evidence that they believed the investments were "conservative": see, for example, J[1714], J[1777], J[1949], J[1963] and J[2083].

3.2.2 LGFS' perception of the Councils' understanding of structured products

1167. LGFS challenged aspects of the primary judge's findings (see [1029(1), (4) and (5) above), namely:

1. Given the nature of the S&P Reports and the ABN Amro term sheet, LGFS' knowledge of the fact that council officers did not understand CDOs and the lack of any questions based on the S&P Reports or ABN Amro term sheet, LGFS could not have believed that the PA Councils read either document before deciding to invest, nor that council officers actually understood the product or its risks from those documents: J[1348];

2. LGFS knew that the council officers would not have understood the material they had been provided: J[1343], J[1348], J[1395], J[1451], J[1566(2)] and J[1682]; and

3. LGFS was fully aware (or ought to have been aware) of the lack of financial sophistication of the PA Councils and that they would not understand the complex nature of the product: J[1282].

1168. LGFS sought to support these challenges by reference to four matters:

1. The PA Councils' previous investment in structured products;

2. LGFS was dealing with the PA Councils as institutions and it was not privy to the PA Councils' internal deliberations concerning the Rembrandt notes;

3. The contents of the documents it provided to the PA Councils and their response to those documents; and

4. The particular circumstances attaching to Eurobodalla.

Each will be addressed in turn.

3.2.2.1 Previous investment in structured products and therefore necessary knowledge

1169. LGFS submitted:

> … Her Honour quoted internal LGFS board papers from 2005 and 2006 which stated that local councils generally lacked understanding of, or the ability to analyse, CDOs and other structured products then on the market [J[1004]- [1005] and J[1036]]. Later at various points in the judgment, she relied on this material in support of findings that the Councils did not understand Rembrandt and that LGFS knew or ought to have appreciated that this was so: see for example [J[1282], J[1317], J[1395] and J[1402]]. She also suggested that LGFS should have realised that (on her findings) the Council officers were not reading or were not understanding the documents provided to them by LGFS: [J[1348]].
>
> The views found in LGFS's board papers were generalisations across local councils as a whole. They did not necessarily apply to all the Councils which were offered Rembrandt by LGFS.
>
> Most of the Councils had previously purchased CDOs and some had purchased other more exotic structured products. In the course of this, the Council officers were exposed to numerous presentation documents, research reports and the like. Promoters of CDOs, such as Grange, also conducted seminars on structured products. It could not be assumed that none of this would have had any effect. Certainly LGFS might reasonably assume that previous dealings with CDOs had given the Councils sufficient appreciation of the issues involved to know the types of risk involved and to be able to ask about the risks or features which concerned the councils. Mr Michell's marketing report of November 2006 referred to the positive response to Rembrandt "both by Councils who have a good understanding of CDO & CPPI and others who are having a structured product explained to them for the first time": [J[1094]]. The Councils who were the subject of the report and who had previously invested in structured products included Oberon, Moree and Narromine.

1170. LGFS contended that it was reasonable for LGFS to assume that previous dealings with CDOs had given the PA Councils sufficient appreciation of the issues involved to be aware of, and understand, the types of risks involved and to be able to ask about the risks which concerned the PA Councils. LGFS' challenges to these findings are untenable. Aspects of these submissions have already been addressed in Part 8, Section 2.2.5.1 under the heading "Challenge 1: Whether the witnesses were the decision makers and the availability of other potential advisers". The same criticisms apply here. LGFS was selective in the evidence it referred to in support of its challenges.

1171. LGFS first referred to some aspects of LGFS' internal board papers which stated that councils generally lacked understanding of, or the ability to analyse, CDOs and other structured products on the market: J[1004]-J[1005] and J[1036]. The evidence was not confined to LGFS' board papers. In particular, it extended to include:

1. Mr Michell’s tour of New South Wales in September 2005 to meet various local council representatives and his contemporaneous record of those meetings: see [104] above;

2. Mr Hilder’s September 2005 Activity Report to the LGFS Board in October 2005: see [106] above;

3. Mr Hilder’s 30 November 2005 email attaching board papers including an “Activity Report December 2005 Quarter”: see [117] above;

4. The fact that LGFS held a copy of the paper published by Mr Cordeiro of ABN Amro on 6 March 2006 (see [120] above) and that, on the same day, Mr Tischler had a meeting with ABN Amro (including Mr Cordeiro) for which Mr Tischler’s contemporaneous notes recorded that “[s]ome CDOs held by councils may not be suitable for inclusion because of excessive risk or unusual structural elements”: see [121] above and J[1011]-J[1012];

5. The fact that, on 5 April 2006, Mr Cordeiro emailed Mr Hilder regarding developing “Further Options for NSW Councils” and, among other things, stated that he was “conscious of the limited level of knowledge of complex financial products such as CDO’s and similar products” and that there was “no independent specialist reviewing the transactions making it difficult for the council to truly understand the level of risk associated with the investment”: see [122] above.

1172. None of this evidence was referred to by LGFS. None of this evidence supports LGFS’ contention that it was entitled to assume that previous dealings with CDOs had given the PA Councils sufficient appreciation of the issues involved to be aware of, and understand, the types of risks involved and to be able to ask about the risks which concerned them. Indeed, the evidence was to the contrary.

1173. LGFS’ placed considerable reliance on Mr Michell’s marketing report of November 2006 to the effect that the Rembrandt notes had received a positive response from “councils who have a good understanding of CDO & CPPI” (see [137] above) and the fact that the report included Oberon, Moree and Narromine who had previously invested in structured products: see [136] above. The report does not assist LGFS. The two page report also related to visits to six other councils who were not parties to these proceedings. No statements about Oberon, Moree or Narromine’s understanding of CDOs were made in that report. Mr Michell was not called to give evidence as to the PA Councils to which those comments in his report related.

3.2.2.2 Councils as institutions

1174. LGFS submitted that it was dealing with the PA Councils as institutions and was not privy to their internal deliberations concerning the Rembrandt notes. Therefore, according to LGFS, LGFS did not know what experience decision makers within the PA Councils had, with the implication that it could not reasonably have known that the PA Councils did not understand structured products. That submission does not assist LGFS. Aspects of this submission have already been addressed in Part 8, Section 2.2.5.1 under the heading “Challenge 1: Whether the witnesses were the decision makers and the availability of other potential advisers”: see [1037]-[1044] above. Moreover, the submission that LGFS did not know what experience decision makers within the PA Councils had, with the implication that it could not reasonably have known that the PA Councils did not understand structured products, was inconsistent with its submission that although Mr Hilder thought the Surf Presentation was too complicated, he was supposedly comforted by the fact that "as Mr Tischler knew, Mr [John] Murphy and Mr [Miles] Craighead [from Eurobodalla] had considerable experience of structured products".

3.2.2.3 Contents of documents provided by LGFS to PA Councils and their response

1175. LGFS then sought to garner support for its contention from the contents of documents provided by LGFS to the PA Councils. LGFS submitted that it provided these documents for the PA Councils to read, but did not know whether they had done so, or how thoroughly, and that, in the absence of a request for an explanation or assistance from the relevant PA Council (and LGFS never received any such request) it was difficult to see what else LGFS should have done. LGFS further submitted that the documents were capable of being understood by the relevant officers at each of the PA Councils, arguing that the LGFS Community Income Notes Brochure "was written in accessible terms" and that the S&P Reports were "not so arcane that [they] could not be read and understood".

1176. Those contentions proceed upon a false premise – that the documents were accurate. They were not. For example, as the primary judge found, reading the LGFS Community Income Notes Brochure, the S&P Reports and ABN Amro term sheet would not have assisted the PA Councils to identify the risks involved with the Rembrandt notes (J[1637]) as:

1. The LGFS Community Income Notes Brochure did not disclose the risks – "[i] t was a wholly one sided description of the potential benefits of investing in a product said to have been arranged by LGFS without any accompanying disclosure of the potential risks which LGFS itself knew about";

2. The S&P Reports did not disclose all of the risks of which LGFS was aware and did not purport to be a summary of the product suitable to be given to the PA Councils for the purpose of explaining the nature of and risks associated with the product; and

3. The ABN Amro term sheet did not identify the risks of the Rembrandt notes.

1177. The inaccuracies in the documents, together with LGFS' non-disclosures (see Part 8, Section 2.3 above), are a complete answer to LGFS' contention that it was entitled to rely upon the fact that it received little or no questioning from the PA Councils to justify its conclusion that the PA Councils understood the product. As the primary judge said (at J[1620] and [1639]), the PA Council witnesses "did not know what they did not know" and could never have asked the right questions to obtain the relevant information. The contention is rejected.

3.2.2.4 Eurobodalla

1178. LGFS sought to distinguish Eurobodalla on the grounds that, in addition to the Pre-Sale Report, Eurobodalla had previously been provided with the Surf Presentation. LGFS submitted that its marketing to Eurobodalla had to be evaluated in the context that Eurobodalla could reasonably be expected to have read the Surf

Presentation. LGFS' submission was that the primary judge therefore erred in finding (at J [2198]) that Eurobodalla was in the same position as the other PA Councils despite receiving the Surf Presentation. That submission is unfounded. It ignored evidence given by officers from Eurobodalla. Mr Craighead said he "tried to read it" but that there would have been terms in the document that he was unable to understand in detail and which he was not sure were totally traversed. Another officer, Mr Murphy, also gave evidence that he did not understand aspects of the Surf Presentation, including how the product used leverage.

1179. There are other flaws in LGFS' submission. The Surf Presentation was not "perfectly comprehensible". Indeed, LGFS' own witness Mr Hilder gave evidence that he did not understand aspects of the Surf Presentation, including that the price of the CPDO was not directly impacted by movements in correlation, and that the mechanics "were a bugger". LGFS' submissions also failed to address the fact that Eurobodalla had previously rejected the notion of investing in the CPDO when it was approached by ABN Amro: J [1481]. It had chosen to invest in the Rembrandt 2006-3 notes because they were recommended by a trusted adviser (LGFS) and Mr Tischler had told Eurobodalla that it was one of the best products he had seen across his desk in a long time: see J[1481] and [1044] above. This contention fails.

3.2.2.5 Oral Presentations to PA Councils

1180. LGFS submitted that there was very little contemporaneous documentary evidence before the primary judge as to what Mr Tischler and Mr Michell said in their oral presentations to the PA Councils concerning the Rembrandt notes. It must be recalled that Mr Michell did not give evidence and Mr Tischler did not remember the individual conversations but gave evidence of what he said his general practice had been. The primary judge expressed a preference for the evidence of council officers over Mr Tischler's evidence where they were in conflict.

1181. LGFS' position was that where the PA Council witnesses were uncontradicted or effectively uncontradicted because of the primary judge's general rejection of Mr Tischler's evidence of his general practice, it did not mean that the PA Council witnesses were necessarily reliable. LGFS submitted that many of the same factors which militated against accepting Mr Tischler's evidence were equally applicable to the PA Council witnesses and, indeed, in some cases, the primary judge rejected specific aspects of the PA Council witnesses' evidence despite the lack of contradiction.

1182. LGFS then submitted that:

> There are therefore limitations to her Honour's findings on what was said in the Council officers' conversations with LGFS and internally. Her Honour did [address] all of the issues which were raised as to what was specifically said. And even where she did so, and accepted the thrust of the Council witnesses' evidence, they were only claiming to remember the "substance" or "context" of what had been said and the precise wording which appeared in their affidavits and oral testimony remained subject to the factors which necessarily affected its reliability.

1183. LGFS does not identify any specific errors which the primary judge made in accepting the evidence of the PA Councils' witnesses. There was nothing inconsistent or erroneous in the approach of the primary judge. LGFS does not identify any error or point to what her Honour should have done differently.

1184. The submission that "there are limitations" to the primary judge's findings on what was said between the PA Councils and LGFS was not articulated with any, or any sufficient, particularity. For that reason alone, it is rejected. However, three points must be made:

1. Unlike many of the PA Council officers, Mr Tischler was found to have no specific recollection of his discussions with the PA Councils about the Rembrandt notes: J[1326];

2. Mr Michell was not called to give evidence; and

3. All of the PA Council officers impressed the primary judge as witnesses who were doing their best to accurately recall what they had been told: J[1325].

1185. The primary judge preferred the PA Council officers' evidence of the oral representations made by LGFS. There was no error in the primary judge's findings of fact as to those representations. There was and is no basis to overturn those findings: *Fox v Percy* at 125-127 ; *Rosenberg v Percival* (2001) 205 CLR 434 at 448 [41]-[42] and *Devries v Australian National Railways Commission* (1993) 177 CLR 472 at 482-483 .

3.2.2.6 Nature of product

1186. The primary judge found that it was misleading for LGFS not to disclose its opinion that Rembrandt 2006-3 was "grotesquely complicated" because the complicated nature of the product prevented the PA Councils from appreciating that it was different in material respects from products with which they had previously dealt: see, for example, [90] above. In particular, the primary judge said investors in CDOs would be misled into thinking that the product was like a CDO, and investors in floating rate notes (**FRNs**) would be misled into thinking it was like an FRN: J[2184]. LGFS submitted that the primary judge erred in finding that LGFS engaged in misleading and deceptive conduct by failing to disclose to the PA Councils that it considered the product to be "grotesquely, extremely, highly or extraordinarily complicated": J[2184]. In short, LGFS' principal complaint was that the fact that the complexity of the Rembrandt notes was obvious to the PA Councils.

1187. These complaints are rejected. It may be accepted as a general proposition that the PA Councils perceived the Rembrandt notes as a complex structured product. But that was just part of the equation. An, if not the key, aspect of the primary judge's finding was LGFS' failures to disclose its opinion as to the degree of complexity of the Rembrandt notes, not the fact that the notes were complicated.

1188. It was LGFS' failure to tell the PA Councils that it regarded the Rembrandt notes as grotesquely complicated which was misleading because it led the PA Councils to believe that whilst the notes were complex, their level of complexity was consistent with other structured products which they had been offered or invested in in the past, such as CDOs and FRNs. As noted earlier, the PA Councils "did not know what they did not know because LGFS had never taken any steps to ensure the contrary": J[1620], J[1639] and J[1177] above.

3.2.3 Specific representations

1189. LGFS then identified specific representations or non-disclosures which it submitted the primary judge erred in finding were misleading or deceptive. Those representations or non-disclosures were:

1. The role of LGFS;

2. The failure to disclose that the Rembrandt notes were highly volatile;

3. The meaning of "market value" for purpose of sale back to LGFS;

4. The modelling disclaimer;

5. The March 2007 rating review by S&P; and

6. The cash out and cash in features of the Rembrandt notes.

Each will be addressed in turn.

3.2.3.1 Role of LGFS

1190. The primary judge found that representations were made to nine of the PA Councils (Corowa, Orange, Oberon, Deniliquin, Moree, Murray, Cooma, Ryde and Narromine) to the effect that Rembrandt 2006-3 had been designed or tailored for local government. In particular, the primary judge found that the relevant representations were made orally to Corowa and Orange by Mr Tischler and to Oberon, Deniliquin, Moree, Murray and Cooma by Mr Michell.

1191. LGFS did not submit that these findings that representations were made to nine of the PA Councils to the effect that Rembrandt 2006-3 had been tailored or designed for local government were wrong. LGFS rather submits that LGFS' conduct as a whole must be assessed to determine whether the representations were misleading and that, in context, they were not misleading because the LGFS Community Income Notes Brochure stated the correct position and there was no finding that the PA Councils were misled by, or relied upon, that finding in making the decision to invest in Rembrandt 2006-3. These submissions are rejected.

1192. LGFS' conduct as a whole must be assessed to determine whether it was misleading (see [770] above) and that was the approach adopted by the primary judge. The problem for LGFS was that the matters of context it identified did not assist it. First, the LGFS Community Income Notes Brochure. Its content, with its emphasis on LGFS' role, confirmed the oral representations that the Rembrandt notes had been tailored for local government: see [125] above, in particular the emphasis on the fact that the notes were "[a]rranged by [LGFS]", diversification and liquidity. Indeed, that was the finding of the primary judge at J[1671] in relation to Moree.

1193. Next, contrary to LGFS submission, the PA Councils' did rely on the representation that the Rembrandt notes were specifically designed for local government. There were findings that the PA Councils were misled by, or relied upon, that finding in making the decision to invest in Rembrandt 2006-3. The primary judge found:

1. In relation to Moree, that that representation "was calculated to induce trust in the product and reliance on LGFS' involvement and had that effect. Mr Johnson

[of Moree] did not need to say he relied on that statement in isolation or over and above the other statements Mr Michell made to establish reliance on it": J[1671]; and

2. In relation to the other PA Councils, who were relevantly in the same position as Moree, that this representation would be a "powerful inducement for councils to believe the product was particularly well suited to their investment requirements having regard to the Ministerial Order, the [I]nvestment [G]uidelines and the prudent person standard to which councils were subject and the fact that councils deal with public money ultimately required for public purposes": J [1712].

1194. Third, and no less importantly, the remaining context in which these representations were made cannot be ignored. The context has been outlined earlier: see [1027]-[1030] above. In particular, the context included the fact that LGFS had "white badged" or rebranded the product as "Community Income Notes" "arranged by LGFS" in order to (as LGFS put it) give the product a local government "feel": see [74] above. As the primary judge found, that assisted LGFS in "leveraging off its rapport with councils": see [74] above and J[1278].

1195. Finally, the primary judge made specific findings in relation to some of the PA Councils. For example, in relation to Narromine, the primary judge found that if Ms Redden had known that LGFS had not tailored the Rembrandt notes to local government she would not have trusted LGFS and would not have invested: J[2058]. In relation to Ryde, the primary judge accepted that if Mr Newsome had known that statements in the CPDO letter (see [131] above) from LGFS, including the statement that the Rembrandt notes were tailored to local government, were false, it would have affected his perception of LGFS and he would have reconsidered investing Ryde's funds with LGFS: J[2105]. That finding must be understood in the broader context of the unchallenged findings made by the primary judge about Ryde: see [1043] above.

1196. For those reasons, LGFS' submission fails. LGFS' representation that the Rembrandt notes were tailored/designed for local government, was a material inducement to each of the PA Councils to invest in the notes.

3.2.3.2 The highly volatile nature of the Rembrandt notes

1197. The primary judge found that LGFS made representations to ten of the PA Councils (all except Orange, Narrandera and Narromine) as to the quality of the Rembrandt notes which were misleading because they did not include an explanation that the NAV might be volatile, and in particular of the effect of the widening of credit spreads. LGFS submitted that the primary judge erred in finding that LGFS engaged in misleading and deceptive conduct in failing to disclose that the Rembrandt notes were highly volatile because: (a) at least seven of the PA Councils were aware that the NAV was linked to the performance of the underlying indices and therefore it could (and would) go up and down and, in any event, this was an inherent feature of any structured product and was implicit in the diagrams in the LGFS Community Income Brochure and in the Pre-Sale Report and (b) the evidence did not support the conclusion that LGFS knew or had reason to believe this was anything more than "an unquantified (but unlikely) possibility".

1198. These contentions are misplaced. First, LGFS challenged the primary judge's finding (at J [2158]) that LGFS knew that the value of the Rembrandt notes might be "highly volatile" and that it might perform within anticipated parameters yet nevertheless lose up to 30% of its value: see also Part 8, Section 2.2.5.7 under the heading "Challenge 7: Price volatility" at [1060] above. That challenge is rejected. The challenge was inconsistent with, and impermissibly ignored the evidence from, Mr Hilder for LGFS. During cross examination, Mr Hilder accepted that:

1. The strategy values in NAV graphs provided to LGFS by ABN Amro on 9 October 2005 showed it was possible for significant losses of market value to occur in the early years of those structures;

2. The 22% loss of value which the Rembrandt notes experienced in 2007 was consistent with the scenarios provided by ABN Amro and that there was a possibility of this occurring; and

3. The possibility that the Rembrandt notes could suffer a 28-30% loss in value based on the ABN Amro scenarios was highly material to LGFS' assessment of whether it was willing to buy the product and that he was "happy to take that risk on LGFS' behalf".

1199. Whether or not Mr Hilder perceived the high volatility of the Rembrandt notes as a "problem", he acknowledged that he understood that it was a "risk" which was highly material to LGFS' assessment of whether it should invest in the notes. Mr Hilder also accepted that he expected that Mr Tischler and Mr Michell would discuss the risk with the PA Councils. Despite that knowledge and understanding, LGFS did not mention that the product might be highly volatile to a single PA Council: J[2158]. Instead, LGFS placed its only warning regarding volatility in the fine print on the LGFS Community Income Notes Brochure in the middle of a long paragraph consisting mainly of boilerplate text: see [125] above and J[2158]. That was wrong.

1200. There are other reasons for rejecting LGFS' submission. First, LGFS' submission that it should have been inferred that the PA Councils were on notice of this fact based on the Surf Presentation (see [62] above) and/or what LGFS described as the "implicit" representations in the descriptions of the product in the diagrams in the LGFS Community Income Notes Brochure (see [125]-[127] above) is not supported by the identified documents. For example, the fact that the Surf Presentation disclosed that the performance of the Rembrandt notes was linked to the evolution of credit spreads (see [62] above) is different to the proposition that the Rembrandt notes were highly volatile. Second, LGFS cross-examined the PA Councils' witnesses about "market value". The primary judge found (at J[2158]) that that cross-examination did not in substance "go beyond the truism that market value might go up or might go down" and the fact that the council officers knew that could not be equated with knowledge that the Rembrandt notes were highly volatile. None of the other documents relied upon by LGFS support LGFS' submission. So, for example, the Grove Report (see [135] above) stated:

> **Credit spreads widening**, with large discontinuities, could reduce NAV substantially, and place coupons at risk. In particular, unlike conventional CDOs, CPDOs directly participate in market value risks.

(Emphasis in original.)

1201. LGFS also submitted that the launch of Rembrandt 2006-3 took place during a long period of benign credit market conditions and that therefore credit spreads could be expected to widen again "sooner or later". That statement does not accurately state the evidence. The primary judge accepted that credit spreads "were expected by *knowledgeable investors* to rise at some time in the not so distant future" (emphasis added): J[1353]. The problem for LGFS was twofold. First, the finding that the PA Councils were not knowledgeable investors: J [1354]. Second, the fact that the PA Councils did not ask questions in relation to the volatility of the NAV does not indicate that it was reasonable for LGFS not to disclose that it was highly volatile. As has been said earlier, it was apparent from the PA Councils' witnesses' evidence that "they did not know what they did not know" and in those circumstances could not have asked the right questions: J[1620], J[1639] and [1177] above.

1202. LGFS knew that it was a real possibility (reflected in the scenarios provided to LGFS by ABN Amro (and accepted by Mr Hilder)) that the Rembrandt notes may lose up to 30% of their value, which was highly material to LGFS' decision to invest and was a material fact which it was incumbent on LGFS to disclose to the PA Councils. It did not do so.

3.2.3.3 The meaning of "market value" for purpose of sale back to LGFS

1203. The primary judge found that LGFS' explanation of its promise to buy back the Rembrandt notes from the PA Councils at "market value" was misleading and inaccurate and LGFS thereby engaged in misleading and deceptive conduct. On appeal, LGFS challenged that finding on the grounds that the primary judge's conclusion was "contestable" (at least so far as it implied that the variation of the value of the notes from NAV could be substantial). That challenge is rejected.

1204. LGFS promised the PA Councils that it would provide liquidity by repurchasing the Rembrandt notes at market value. The market value of the Rembrandt notes was to be determined by ABN Amro having regard to the supply of and demand for the notes: see [84] and [130] above. Accordingly, the market value of the Rembrandt notes could be substantially below the par or NAV of the notes: J[1363]. That fact was disclosed in the Surf Presentation, which stated that "[t]he traded price may be different from the NAV of the notes due to supply and demand issues". The primary judge found that Mr Hilder understood this: J [1357]. The problem for LGFS is that it did *not* inform the PA Councils that the market value at which LGFS promised to repurchase the Rembrandt notes from them could be substantially below the par or NAV of the notes (as it would be whatever price ABN Amro determined having regard to supply and demand at the time): J[1363].

1205. The relevant question was not the construction of the promise between ABN Amro and LGFS. The relevant question was whether LGFS' conduct was misleading and deceptive in failing to disclose to the PA Councils that the "market value" of the Rembrandt notes for the purpose of its buy-back promise was not the face value of the notes. The PA Councils entered into the investment in reliance on LGFS' promise to buy-back the notes: see, for example, J [2147(16)] and J[1552] (Parkes); J[1641] (Orange); J[1914] (Narrandera); J[1954] (Murray) and J[2089] (Ryde). Mr Hilder believed that the 24-hour liquidity promise "would be a great comfort for [the PA] Councils" and that the liquidity of the Rembrandt notes "was an essential feature for [c]ouncils because they could direct LGFS to deconstruct the [n]otes with 24 hours' notice at any stage throughout the life of the product": see also [130] above. Likewise, Mr Tischler believed that the liquidity feature would be attractive to the PA Councils and that liquidity was "very important to the [PA Councils'] cash flow and their potential desire for access to funds". Mr Tischler understood that because liquidity was important for the PA Councils, it was very important for them to get back all, or nearly all, of the funds they had invested if they wanted to redeem the Rembrandt notes. Mr Tischler agreed during cross-examination that he never told councils that the market value of the notes may not be their face value or that if they chose to sell the notes before maturity, it could be substantially below par. He also agreed that it was one of the major sources of risk, that it was not disclosed by the S&P Reports and that he "never gave the council representatives the benefit of [his] knowledge about that as a major risk".

1206. In those circumstances, it was misleading and deceptive for LGFS to fail to tell the PA Councils that LGFS' promise to buy back the Rembrandt notes at market value might be at a price below (or substantially below) par.

3.2.4. The modelling disclaimer

1207. The Surf Presentation contained a disclaimer concerning the modelling which supported the rating: see [853] above. The disclaimer, in the "Key Risk Factors" section of the presentation, stated that "Current modelling assumptions are unlikely to be consistent with the actual performance of CPDO": see [62] above. The primary judge found that this disclaimer should have told LGFS that "notwithstanding the rating of AAA, there was an element of risk in the performance of the product because the rating of it involved modelling based on assumptions which were unlikely to reflect actual conditions as they evolved in the future": J [2200]. As the primary judge said, this indicated "the existence of risk which the rating could never eliminate given the way in which the rating was derived": J[2200].

1208. Accordingly, the primary judge found that it was misleading and deceptive of LGFS not to communicate the rating to the PA Councils without also communicating that there was an element of risk in the performance of the product not accounted for by the rating – the rating involved modelling based on assumptions unlikely to reflect actual conditions in the future: J [2200].

1209. LGFS challenged this finding on the grounds that the primary judge overstated the significance of the disclaimer. That challenge is misplaced. The primary judge's finding was not that the disclaimer meant the rating was unreliable. The primary judge's finding was not inconsistent with her Honour's other findings at J[3100]. Instead, the primary judge found that the disclaimer was a factor which was not accounted for by the rating and that therefore it was misleading and deceptive for LGFS to pass on the rating without also disclosing the existence of a risk which the rating could not and did not eliminate given the manner in which the rating was derived: see Part 3, Section 1 above.

1210. LGFS again placed considerable emphasis on the fact that Eurobodalla had the Surf Presentation. LGFS submitted that Eurobodalla could not sensibly claim that LGFS should have made the further disclosure described in the previous paragraph when LGFS knew that Eurobodalla already had the presentation. That contention fails for the reasons set out at [1178] above.

1211. In this context, LGFS again resorted to the contention that the PA Councils did not ask about the rating, including the modelling assumptions, and that therefore LGFS could reasonably assume that the PA Councils understood that S&P's modelling was based only on past events. That contention is untenable for a number of reasons. LGFS represented to the PA Councils that the product was a suitable investment (and had been tailored) for local government: J [2148]. LGFS failed to disclose that the product was grotesquely complicated: J[2268]. The PA Councils did not have the resources or expertise to second-guess the rating of a structured financial product: J[2816]. The PA Councils "did not know what they did not know" and could never have asked the right questions to obtain the relevant information: J[1620], [1369] and see [1177] above. In those circumstances, LGFS could not reasonably assume that the PA Councils would independently come to the conclusion that the product carried with it an additional risk not accounted for by the rating and not disclosed by LGFS.

3.2.5 The March 2007 rating review by S&P

1212. The primary judge found that LGFS engaged in misleading and deceptive conduct by failing to disclose that, in March 2007, S&P was reviewing its ratings approach for CPDOs. LGFS appealed against that finding on the basis that as S&P's review of its ratings approach did not apply to the Rembrandt notes, LGFS was under no duty to disclose the fact of that review to the PA Councils. Its challenge is rejected.

1213. First, the background. S&P started reconsidering its rating approach in November 2006. At that time, S&P went to considerable trouble (at ABN Amro's behest) to avoid making any public comment which would question the rating of the products already issued. When a rumour of the reconsideration surfaced (and was referred to in the Grove Report (see [135] above), LGFS raised the issue with ABN Amro and was told that the new ratings matrix had no impact on the rating for the Rembrandt notes: J[1191(6)] and J[1368]-J[1369]. The primary judge made no adverse finding against LGFS. The primary judge accepted that LGFS could legitimately rely upon what it had been told by ABN Amro.

1214. S&P then adopted a revised rating matrix in the form of the CPDO Evaluator in March 2007: see [364] and [366] above. LGFS (through Mr Hilder) was aware that S&P had announced that it was revising the way it rated products such as the CPDO, and was aware that it had potential ramifications for how the Rembrandt notes would be perceived: see [142] above and J[1369]. Indeed, LGFS' February 2007 Status Report annexed to its 21 March 2007 board papers recorded that:

> More recently Standard Poor's (sic) announced that it was revising the way in which it rates such products. Whilst this does not impact our product directly there may be some ramifications in how the product is perceived. As a consequence ABN [Amro] declined our request to issue more of the notes ... The primary strategy will remain to sell the notes directly to councils.

Mr Hilder agreed that those facts were never disclosed to any of the PA Councils.

1215. Mr Tischler's position was different. He first heard about the new CPDO Evaluator from Grove Research and Advisory by email on 10 November 2006. That email was to the effect that, if issued now, the Rembrandt notes would be rated A+ and not AAA: J[1368]. Mr Tischler agreed that no council would have bought the Rembrandt notes if they had been told of those facts. And the PA Councils were not told. Yet despite this knowledge, the February 2007 Status Report stated that the primary strategy would remain to sell the Rembrandt notes directly to councils: see [1214] above. LGFS was aware that the perception of the Rembrandt notes would be affected by these facts and the inclusion of these facts in its February 2007 Status Report, indicates that LGFS knew that they would be material to potential investors in the notes.

1216. The primary judge was correct to find that LGFS engaged in misleading and deceptive conduct by failing to disclose to the PA Councils in March 2007 that S&P was reviewing its ratings approach for CPDOs with the effect that, if issued now, the Rembrandt notes would be rated A+ and not AAA. The fact that new CPDO Evaluator was expressed not to apply to the Rembrandt notes was not determinative.

3.2.6 The cash out and cash in features of the Rembrandt notes

1217. LGFS was found to make cash out representations to three PA Councils and cash in representations to five PA Councils: J[2147(12), (13) and (15)]. The representations were that:

1. Rembrandt 2006-3 was designed/built to cash in and become a risk free investment in six or seven years (made to Eurobodalla, Orange and Moree): J [2147(12)];

2. Rembrandt 2006-3 was likely to cash in in six or seven years and then become risk free (made to Eurobodalla, Parkes and Narrandera): J[2147(13)]; and

3. the likelihood of cash out was very remote/very low/very unlikely (made to Eurobodalla, Moree and Narrandera): J[2147(15)].

1218. The primary judge found that these representations were unjustified. The primary judge stated (at J[2175]):

> To the extent that LGFS made representations about the likelihood of the product cashing in and the unlikelihood of it cashing out, I am satisfied that LGFS unwittingly and innocently engaged in misleading and deceptive conduct. *LGFS had been given information by both ABN Amro and S&P which provided LGFS with reasonable grounds to believe that the product was unlikely or very or extremely unlikely to cash out*, but (as discussed) that information was itself misleading and deceptive and *LGFS did not merely pass the information on for what it was worth. LGFS adopted and adapted the information for its own marketing purposes*. Even if, as S&P would have it, the meaning of the AAA rating on interest and principal is limited to an extremely strong capacity for the instrument to meet its financial obligations LGFS believed, based on the AAA rating, that the instrument was unlikely or very or extremely unlikely to cash out (which would require a loss of value of 90%). From the information provided by ABN Amro LGFS also believed that the product was designed to cash in and was likely to cash in in six or seven years. Hence, LGFS's conduct was innocent but nevertheless misleading and deceptive.
>
> … As LGFS knew, S&P's rating did not address the volatility of the product, only its capacity to meet its financial obligations (that is, whether or not the product would pay

interest and principal as promised or would cash out). As LGFS also knew, the information it was provided by ABN Amro dealt with not only the likelihood of cash-in and its timing but also the high volatility the product might experience before cashing in (or cashing out). In these circumstances while LGFS had a reasonable basis to believe that the AAA rating and the information provided by ABN Amro supported its representations about the likelihood and timing of cash-in and the likelihood of cash-out of the investment, this basis did not exist in respect of any representation LGFS made (as it did – see above) as to the safety, security, soundness or risks of the product as a whole which included its potentially high volatility.

(Emphasis added.)

1219. **Following paragraph cited by:**

Luo v Windy Hills Australian Game Meats Pty Ltd (No 3) (10 July 2019) (Stevenson J)

LGFS had two complaints. First, that the primary judge impermissibly treated these representations as a statement of fact, rather than a statement of opinion and, second, that the primary judge failed to find that LGFS had reasonable grounds for that opinion. Those contentions are misplaced. The primary judge treated the representations as statements of opinion which carried with them a representation that the opinion was based on reasonable grounds: see the italicised section extracted above. The difficulty for LGFS was that the primary judge found that LGFS had no reasonable grounds for that opinion. The primary judge's reasons for reaching that view are set out in the second paragraph above. LGFS' subjective view was and remains irrelevant. That was the reason why the primary judge stated that LGFS "unwittingly and innocently engaged in misleading and deceptive conduct".

1220. LGFS again sought to distinguish the position of Eurobodalla by reason of the fact that it had received the Surf Presentation and that presentation expressly referred to the rating and ascribed a probability of default based on the rating of 0.728% and early cash in. That contention fails for the reasons set out at [1178] above. Moreover, in response to a query from Mr Craighead about the security of Eurobodalla's capital, Mr Tischler explained to Mr Craighead that it was unlikely Eurobodalla would lose capital because of Rembrandt's "cash in" and "self-cleansing" features and that for a "cash out" to occur a significant number of defaults of major international companies would have to occur within a six-month period: J [1481] and [1044] above. There was no basis for suggesting that Eurobodalla would have assumed such a statement to be LGFS merely passing on information from ABN Amro.

1221. Finally, in this context it is important to recall that LGFS did not challenge the findings that LGFS engaged in misleading or deceptive conduct by not disclosing to the PA Councils that the performance of the Rembrandt notes depended on spread evolution, and in not disclosing that in the period prior to marketing the Rembrandt notes, there had been negative movements in the credit spreads on the CDX and iTraxx indices which were likely to have an adverse effect on the future performance of the notes.

3.3 Section 1041E of the *Corporations Act*

1222. LGFS did not challenge the finding that it made representations that the Rembrandt notes were tailored or designed for local government and that these representations were false for the purposes of s 1041E of the *Corporations Act* : J[2237]-J[2238]. However, LGFS submitted that those misrepresentations were not causative of the PA Councils' losses. That issue is addressed in Section 5 below.

3.4 Section 12DA of the *ASIC Act*

1223. It was common ground that no additional issues arise in relation to s 12DA of the *ASIC Act* an d that LGFS' liability under that section falls to be determined with its liability under s 1041H of the *Corporations Act* .

4. CONTRACT CLAIMS IN RELATION TO COOMA AND COROWA

1224. LGFS accepted that these Appeal Grounds (LGFS Appeal Grounds Matrix Rows 109 and 115-117) should stand or fall with its Appeal Grounds in relation to the tort claims and the statutory claims. Accordingly, these Appeal Grounds are rejected.

5. CAUSATION

1225. LGFS challenged the primary judge's finding at J[2275] that LGFS' negligence and misleading conduct was causative of the PA Councils' losses. The applicable principles have been addressed earlier: see [775]-[781] above. Causation requires a two-step analysis: (a) whether the PA Councils would have proceeded with the purchase of the Rembrandt 2006-3 notes "but for" the non-disclosures and misrepresentations of LGFS (**the 'But For' Test**) and (b) whether it was appropriate that LGFS be held liable for the actual losses suffered under s 5D(1)(a) of the *Civil Liability Act* (**the Scope of Liability Test**).

5.1 The 'But For' Test – the first step

1226. The first step in the inquiry – whether each loss was *in fact* caused by LGFS' negligent or misleading conduct – was a step considered by the primary judge. Her Honour found that but for LGFS' breaches of its duty of care, none of the PA Councils would have invested in the Rembrandt 2006-3 notes and that LGFS' negligence was a necessary condition of the harm the PA Councils suffered when the notes cashed out in October 2008: J[2275].

1227. LGFS sought to challenge these findings by reference to the following headings:

1. Role of LGFS;
2. NAV volatility and evolution of credit spreads;
3. Calculation of market value;
4. Modelling disclaimer;
5. March 2007 S&P CPDO Evaluator;
6. Unlikelihood of cash out; and

7. Prospects of cash in.

Each will be addressed.

5.1.1 Role of LGFS

1228. LGFS submitted that the PA Councils would still have invested in the Rembrandt notes had it not represented that the notes were tailored for local government because what “was important for them was [LGFS’] involvement through ‘white badging’ the product”. That is rejected. As explained at [1190]- [1196] above, in relation to Moree, the primary judge found that the representation “was calculated to induce trust in the product and reliance on LGFS’ involvement and had that effect”. The primary judge was correct to hold that Mr Johnson of Moree did not need to say he relied on that statement in isolation or over and above the other statements Mr Michell made to establish reliance on this representation: J[1671].

1229. The primary judge found that the other PA Councils were in relevantly the same position as Moree. As the primary judge said, the representation would be a “powerful inducement for councils to believe the product was particularly well suited to their investment requirements having regard to the Ministerial [O]rder, the [I]nvestment [G]uidelines and the prudent person standard to which councils were subject and the fact that councils deal with public money ultimately required for public purposes”: J[1370].

1230. LGFS sought to distinguish Narromine’s position. LGFS submitted that Narromine did not rely on the representation that the Rembrandt notes were tailored to local government. That submission is rejected. It was not supported by any evidence and was inconsistent with the primary judge’s finding at J[2058] that if Ms Redden of Narromine “had known that LGFS had not in fact tailored the CPDO to local government as represented in the CPDO letter she would not have trusted LGFS and would not have invested”: see [1195] above.

5.1.2 NAV volatility and evolution of credit spreads

1231. LGFS presented this argument in two parts. First it dealt with Eurobodalla and then it addressed the position of the PA Councils’ generally.

1232. In relation to Eurobodalla, LGFS submitted that Eurobodalla was on notice that the NAV could fluctuate and that the Rembrandt notes’ performance was based on the evolution of credit spreads and that, despite being on notice of these matters, Eurobodalla was not dissuaded from investing in the notes. That submission is incorrect. Mr Murphy of Eurobodalla gave evidence that he appreciated that the value of the notes could go up and down but that he was not aware that money invested in the notes would then be used to invest in credit indices. That evidence does not support the contention that Eurobodalla was aware of NAV volatility and the evolution of credit spreads and that this did not affect its decision to invest. Indeed, the primary judge found that the PA Councils’ knowledge that the value of the Rembrandt notes could go up and down did not amount to knowledge that the notes were highly volatile: see [1200] above. As we have explained at [1199] above, this was a factor which was highly material to LGFS’ decision to invest, which LGFS knew was important to councils and which Mr Hilder expected would be discussed with the councils but it was not: J [1314].

1233. Further, if the PA Councils had been told that the Rembrandt notes were highly volatile, and that there was a real possibility they could lose up to 30% of their value, the PA Councils would not have invested in the Rembrandt notes: see [1198]-[1202] above. The Grove Report does not support LGFS' contention that high NAV volatility would not have been an important factor which would have deterred the PA Councils from investing: see [1148] above. The further contention that the PA Councils "would have seen themselves as meeting Grove's criteria" is unsubstantiated by any evidence.

1234. Finally, LGFS submitted that the PA Councils saw the Rembrandt notes as buy and hold investments. That submission goes nowhere. It does not indicate that the PA Councils would have proceeded to purchase the Rembrandt notes if told that the notes were highly volatile such that they could lose up to 30% of their market value. Liquidity was an important concern for all of the PA Councils and LGFS knew that the funds being invested would be required for public purposes and that the cash flow requirements of a council may change over a term as long as 10 years: see [130] above. The primary judge was correct to conclude that the PA Councils would not have invested in the Rembrandt notes had they been informed of the volatility risk.

5.1.3 Calculation of market value

1235. In relation to LGFS' failure to disclose that market value could be significantly below par, LGFS submitted that the calculation of market value only arose if the PA Councils were forced sellers. This contention is rejected for the reasons at [1203]- [1206] above. The PA Councils invested in the Rembrandt notes relying on LGFS' promise to buy back the notes. LGFS knew that the liquidity of the Rembrandt notes "was an essential feature for [c]ouncils because they could direct LGFS to deconstruct the [n]otes with 24 hours' notice at any stage throughout the life of the product".

5.1.4 Modelling disclaimer

1236. The modelling disclaimer was not adequately disclosed and there was no basis for suggesting that Eurobodalla, or any other PA Council, would have proceeded to invest notwithstanding that issue: see [1209]-[1210] above.

5.1.5 March 2007 S&P CPDO Evaluator

1237. LGFS submitted that while the primary judge made a finding that the perception of an effect on the Rembrandt notes from the issuing of the CPDO Evaluator in March 2007 would have dissuaded Ryde from investing (J[2114]) and probably Narrandera (J[1908]), no such finding was made for Cooma or Narromine. The implication of LGFS' submission was that absent a positive finding that the issuing of the CPDO Evaluator would have dissuaded a council from purchasing the notes, causation could not be established. The submission fails: see [1212] -[1216] above. It must be recalled that Mr Tischler agreed that *no* council would have bought the Rembrandt notes if they had been told those facts: see [1215] above.

5.1.6 Likelihood of cash out

1238. LGFS submitted that its failure to disclose that market value could be significantly below par on cash out only arose if the PA Councils were forced sellers. That submission is rejected for the reasons at [1217]ff above. The PA Councils invested in the Rembrandt notes in reliance on LGFS' promise to buy back the notes. LGFS knew that the liquidity of the Rembrandt notes "was an essential feature for [c]ouncils because they could direct LGFS to deconstruct the [n]otes with 24 hours' notice at any stage throughout the life of the product".

5.1.7 Prospects of cash in

1239. LGFS submitted that the time to cash in was not of itself important to the PA Councils because none of the PA Councils made any plans to schedule capital expenditure in reliance on these statements. That statement is incorrect. The evidence before the primary judge established that a number of the PA Councils relied on this promise, including, for example, Eurobodalla; Orange; Moree (see J[1683]), Parkes and Narrandera.

5.2 The Scope of Liability – the second step

1240. LGFS submitted that the direct and immediate cause of the PA Councils' losses was the cash out of the Rembrandt notes. That submission is rejected.

1241. First, LGFS ignores the primary judge's finding that "LGFS' misrepresentations had a direct and immediate connection with the loss the PA Councils suffered": J[3521]. LGFS did not identify any error in that finding or that it was appropriate that LGFS be liable for the loss suffered.

1242. Second, LGFS misunderstands the second step. It is not necessary that each and every risk which LGFS failed to warn of came to pass in order for the scope of LGFS' liability to extend to the PA Councils' losses. The relevant question is whether the loss flowed directly from the inducement to enter into the investment: *Kenny & Good* at 330. Put another way, a defendant will be liable for loss that is "the reasonable consequence of the inducement", not for losses which have extraneous causes: *NMFM Property* at 373-374 [463]-[464] . Here, the loss on the Rembrandt notes, being sustained spread widening causing cash out of the notes, was a reasonable consequence of LGFS' inducement to the PA Councils to purchase the notes. That was the "central risk" of an investment in the Rembrandt notes: J[3454]. Accordingly, LGFS' submission that LGFS' conduct was not the real and practical cause of the loss because it only put the PA Councils in the position that certain risks (e.g., cash out risk) "might come to pass" must be rejected. It asks the wrong question.

5.3 Contributory negligence of the Councils?

1243. This is addressed in Part 13 below.

6. LOSS AND DAMAGE

1244. LGFS had one Appeal Ground in relation to loss and damage. LGFS' reliance on that Appeal Ground was contingent on this Court finding that the PA Councils did not suffer loss and damage in circumstances where: (a) the PA Councils continued to hold the Rembrandt notes after late February 2007; or (b) have not proved the alternative investments they would have made had they not purchased the notes: LGFS Appeal Grounds Matrix Row 120. We have not made those findings: see [1311]-[1312] and [1383]-[1385] below.

7. SECTION 1041E CLAIMS APPORTIONABLE?

1245. The primary judge concluded that the various claims pursuant to s 1041E of the *Corporations Act* were not apportionable but that they were apportionable under s 1041L of the *Corporations Act* because they arose out of the same facts as the claim under s 1041H . For the reasons set out at Part 13, Section 3 below, the primary judge was in error. The primary judge should have found that LGFS was liable to the PA Councils for the whole of the loss and damage caused by LGFS' misleading or deceptive conduct in contravention of s 1041E of the *Corporations Act* .

8. UNLICENSED TO DEAL CLAIM

1246. LGFS filed a Notice of Contention that the primary judge should have held each of the notes a debenture and that it was therefore authorised pursuant to the AFSLs to advise in relation to and deal with the notes: LGFS Appeal Grounds Matrix Row 123. That submission was considered in Part 4 , Section 1.1.4.4 above and is rejected for those reasons.

9. RESCISSION CLAIM BY COUNCILS

1247. These Appeal Grounds were abandoned by the PA Councils: PA Councils Appeal Grounds Matrix Rows 129-131. It remained an Appeal Ground for Bathurst and will be addressed in Part 11, Section 4 below.

PART 9: PA COUNCILS' PURCHASE OF 2006-3 NOTES: S&P

1. INTRODUCTION

1248. The PA Councils' claims against S&P were in tort and for misleading or deceptive conduct. The primary judge held that S&P's rating of AAA of the Rembrandt notes was misleading and deceptive and involved the publication of information or statements false in material particulars and otherwise involved negligent misrepresentations to the class of potential investors in Australia, which included LGFS and the PA Councils, because the S&P Representations (see [723] above) were not true and S&P also knew them not to be true at the time they were made.

1249. The findings made against S&P in relation to the PA Councils were inextricably linked with the findings made against it in relation to LGFS. To a large extent, the findings have been addressed in Part 4 above.

2. TORT CLAIMS

2.1 Negligence

1250. The duty owed by S&P to the PA Councils was a duty to exercise reasonable care in forming, and to have reasonable grounds for, the opinion expressed by the rating: see, by way of example, J[2453], J[2455] and J[2457]. This was the same duty S&P owed LGFS: see [566] above.

1251. S&P appealed against that finding. As with the claim made by LGFS (see [567] above), S&P contended (at trial and again on appeal) that it owed no duty of care to the PA Councils because:

1. It was not reasonably foreseeable that S&P's conduct would cause loss and damage to the PA Councils and the risk of harm was insignificant: S&P Appeal Grounds Matrix Rows 1 and 13;

2. The salient features of a duty of care were not present, or not sufficiently present: S&P Appeal Grounds Matrix Rows 2-6;

3. The special prerequisites for the imposition of a duty of care for negligent misstatement were not satisfied: S&P Appeal Grounds Matrix Rows 7-9; and

4. It would be incongruous for a duty to exist when the PA Councils were in breach of s 625 of the *Local Government Act* and the Ministerial Order in purchasing the Rembrandt notes: S&P Appeal Grounds Matrix Rows 11 and 12.

1252. This section of the judgment will consider the relevant findings of fact, the applicable legal principles and then turn to consider S&P's Appeal Grounds in relation to the PA Councils' claims against S&P. A careful reader will notice that these Appeal Grounds substantially repeat S&P's Appeal Grounds in relation to LGFS' claim.

2.2 Facts

1253. The relevant facts have been addressed at [569]- [572] above.

2.3 Applicable legal principles

1254. The applicable legal principles have been addressed at [573]- [578] above.

2.4 Application of principles to facts

1255. The analysis at [579]-[582] was, and remains, equally applicable to the PA Councils' claim against S&P. One S&P Appeal Ground (S&P Appeal Grounds Matrix Row 7, referring to Appeal Ground 2(f)) was that the requirements for establishing negligent misstatement set out in *Tepko* were not satisfied. That Appeal Ground is dismissed for the reasons set out at [569] -[582] above.

2.5 S&P's Appeal Grounds

1256. Against that background, it is necessary to turn to consider S&P's other Appeal Grounds. Each of the matters listed in [1251] above will be addressed.

2.5.1 No reasonable foreseeability / risk of harm insignificant?

1257. S&P contended at trial and on appeal that the risk of harm was not reasonably foreseeable and / or was insignificant with the consequence that S&P owed no duty of care to the PA Councils: see [1251] above. These grounds of appeal are rejected.

1258. A number of matters were relied upon by S&P. First, S&P's liability was indeterminate and, in particular, S&P did not know the identity of LGFS as a purchaser of the notes and did not know (and could not have known) of the identity of the PA Councils as secondary purchasers: S&P Appeal Grounds Matrix Rows 1-3. Next, the PA Councils were not vulnerable and, even if they were, S&P was not aware of their vulnerability: S&P Appeal

Grounds Matrix Rows 1 and 4-6. Third, S&P did not control the PA Councils or have any direct dealings with them: S&P Appeal Grounds Matrix Rows 1 and 8-10. Fourth, LGFS acted in contravention of the *Corporations Act* in purchasing and on-selling the notes to the PA Councils, and, finally, the PA Councils were in breach of s 625 of the *Local Government Act* and the Ministerial Order in purchasing the Rembrandt notes: S&P Appeal Grounds Matrix Rows 11 and 12. Each will be considered.

2.5.2 S&P's liability indeterminate and S&P did not know identity of the PA Councils

1259. When S&P published its ratings of the Rembrandt notes, S&P did not know the identity of LGFS as a purchaser of the notes or the identity of the PA Councils. S&P submitted that those facts meant that the primary judge made an error in finding that S&P owed the PA Councils the duty earlier described. The first limb of the argument (that S&P did not know the identity of LGFS as a purchaser of the notes) has been addressed and rejected at [587] -[595].

1260. Further, the fact that S&P did not know the identity of the PA Councils falls to be determined by reference to the same legal principles as LGFS and is rejected for the same reasons as LGFS: see [587]-[595] above. The class was not indeterminate. It was both known and identified. It was possible to identify the class to whom the duty was owed as investors in the Rembrandt notes. That was and remains sufficient. Liability was not indeterminate because S&P did not know the precise identity of the members of the class, the exact number of members in the class or the exact loss. S&P knew what it needed to know. It knew the characteristics of the class. S&P knew that a characteristic of the class (some might say a critical characteristic of the class) was that each was an investor in the Rembrandt notes and S&P also knew the foreseeable type of loss. It is the nature of the loss, not the precise amount which is relevant: *Perre v Apand* at 221-222 [107]-[108] . Here, the nature of the foreseeable loss was not in doubt. As we have said, S&P knew that if S&P's opinion as to the creditworthiness of the Rembrandt notes was careless, *investors* were likely to lose the money they had invested in the notes. And, in that context, S&P knew the size of the notes issued ([580] above), the level of minimum subscription ([580] above), that investors would rely on S&P's ratings ([57] and [580] above) and the 10 year period to the maturity of the notes (see [50] above): see also J[290] and J[2950]. As with LGFS, the class and the foreseeable loss were determined by the function S&P undertook. That function was delineated by the purpose of the rating (the first limb of *Tepko* addressed at [574] above) and the known reasonable reliance (the second limb of *Tepko* addressed at [575] above).

1261. That leads to a further aspect in the context of the PA Councils. S&P submitted that the primary judge should have found that its potential liability was for an unascertainable amount or to an unascertainable class because the notes could have been sold on a secondary market and that an informal secondary market did develop when LGFS on-sold the notes to the PA Councils. We reject those contentions.

1262. There was no indeterminacy. As we have said, S&P's ratings applied only to an identified tranche of a nominated amount of Rembrandt 2006-3 notes: J[2747] and J[2451]. The size of the notes issued ([580] above), the level of minimum subscription ([580] above) and the 10 year period to the maturity of the notes (see [50] above) never altered. The quantum of S&P's liability was not indeterminate. Further, even if LGFS' sale to the PA Councils, or offer to buy back the notes from the PA Councils, was able to be described as a secondary market, the class was ascertainable (each was an investor in the Rembrandt notes) subject to the same prescribed parameters. That conclusion is reinforced by the fact that indeterminacy is assessed at the time of the impugned conduct, not at some later point in time: *Perre v Apand* at 221-222 [112] . The impugned conduct was S&P's failure to exercise reasonable care in forming, and to have reasonable grounds for, the opinion expressed by the rating. None of the parameters just addressed altered at the time of the impugned conduct. Two final points should be noted in this context. First, it was common ground that when the rating was issued, there was no secondary market in existence and, second, at all relevant times, S&P was in a position to withdraw or change the rating. It did not.

2.5.3 PA Councils not vulnerable

1263. S&P contended at trial and on appeal that the PA Councils were not vulnerable because they were capable of protecting themselves from the loss suffered. The primary judge found that the PA Councils were vulnerable: J[2767]-J[2778]. S&P submitted that finding was in error. Again it is necessary to address the legal and factual foundation for S&P's submission.

1264. The applicable legal principles have been addressed at [597]- [598] above. As we said at [598] above, in the field of negligent misstatement, vulnerability is the consequence of, not an additional criterion of, knowledge (actual or which a reasonable person would have) of reasonable reliance by an ascertainable class of persons. There is no superadded requirement of vulnerability in addition to the *Tepko* criteria.

1265. That leaves the application of those principles to the PA Councils. As we have said (at [599] above), S&P knew that an ascertainable class of persons (investors in the notes of which each of the PA Councils was a member) would be reliant on S&P's conduct. However, the conduct of S&P was not at large. Its function was to rate the notes and, in particular, a certain aspect of the notes – their creditworthiness: see [40]-[58] above. S&P knew that its function was specialised and that the members of that ascertainable class were likely to rely on S&P carrying out its function. Indeed, the only available information as to the creditworthiness of the notes was S&P's rating: see [581] above. None of the PA Councils could not replicate or "second-guess" S&P's rating or undertake its own analysis of the credit risk of the Rembrandt notes: see [39] and [580] above.

1266. It was that function – to rate the notes and, in particular, the creditworthiness of the notes – that informed the duty of care owed by S&P to the PA Councils. S&P's duty was not to protect against any loss suffered by the PA Councils. Its duty was to exercise reasonable care in forming and expressing the relevant opinion about the credit risk of the Rembrandt notes. It was in that respect, and that respect alone, that S&P owed a duty of care to the PA Councils because S&P knew of an ascertainable class of persons "who is or are reliant, and therefore vulnerable". That ascertainable class included the PA Councils.

1267. Contrary to S&P's submissions, none of the PA Councils was capable of protecting itself from the loss it suffered and the PA Councils were induced by S&P's conduct not to take steps to protect itself: *Perre v Apand* at 225 [118] . None of the PA Councils could replicate or "second-guess" S&P's rating: see [39] and [580] above.

1268. The other factual matters relied upon by S&P do not support S&P's contention that the PA Councils were not vulnerable. S&P submitted that the PA Councils were not vulnerable because they could have read the Pre-Sale Report and sought clarification from LGFS about aspects that they did not understand. The contention has been addressed at [602]-[604] and [1175]-[1177] above and is dismissed for those reasons. Put simply, the contention proceeds upon a false premise – that the documents were accurate. They were not. For, example, as the primary judge found, the Pre-Sale Report would not have assisted the PA Councils to identify the risks (J[1637]) as "the [Pre-Sale Report] did not disclose all of the risks of which LGFS was aware and did not purport to be a summary of the product suitable to be given to the [PA Councils] for the purpose of explaining the nature of and risks associated with the product". There was no step which the PA Councils could have taken to protect themselves from the faulty rating assigned by S&P. The inaccuracies in the Pre-Sale Report, together with S&P's faulty rating, are a complete answer to S&P's contention that the PA Councils could have protected themselves because they could have read the Pre-Sale Report and sought clarification from LGFS about aspects that they did not understand. As the primary judge said (at J[1639]), the PA Council witnesses "did not know what they did not know" and could never have asked the right questions to obtain the relevant information. The contention is rejected.

1269. S&P further submitted that even if the PA Councils were vulnerable (and they were), the primary judge erred in imposing a duty of care because as it did not know the identity of the PA Councils, it could not know they were vulnerable. That contention has been addressed in the context of indeterminacy and is rejected: see [1259]-[1262] above.

2.5.4 S&P did not control the PA Councils or have any direct dealings with them

1270. S&P had no contractual relationship with any of the PA Councils. S&P had a contractual relationship with ABN Amro. The significance of that contractual relationship has been addressed at [614]- [616] above.

1271. Next, it is necessary to address S&P's submission that the absence of a direct dealing between S&P and each PA Council precludes a duty being owed by S&P to a non-party such as the PA Councils. That submission is rejected. It is inconsistent with:

1. The principles of determinacy that a duty can be owed to a class: see [591] -[595] and [1259]-[1262] above. The PA Councils were within the class of "interested parties" referred to in the Ratings Letters;

2. The authorities which have held a duty to be owed even where there has been no direct relationship between the person who owed the duty and the person to whom the duty was owed: *The Dredge "Willemstad"* at 573-574 ; *Hedley Byrne* ; *Henderson* ; *Aiken v Stewart Wrightson*; *Kestrel Holdings* ; *Dartberg* and *BT Australia* ; and

3. What the primary judge described as the "real nature" of the transaction between S&P and ABN Amro: J[2780]. ABN Amro engaged S&P to provide the rating and paid S&P for it. But that statement is incomplete. It does not address the purpose of the rating, why S&P authorised the distribution of the rating or why S&P published the Pre-Sale Report and the Post-Sale Report: see [40]-[57] above. S&P knew that ABN Amro obtained and paid for the ratings for the sole

purpose of communicating the rating to “interested parties” so that those parties could consider the rating in deciding whether to invest in the notes: see also J [2759] and J[2775].

2.5.5 Councils acted unlawfully: s 625 of the Local Government Act

1272. The fourth limb of S&P’s arguments on appeal was that the duty should not be imposed on it because LGFS acted in contravention of the *Corporations Act* in purchasing and on-selling the notes to the PA Councils, and, finally, that the PA Councils were in breach of s 625 of the *Local Government Act* and the Ministerial Order in purchasing the Rembrandt notes: S&P Appeal Grounds Matrix Rows 11 and 12.

1273. The first limb, that LGFS acted in contravention of the *Corporations Act* in purchasing and on-selling the notes to the PA Councils, has been addressed in Part 4 , Section 1.1.4.4 above. The second limb raises the question whether the Rembrandt 2006-3 notes were “securities” under s 625(1) of the *Local Government Act* : J[2212]-J[2229].

1274. The PA Councils were entitled to “invest money that [was] not, for the time being, required by the council for any other purpose”: s 625(1) of the *Local Government Act* and [SAF8] However, “[m]oney [could] be invested only in a form of investment notified by order of the Minister published in the Gazette”: s 625(2) of the *Local Government Act* and [SAF8].

1275. The Ministerial Order permitted investment in certain investments. The relevant extracts of the Ministerial Order are at [20] above.

1276. At trial and on appeal, S&P contended that investment in Rembrandt 2006-3 was not permitted under s 625 of the *Local Government Act* as they were not “securities” as required by paras (k) and/or (l) of the Ministerial Order and were not otherwise authorised for investment by councils within the meaning of the Ministerial Order. S&P contended that the PA Councils’ purchase of Rembrandt 2006-3 in contravention of s 625 was unlawful and had a number of consequences: (1) it precluded the imposition of a duty of care because loss and damage could not be reasonably foreseeable; (2) no duty of care could arise on the basis of the principles set out in *Miller*, it being “incongruous for the law to proscribe the plaintiff’s conduct and yet allow recovery in negligence for damage suffered in the course, or as a result, of that unlawful conduct”: see *Miller* at 454 and (3) that the PA Councils could not establish causation because the “real, essential, substantial, direct or effective cause of the loss or damage” was not S&P’s negligence but the PA Councils’ unlawful conduct. ABN Amro adopted S&P’s submissions.

1277. By contrast, the PA Councils contended that the Rembrandt 2006-3 notes were “securities” for the purposes of the Ministerial Order. In the alternative, they contended that *Miller* did not lay down an inflexible rule precluding the recovery of damages. Rather, they contended that *Miller* required identification of the purpose of the law to determine whether a purpose of the law was to deprive the relevant offender of his or her civil remedies. They submitted that no such purpose could be divined from the *Local Government Act* .

1278. At trial, Bathurst conceded that the Rembrandt 2006-3 notes were not “securities” and therefore investment in them was unlawful. The primary judge found that Bathurst was not bound by its concession: J[2230]. S&P challenges that finding on appeal and we deal with its challenge at [1298]- [1301] below. Bathurst also submitted that *Miller* did not lay down a rigid test but that the consequences of statutory prohibitions would depend on the true construction and operation of the statute, referring to *Nelson v Nelson* (1995) 184 CLR 538 at 551 (Deane and Gummow JJ) and 611-613 (McHugh J); *Fitzgerald v FJ Leonhardt Pty Ltd* (1997) 189 CLR 215 at 2-7 (McHugh and Gummow JJ); *Yango Pastoral Co Pty Ltd v First Chicago Australia Limited* (1978) 139 CLR 410 and *Tonkin v Cooma-Monaro Shire Council* (2006) 145 LGERA 48 at 59-60 [67]-[72] .

1279. The primary judge held the Rembrandt 2006-3 notes were “securities” within the meaning of the Ministerial Order and that investment in the notes was authorised under s 625 of the *Local Government Act* : J[2215] and J[2225]. There was no error in her Honour’s approach.

1280. “Securities” is not defined in the *Local Government Act* or the Ministerial Order. Its meaning and effect must be determined by reference to ordinary principles of construction: J[2216]. The primary judge correctly accepted that the relevant principles of construction are those identified in *Project Blue Sky Inc v Australian Broadcasting Authority* (1998) 194 CLR 355 at 381-382 [69]-[71] and *CIC Insurance Ltd v Bankstown Football Club Ltd* (1997) 187 CLR 384 at 408 : J[2222]. Those principles do not need restating.

1281. The term “securities” in the Ministerial Order should therefore take its ordinary meaning: J[2216]. There is no reason to ascribe an artificially narrow meaning to the word “securities” in s 625 of the *Local Government Act* . As the primary judge held, “securities” is not limited to a debt which is secured but extends to a claim which is in some way secured and an “instrument which creates or acknowledges an obligation to pay a sum of money, even though it is the original source of the obligation and the obligation is executory”: *Handevel* at 217 and *Singer v Williams* [1921] 1 AC 41 at 49. That conclusion is reinforced by the express language of paras (k) and (l) of the Ministerial Order which use ratings as the control on the scope of investment in “securities”: J[2227]. In other words, on its face, the concept of securities in the Ministerial Order includes structured financial products like the Rembrandt 2006-3 notes.

1282. What then were the matters relied upon by S&P to contend that a different meaning of the word “securities” should be adopted?

1283. At trial and on appeal, S&P contended that the definition of “security” in the *Trustee Act 1925* (NSW) (**Trustee Act**) ought to be applied for the purposes of construing paras (k) and (l) of the Ministerial Order, with any necessary modifications to ensure that the definition reflects the purpose and policy of s 625 of the *Local Government Act* and the Ministerial Order. At all relevant times, the *Trustee Act* defined “security” in s 5 as “includes stock, funds, shares”.

1284. S&P’s argument proceeded on the basis that, prior to the Ministerial Order being introduced, the *Local Government Act* permitted Councils to invest in “any security authorised under the *Trustee Act 1925* ”. S&P submitted that construing “securities” in paras (k) and (l) of the Ministerial Order as meaning, *exhaustively*, “stock, funds, shares” (and thereby excluding “debentures”) was supported by a review of the legislative history of s 625 of the *Local Government Act* and the Ministerial Order and the purpose, and policy, of its predecessor provisions: J[2216]-J[2220]. S&P contended that if “securities” was construed as including “debentures”, it would render the phrase “debentures or” in paras (b), (c), (d), (e) and (m) of the Ministerial Order otiose.

1285. The primary judge considered and rejected those submissions: J[2225]. Her Honour correctly found that the reference to “securities” in the *Local Government Act* was not so limited.

1286. First, the definition in s 5 of “stocks, funds or shares” in the *Trustee Act* was inclusive, not exhaustive: J[2223]. In support of the contention that the word “includes” in s 5 should be interpreted as identifying an exhaustive list of securities, S&P referred to *YZ Finance Co Pty Ltd v Cummings* (1964) 109 CLR 395 at 398-399 . That authority does not assist S&P. In *YZ Finance* at 398, McTiernan J stated:

> The word “include” is very generally used in interpretation clauses in order to enlarge the meaning of words or phrases occurring in the body of the statute; and when it is so used these words or phrases must be construed as comprehending, not only such things as they signify according to their natural import, but also those things which the interpretation clause declares they shall include. But the word “include” is susceptible of another construction, which may become imperative, *if the context of the Act is sufficient to show that it was not merely employed for the purpose of adding to the natural significance of the words or expressions defined.*
>
> (Emphasis added.)

1287. There is nothing in the context of the *Trustee Act* or the *Local Government Act* that supports the contention that the latter construction should be adopted. Indeed, the contrary is the position. The *Trustee Act* specified authorised securities which were beyond the s 5 definition and also authorised investments in prescribed securities with a particular rating which excluded the investments expressly named in s 5 . For those reasons, the definition in s 5 cann ot have been intended to be exhaustive: J[2225]-J[2226].

1288. Second, the legislative history of the *Local Government Act* and the *Trustee Act* do not support S&P’s contention. As the primary judge explained (at J[2223]):

> In s 201 of the 1919 [Local Government] Act, for example, a council was authorised to invest in “any security authorised by the Trustee Act 1925 ”. In s 14(2) of the latter Act authorised securities were identified as including nominated debentures. The definition of “securities”, … was expressed to be inclusive of stocks, funds and shares. Insofar as it might be permissible to impugn any objective intention to the legislature it is apparent that under s 201 “any security authorised by the Trustee Act 1925 ” included the nominated debentures. This position remained at the enactment of the Local Government Act 1993 which … also identified permissible investments as “any security authorised by the Trustee Act 1925 ”. The authorised investments under the latter Act, then in s 14A(2) , also nominated as authorised securities various investments including investments in debentures. Authorised securities at this time included under s 14A(2)(m) “any debentures, promissory notes or other prescribed securities which” satisfied particular ratings requirements.

1289. As the primary judge found, immediately before the current regime, councils were permitted to invest in “any security” in s 14A(2) of the *Trustee Act* which included “any debentures, promissory notes or other prescribed securities [which satisfied particular ratings requirements]” but which excluded stocks or shares.

1290. When the relevant provision of the *Trustee Act* was repealed so that the *Local Government Act* no longer defined authorised investments by reference to the *Trustee Act* , the words “any debentures, promissory notes or other prescribed securities” in the former s 14A(2)(m) of the *T* *rustee Act* were condensed into the words "any securities" in the Ministerial Order and in a context where "securities" had long been used to refer to all nominated classes of permissible investments including debentures.

1291. As is apparent, S&P's submission that "securities" in the Ministerial Order should be interpreted as meaning only "stock, funds and shares" is not supported by the legislative history. Indeed, as the primary judge stated, S&P's construction of "security" in the *Trustee Act* would lead to the surprising result that two types of investments previously excluded under the old regime (stocks and shares) became two of only three permitted types of securities under the Ministerial Order: see [20] above. That is unlikely to have been the intention of the legislature.

1292. The third matter referred to by S&P was that "the Rembrandt notes are complex, relatively new, derivatives which could not in any stretch of the imagination be described as being 'conservative'" such that they cannot have been intended to be permissible investments for councils. That matter does not support S&P's "narrow" construction of "security" in s 625 of the *Local Government Act* . First, it ignores the role of credit ratings in controlling authorised investments. The Investment Guidelines indicated that credit ratings were the best independent information available as to the creditworthiness of an investment. Indeed, the Ministerial Order used credit ratings as a control over the scope of investments in securities by prescribing that investments must have a minimum credit rating of A from S&P (or its equivalent), which indicated that the investment had a "strong" capacity to meet its financial obligations. Second, S&P assigned the notes a AAA rating. As the PA Councils submitted, the construction of "securities" adopted by the primary judge was consistent with the mischief which the restriction on permissible investments imposed by the Ministerial Order was intended to remedy and consistent with the policy and purpose of the Ministerial Order. That was consistent with the objective of the *Local Government Act* and the Ministerial Order to promote the investment of public funds in safe and secure investments, determined by reference to the credit ratings assigned to those products by ratings agencies including S&P. Contrary to the submission of S&P, there was no requirement that investments authorised by the Ministerial Order be capital guaranteed.

1293. In the alternative, S&P argued at trial and on appeal that the common law definition of "securities" ought to be applied, tempered, if necessary, by reference to the purpose and policy of the provisions. S&P submitted that care must be taken to modify the common law meaning to recognise the purpose and policy of s 625 of the *Local Government Act* and the Ministerial Order and the mischief they were intended to cure, citing *R v Scott* (1990) 20 NSWLR 72 at 76-77 : see J[2216]. The primary judge comprehensively considered and rejected these arguments: see J[2216]-J[2229].

1294. S&P contended on appeal that while the primary judge found that the term "securities" should take its "ordinary meaning", her Honour incorrectly characterised and applied that meaning, or in the alternative incorrectly failed to modify that ordinary meaning, to reflect the purpose and object of the provisions. Specifically, S&P submitted, the applicable common law definition of securities includes an obligation to repay and no such obligation existed in the Rembrandt notes, thereby precluding them from being "securities" for the purposes of the Ministerial Order. That argument is rejected. As the primary judge stated (at J[2228]):

> Whether or not the Rembrandt CPDO created a debt ... it is apparent that it created a claim in some way secured or involved an instrument which creates or acknowledges an obligation to pay a sum of money. The mere fact that the obligation was not to repay the principal as invested does not change the legal character of the instrument so that it is not one which creates or acknowledges an obligation to pay a sum of money. The terms of the transaction created obligations in the trustee to pay the interest and principal as specified and to pay the balance of the cash deposit in the event of cash-out.

S&P did not identify any error in that finding. There is no inconsistency between this conclusion and the conclusion we reached at [665]ff that the Rembrandt notes were not a debenture. It was sufficient for the purposes of the Ministerial Order that the instrument acknowledged an obligation by Perpetual to pay a sum of money even though the issuer of the security did not undertake to repay the loan as a debt.

1295. Finally, the position adopted by S&P in relation to this issue is inconsistent. In relying on the disclaimer in the S&P Reports, S&P characterised the Rembrandt notes as a security. If the Rembrandt notes are not a security, that disclaimer has no application. S&P cannot and should not approbate and reprobate on this issue.

1296. For those reasons, the primary judge was correct to conclude that the Rembrandt notes were "securities" within the meaning of paras (k) and/or (l) of the Ministerial Order and were therefore authorised for investment by the Councils within the meaning of the Ministerial Order and s 625 of the *Local Government Act* .

1297. S&P's arguments in relation to statutory illegality and causation do not need to be considered further.

2.5.6 Bathurst's concession

1298. It is however necessary for us to deal with the further Appeal Ground of S&P relating to Bathurst's concession at trial that the Rembrandt notes were not "securities" for the purposes of s 625 of the *Local Government Act* and therefore investment in them was unlawful. The primary judge found that Bathurst was not bound by its concession because it involved an admission that was nothing but a conclusion of law: J[2230]. On appeal, Bathurst did not depart from its position that the notes were not securities but submitted that the primary judge was correct to hold that they were not bound by their concession.

1299. S&P contended that Bathurst was bound by its concession and that the primary judge erred. It argued that it was open for parties to make admissions of fact and law through pleadings or otherwise: *Dovuro Pty Ltd v Wilkins* (2003) 215 CLR 317 at 340 [69] (Gummow J) (McHugh J at 331 [40] and Heydon J at 372 [177] agreeing), 327 [25] (Gleeson CJ), and 348-349 [94] (Kirby J); *Lym International Pty Ltd v Marcolongo* [2011] NSWCA 303 at [130] (Campbell JA, Basten JA and Sackar J agreeing) and *Commissioner of Taxation v Star City Pty Ltd* (2009) 175 FCR 39 at 62-63 [89]-[95] .

1300. That much may be accepted. But as the primary judge noted, both *Dovuro* and *Marcolongo* dr aw a distinction between an admission as to a point of law and an admission as to a conclusion which depends upon the application of a legal standard: J [2230]. Different questions arise in relation to the latter type of admission, which has been described as "valueless" owing to the maker's general "unfamiliarity with the [legal] standard" governing such an admission: *Dovuro* at 340-342 [70]-[71] (Gummow J); *Grey v Australian Motorists and General Insurance Co Pty Ltd* [1976] 1 NSWLR 669 at 676 (Glass JA) and *Eastern Express Pty Ltd v General Newspapers Pty Ltd* (1992) 35 FCR 43 at 68 (Lockhart and Gummow JJ).

1301. Her Honour found that Bathurst's concession involved "nothing but a conclusion of law" which she had found to be wrong: J[2230]. By that we take her Honour to have meant that it involved a conclusion which depended on the application of a legal standard. S&P identified no error with her Honour's characterisation of the admission flowing from Bathurst's concession and it was entirely open for her Honour to hold, as she did, that Bathurst was not bound by that concession. We reject this Appeal Ground.

2.5.7 Conclusion

1302. The primary judge correctly found that it was foreseeable that potential investors in the Rembrandt notes, including the PA Councils, would suffer loss if the rating was not based on reasonable grounds or the product of the exercise of reasonable care. We reject S&P's contention that it was not foreseeable that potential investors would suffer loss and that the risk of loss was not significant (S&P Appeal Grounds Matrix Row 13) for the reasons at [588]-[595], [602]-[616] and [1272]-[1301] above.

2.6 Breach of duty

1303. S&P did not appeal against the primary judge's findings that S&P breached the duty it owed to the PA Councils, namely the duty to exercise reasonable care in forming, and to have reasonable grounds for, the opinion expressed by the rating: S&P Appeal Grounds Matrix Row 14.

3. STATUTORY CLAIMS

3.1 Introduction

1304. The PA Councils made a series of claims that S&P had engaged in misleading or deceptive conduct in contraventions of ss 1041E and 1041H of the *Corporations Act* and s 12DA of the *ASIC Act*. The primary judge held that S&P's rating of AAA of the Rembrandt notes was misleading and deceptive and involved the publication of information or statements false in material particulars to the class of potential investors in Australia, which included LGFS and the PA Councils, because by the AAA rating there was conveyed a representation that in S&P's opinion the capacity of the notes to meet all financial obligations was "extremely strong" and a representation that S&P had reached this opinion based on reasonable grounds and as the result of an exercise of reasonable care and skill when neither representation was true and S&P also knew them not to be true at the time they were made.

3.2 Section 1041H of the *Corporations Act*: S&P Appeal Grounds Matrix Rows 15 and 16

1305. S&P again challenged the primary judge's finding of liability under s 1041H of the *Corporations Act* on the grounds that the impugned conduct of S&P was not conduct "in this jurisdiction" within the meaning of that section. These Appeal Grounds were addressed at [729]-[745] in the context of LGFS' claim against S&P. These Appeal Grounds are substantively the same and are rejected for those reasons.

3.3 Section 1041E of the *Corporations Act*: S&P Appeal Grounds Matrix Rows 23, 24, 25 and 26

1306. S&P again challenged the primary judge's finding of liability under s 1041E of the *Corporations Act* that S&P made a statement or disseminated information that was false in a material particular and was materially misleading. These Appeal Grounds were addressed at [746]-[753] in the context of LGFS' claim against S&P. These Appeal Grounds are substantively the same and are rejected for those reasons.

3.4 Section 12DA of the *ASIC Act*: S&P Appeal Grounds Matrix Rows 17, 19, 20, 21 and 22

1307. S&P challenged the primary judge's finding that its conduct was misleading or deceptive in contravention of s 12DA of the *ASIC Act*. These Appeal Grounds were addressed at [754]-[764] in the context of LGFS' claim against S&P. These Appeal Grounds are substantively the same and are rejected for those reasons.

3.5 Conduct of S&P misleading or deceptive: S&P Appeal Grounds Matrix Rows 27, 28, 29 and 30

1308. S&P challenged the primary judge's finding that its conduct was misleading or deceptive. These Appeal Grounds were addressed at [765]-[773] in the context of LGFS' claim against S&P. These Appeal Grounds are substantively the same and are rejected for those reasons.

3.6 Causation: S&P Appeal Grounds Matrix Rows 31, 32, 33, 34, 35, 36, 37 and 38

1309. The causation Appeal Grounds (and the arguments S&P raised in relation to them) were addressed at [774]-[794] and [797]-[800] in the context of LGFS' claim against S&P, and at [1272]-[1301] above. These Appeal Grounds are substantively the same and are rejected for those reasons.

4. CONTRIBUTORY NEGLIGENCE

1310. This is addressed in Part 13 below.

5. LOSS AND DAMAGE

1311. S&P raised three matters on appeal against the PA Councils:

1. To establish causation on each of its claims, the PA Councils had to prove on the balance of probabilities that, absent the impugned conduct, they would have

taken some other more beneficial course (the **Alternative Universe Contention**): S&P Appeal Grounds Matrix Rows 47 and 50;

2. The PA Councils' claim infringed the "rule" in *Potts v Miller* : S&P Appeal Grounds Matrix Rows 47-48 and 51-56; and

3. The primary judge failed to deduct the amount of the coupon (or interest) payments made to the PA Councils (the **Coupon Contention**): S&P Appeal Grounds Matrix Row 49.

1312. The Alternative Universe Contention was addressed at [786]-[790] and [934]-[935] above. These Appeal Grounds are rejected for the same reasons. The Appeal Grounds founded on *Potts v Miller* were addressed at [958]-[988] above and are rejected for those reasons. The Coupon Contention was addressed at [989] above. This Appeal Ground is rejected for the same reasons.

PART 10: PA COUNCILS' PURCHASE OF 2006-3 NOTES: ABN AMRO

1. INTRODUCTION

1313. The PA Councils' claim against ABN Amro was for misleading and deceptive conduct, knowing involvement in S&P's misleading and deceptive conduct and negligence. ABN Amro was found to be knowingly concerned in S&P's contraventions of the various statutory provisions proscribing such misleading and deceptive conduct, and also itself having engaged in conduct that was misleading and deceptive by publishing information or statements false in material particulars and otherwise involved in negligent misrepresentations to the class of potential investors with which ABN Amro knew LGFS intended to deal, being the PA Councils, by reason of ABN Amro's deployment of the AAA rating and its own representations as to the meaning and reliability of the AAA rating which also were not true and which ABN Amro knew not to be true at the time they were made.

1314. ABN Amro appealed those findings. This section of the judgment will deal with the tort claims and then the statutory claims.

2. FACTUAL FINDINGS

1315. The facts relevant to ABN Amro's involvement have been addressed in [813] above. It is unnecessary to repeat that detailed analysis.

1316. Put simply, ABN Amro created the Rembrandt notes for LGFS to enable LGFS to sell a structured financial product to councils. ABN Amro's task was directed to that end. ABN Amro was aware that LGFS would on-sell any financial product it purchased to councils: see [60] above. ABN Amro knew that LGFS would reasonably rely on the AAA rating and the representations ABN Amro made about it. ABN Amro intended that LGFS would rely on the rating: see [813] above. The insurmountable hurdle for ABN Amro was that it knew that the rating was unreliable and lacked reasonable grounds: see Part 3 above.

1317. It will be necessary to return to consider these factual findings below.

3. TORT CLAIMS: ABN Amro Appeal Grounds Matrix Rows 69-79

3.1 Introduction

1318. The findings against ABN Amro were significant. ABN Amro was found to have known that S&P's rating lacked reasonable grounds and was not the product of the exercise of reasonable care and skill on the part of S&P: J[3212].

1319. ABN Amro was found liable in negligence to the PA Councils (and to LGFS) for promoting the AAA rating when it knew it lacked reasonable grounds. ABN Amro was also found to owe to the PA Councils, as members of the class of known intended purchasers of notes from LGFS, a duty to exercise reasonable care and skill in the provision of information and advice to LGFS about the Rembrandt 2006-3 notes: J[3279]. ABN Amro was found to have breached that duty when it failed to disclose to LGFS (and therefore the PA Councils) that the rating could not be relied upon: J[3280] and J[3201]-J[3204].

1320. On appeal, ABN Amro challenged the imposition of the duty and that it breached that duty: ABN Amro Appeal Grounds Matrix Rows 69-77.

3.2 Did a duty of care exist?

3.2.1 Introduction

1321. In relation to the imposition of the identified duty, ABN Amro identified eight reasons why it contended that the duty should not have been imposed:

1. ABN Amro did not know that LGFS intended to market the Rembrandt 2006-3 notes to the PA Councils or any specific matter which might have enabled it to assess the type of information which should be provided to the PA Councils: ABN Amro Appeal Grounds Matrix Row 70;

2. ABN Amro had no control over what (if any) information LGFS provided to the PA Councils: ABN Amro Appeal Grounds Matrix Row 71;

3. ABN Amro did not assume responsibility for the provision of information to the PA Councils: ABN Amro Appeal Grounds Matrix Row 72;

4. ABN Amro did not assume responsibility to LGFS "for modelling and structuring" the Rembrandt 2006-3 notes: ABN Amro Appeal Grounds Matrix Row 73;

5. The PA Councils were not vulnerable to a breach of the alleged duty by ABN Amro: ABN Amro Appeal Grounds Matrix Row 74;

6. The alleged duty was incompatible with the contractual relationship between ABN Amro and LGFS: ABN Amro Appeal Grounds Matrix Row 75;

7. The alleged duty would leave ABN Amro exposed to liability in an indeterminate amount to an indeterminate class: ABN Amro Appeal Grounds Matrix Row 76;

8. The alleged duty would require ABN Amro to review and assess the adequacy of S&P's rating of the Rembrandt 2006-3 notes in circumstances where (ABN Amro Appeal Grounds Matrix Row 77):

(1) S&P was an expert ratings agency and ABN Amro was not;

(2) ABN Amro had no power to require S&P to disclose to it the basis on which it rated the Rembrandt 2006-3 notes or any other CPDO;

(3) S&P's rating of the Rembrandt 2006-3 notes and other CPDOs necessarily involved matters of judgment which ABN Amro could not assess adequately or at all;

(4) Potential purchasers of the Rembrandt 2006-3 notes were interested to know S&P's opinion as to their creditworthiness, not ABN Amro's; and

(5) This would cause ABN Amro to incur significant costs without being likely to produce any commensurate benefit.

1322. None of these reasons is valid.

3.2.2 Applicable principles

1323. In identifying the applicable legal principles, ABN Amro referred to and relied upon the submissions it made in relation to LGFS' claim against ABN Amro. Those submissions and the analysis of the relevant applicable principles are set out at [808]- [812] above and, by reference, at [573]-[578] and [589]-[595] above.

1324. A recipient of information or advice is owed a duty by the speaker if (a) that recipient is part of a class to whom the statement or advice is directed and (b) reliance on the statement or advice by a member of the class is consistent with the substance of the purpose for which the statement is made or advice given: see [573] and [578] above. It is those principles which must be kept at the forefront of any consideration of the duty found to be owed by ABN Amro to the PA Councils.

3.3.3 Findings

1325. The facts surrounding the Councils' purchase of the Rembrandt 2006-3 notes are addressed in Part 2 , Section 4 (ABN Amro), Section 6 (Sale of Notes to LGFS), Section 7 (Sale of Notes to the Councils) and in Part 5 , Section 1.2.3 in relation to LGFS' claim against ABN Amro and at [1019]-[1062] above. It is unnecessary to repeat or amplify those facts except in respect of a particular Appeal Ground addressed later in these reasons.

3.2.4 Appeal Grounds

1326. It is against that background that we address ABN Amro's Appeal Grounds which it contended demonstrated that the identified criteria for the imposition of a duty to exercise reasonable care in making a statement or giving advice (see [573] above) were absent.

1327. ABN Amro contended that “there was simply no relationship between ABN [Amro] and the PA Councils sufficient to support the imposition of such a duty”. It further contended that “[t] aken together, the following uncontroversial factual matters precluded a finding that there was any relationship”. Those contentions are rejected.

3.2.4.1 ABN Amro did not know that LGFS intended to market the Rembrandt 2006-3 notes to the PA Councils or any specific matter which might have enabled it to assess the type of information which should be provided to the PA Councils

1328. Three questions were raised by ABN Amro’s submission. First, did ABN Amro know that LGFS intended to market the Rembrandt 2006-3 notes to the Councils? The answer is yes. Contrary to ABN Amro’s submission, there was evidence that the PA Councils would trust in ABN Amro’s especial competence to give information or advice about the Rembrandt 2006-3 notes. The relevant facts have been identified earlier: see [813] above. Those facts support the factual findings summarised at [1316] above.

1329. The second question was whether it was necessary for ABN Amro to know the identity of the *s pecific* councils to whom the notes were to be marketed. ABN Amro relied on particular aspects of its cross-examination of Mr Hilder at trial to establish that it did not know the level of sophistication of each PA Council, their risk appetite and investment portfolio and, therefore, no duty could arise in relation to the PA Councils with respect to the provision of information by ABN Amro to LGFS. That cross-examination was as follows:

> *At no time up to the middle of ‘07 did you disclose to anyone at ABN the investment strategy or policy of any particular council?*No.
>
> *Nor the investment portfolio of any council?*No. I wouldn’t do that, no.
>
> *And at no time up to the middle of ‘07 did you disclose to ABN your understanding of the level of financial sophistication of any council?*No.
>
> *And didn’t disclose the name of any council you were seeking to sell the Rembrandt product to?*No - well, I don’t think so.

1330. This submission goes nowhere. It was not necessary for ABN Amro to know the identity of specific councils: see [589]-[595] above. The fact that it did not know the PA Councils specifically does not militate against the imposition of the second duty: see [587]- [595] above. In any event, it knew a sufficient amount about local councils in New South Wales generally to justify the imposition of a duty: see [813] above and, in particular, [83]- [84] and [121]- [122] above.

1331. The third question concerned the information LGFS would provide to the PA Councils to enable them to assess the Rembrandt 2006-3 notes and ABN Amro’s knowledge of that information. ABN Amro provided information about the notes to LGFS. ABN Amro submitted that it did so in response to LGFS’ requests for information for LGFS’ own purposes and not for the provision to the PA Councils. In support of this contention, ABN Amro referred to cl 3.4 of the Mandate Letter: see [83] above. ABN Amro submitted that cl 3.4 prevented the disclosure of information by LGFS to the PA Councils. This contention does not address the duty found to be owed by ABN Amro. The duty found was a duty to exercise reasonable care in the provision of information and advice to *LGFS* about the product. That did not mean that ABN Amro was required to provide LGFS with anything, but if it chose to, it had to exercise reasonable care in doing so. By choosing to provide information about the notes to LGFS, ABN Amro had to exercise reasonable care with the result that it had to tell LGFS that it knew or ought to have known information it was providing was not reliable. That basic obligation did not require ABN Amro to know anything about the characteristics of the individual councils. That basic obligation arose because ABN Amro was seeking to arm LGFS with the means to sell the notes to the PA Councils: see [813] above. The problem for ABN Amro was that it armed LGFS with information and advice which was wrong – the rating. ABN Amro knew that S&P's rating lacked reasonable ground and was not the product of the exercise of reasonable care and skill on the part of S&P: see Part 3 above.

3.2.4.2 ABN Amro had no control over what (if any) information LGFS provided to the PA Councils

1332. ABN Amro contended that it could not ensure that LGFS provided to the PA Councils the information and advice ABN Amro provided to LGFS. This factor was said to be a reason why there was "minimal utility" in imposing on ABN Amro a duty to the PA Councils in relation to information and advice provided to LGFS when ABN Amro could not ensure that information was provided by LGFS to the PA Councils.

1333. This contention does not address, and in fact ignores, the facts. ABN Amro was negligent in promoting the AAA rating to LGFS: see [805]-[860] above. If ABN Amro had not been negligent, ABN Amro would not have promoted the rating to LGFS. Moreover, ABN Amro knew that LGFS would rely on S&P's rating and the ABN Representations, ABN Amro intended that LGFS would rely on the rating and that LGFS would market the Rembrandt 2006-3 notes to the PA Councils on the basis of the AAA rating and on the basis of the ABN Representations and that the rating was unreliable. If ABN Amro had provided LGFS with accurate information (and it did not) and then LGFS failed to pass it on to the PA Councils, then LGFS would be liable and ABN Amro would not be liable. That was not what occurred. This Appeal Ground is dismissed.

3.2.4.3 ABN Amro did not assume responsibility for the provision of information to the PA Councils

1334. ABN Amro submitted that it was not appropriate to impose on ABN Amro a duty to the PA Councils in relation to information or advice about the Rembrandt 2006-3 notes provided to LGFS when it had assumed *no* responsibility for the information or advice which LGFS itself provided to the PA Councils. ABN Amro conceded on appeal that "it may be that it was, or ought to have been, reasonably foreseeable to ABN [Amro] that LGFS would market the Rembrandt 2006-3 notes to local councils generally on the basis of S&P's AAA rating, and that councils might suffer loss if the rating was incorrect": see also J[3272]-J[3274]. However, it contended that this was not sufficient to make ABN Amro "responsible" for the provision of the rating to the PA Councils: cf J[3274].

1335. This Appeal Ground is dismissed for the same reasons as the previous Appeal Ground. It fails on the facts. ABN Amro knew that LGFS would rely on S&P's rating and the ABN Representations, ABN Amro intended that LGFS would rely on the rating and that LGFS would market the Rembrandt 2006-3 notes to the PA Councils on the basis of the AAA rating and on the basis of the ABN Representations and that the AAA rating was unreliable.

1336. These findings do not "bypass" the requirement for a relationship of the relevant kind between ABN Amro and the PA Councils before the imposition of the duty. In fact, these findings establish that the requirements for a relationship of the relevant kind between ABN Amro and the PA Councils were satisfied: see [573]-[574].

3.2.4.4 ABN Amro did not assume responsibility to LGFS "for modelling and structuring" the Rembrandt 2006-3 notes

1337. This Appeal Ground was not separately addressed by ABN Amro. It fails for the reasons set out in Part 5 , Section 1.3 above. ABN Amro did assume responsibility to LGFS "for modelling and structuring" the Rembrandt 2006-3 notes.

3.2.4.5 The PA Councils were not vulnerable to a breach of the alleged duty by ABN Amro

1338. This Appeal Ground concerned the PA Councils' vulnerability. ABN Amro submitted that the primary judge was incorrect to conclude that the PA Councils, who had, in LGFS, a "sophisticated, licensed financial services provider protecting their interests", were unable to protect themselves against a want of care in the provision of information by ABN Amro to that provider.

1339. ABN Amro submitted that the PA Councils were able to protect themselves by the terms on which they contracted with LGFS including, for example, by obtaining a warranty as to the accuracy and completeness of the information which LGFS provided to them: *Perre v Apand* at 226 [120] . ABN Amro submitted that the fact that LGFS had no capacity to replicate S&P's ratings modelling was not an answer because it impermissibly focussed on S&P's rating rather than the general nature of the duty of care imposed on ABN Amro. Finally, ABN Amro submitted that another factor which supported its contention that the PA Councils were not vulnerable was that they were wholesale clients under s 761(7)(a) of the *Corporations Act* and trustees of substantial amounts of public funds with obligations to understand, and with sufficient resources to engage qualified staff and advisors to control, their investments.

1340. There is a complete answer. The PA Councils were vulnerable: see [1263]-[1269] above. The PA Councils' financial adviser, LGFS, was vulnerable: see [817]-[833] above. ABN Amro knew that S&P's rating lacked reasonable grounds and was not the product of the exercise of reasonable care and skill on the part of S&P: see Part 3 above. ABN Amro alone had the capacity, and did, replicate S&P's rating: J[3275]. Neither LGFS nor the PA Councils could or did replicate S&P's rating: see [599]-[600] and [1265] above. Moreover, as we have said earlier (see [1037] above), their vulnerability was not limited to the rating and ABN Amro knew that from the outset: see [39] above. ABN Amro obtained the rating because many potential investors would not have the resources or expertise to assess the creditworthiness of the CPDO or to second-guess the rating of a structured financial product: J[2759] and J[2816]. ABN Amro had no basis to believe that LGFS or any council in New South Wales had the resources or the capacity to check the rating: J [3275]. The PA Council witnesses' "did not know what they did not know" and thus could never have asked the right questions to obtain the relevant information: J[1620], J[1639] and [1177] above.

3.2.4.6 The alleged duty was incompatible with the contractual relationship between ABN Amro and LGFS

1341. ABN Amro contended that the alleged duty was incompatible with the contractual relationship between ABN Amro and LGFS. That relationship was the Mandate Letter: see [83] above. That contention has been addressed at [1332]- [1333] above and is rejected for the same reasons.

3.2.4.7 The alleged duty would leave ABN Amro exposed to liability in an indeterminate amount to an indeterminate class

1342. ABN Amro's submissions in relation to indeterminate liability raise the same substantive issues as S&P's contentions. They are rejected for the same reasons: see [1259]-[1262] above and for the further reasons set out in Part 10, Section 3.2.4.1 above.

3.2.4.8 The alleged duty would require ABN Amro to review and assess the adequacy of S&P's rating of the Rembrandt 2006-3 notes in circumstances where it was inappropriate or impossible

1343. ABN Amro submitted that the imposition of duty required ABN Amro to assess the competency with which S&P rated the Rembrandt 2006-3 notes and therefore the duty was inefficient, inutile and inappropriate. In support of that contention, ABN Amro referred to the following facts and matters:

1. ABN Amro (like other arrangers) was not expert in conducting credit ratings, whereas S&P (as an expert credit rating agency) was;

2. Not having designed the CPDO, S&P was independent of the Rembrandt 2006-3 notes, whereas ABN Amro, as the arranger of the product, was not;

3. S&P was not obliged to disclose to ABN Amro its rating methodology or reasoning; and

4. Potential purchasers of the Rembrandt 2006-3 notes were interested in the opinion of S&P as to the creditworthiness of the notes, rather than the opinion of ABN Amro.

According to ABN Amro, viewed overall, the imposition of the duty required ABN Amro to incur significant costs without being likely to produce any commensurate benefit or, indeed, any benefit at all.

1344. This contention fails on the facts. The submission that S&P was the expert credit ratings agency and not ABN Amro does not address ABN Amro's role in procuring the rating and its knowledge of S&P's ratings process: see Part 3 above and J[3155]. ABN Amro designed the product: see [158] above. ABN Amro was capable of assessing the creditworthiness of the CPDO. Indeed, it was more capable than S&P and identified shortcomings in the rating before S&P: see, for example, [220]- [226] above. ABN Amro knew that S&P was using ABN Amro's model, was aware of the process applied by S&P to rate the Rembrandt notes and of all material inputs S&P used in its modelling: see Part 3 above and J[3208]. ABN Amro's involvement was so great that the rating was not independent: see, by way of example, [434] above.

1345. Having regard to ABN Amro's intimate knowledge of the product and the rating, it was not unreasonably burdensome for ABN Amro to exercise reasonable care and skill in providing information to LGFS about the Rembrandt notes. Of course, it must be recalled that ABN Amro had no difficulty in disclosing to LGFS what it identified and described as the "key risks" associated with the CPDO: see [62] above and J[3271]-[3277] and J[3207]. As the primary judge said at J[3207], ABN Amro was intimately involved in the closest possible scrutiny of S&P's work to ensure a AAA rating and the duty arises because of the actual relationship between ABN Amro, S&P and LGFS.

1346. ABN Amro's reference to incurring significant costs without being likely to produce any commensurate benefit or, indeed, any benefit at all is fanciful. ABN Amro incurred costs in conducting modelling that was designed to assess the creditworthiness of the Rembrandt notes, the results of which it used to try to persuade S&P to assign a AAA rating: see Part 3 above. As the primary judge stated "ABN Amro did comprehensively review S&P's rating for the purposes of ensuring that ABN Amro got what it wanted, the rating of AAA": J [3211]. Potential purchasers would have been interested in knowing facts that made or ought to have made ABN Amro aware that S&P's opinion was unreasonable and unreliable.

3.3 ABN Amro breached the duty?

1347. ABN Amro was found to have known that S&P's rating lacked reasonable grounds and was not the product of the exercise of reasonable care and skill on the part of S&P: J[3212]. ABN Amro was found liable in negligence to the PA Councils (and to LGFS) for promoting the AAA rating when it knew it lacked reasonable grounds. ABN Amro was also found to owe to the PA Councils, as members of the class of known intended purchasers of notes from LGFS, a duty to exercise reasonable care and skill in the provision of information and advice to LGFS about the Rembrandt 2006-3 notes: J[3279]. ABN Amro was found to have breached that duty when it failed to disclose to LGFS (and therefore the PA Councils) that the rating could not be relied upon: J[3280] and J[3201]-J[3204]. ABN Amro appealed against the findings that it breached those duties on, amongst other things, the basis that the rating could achieve a AAA rating at 25% volatility (the volatility issue, in particular taking into account the rebalancing referred to at [148] above): ABN Amro Appeal Grounds Matrix Row 78.

1348. For the reasons set out in Part 3, this Appeal Ground fails . ABN Amro is not entitled to raise the rebalancing issue on appeal (see [387]-[418] above) and we have rejected ABN Amro's submissions on the volatility issue: see [431]ff above. ABN Amro knew (or at the very least, ought to have known) that S&P's rating lacked reasonable grounds and was not the product of the exercise of reasonable care and skill on the part of S&P and it failed to disclose to LGFS (and therefore the PA Councils) that the rating could not be relied upon.

4. STATUTORY CLAIMS

4.1 Introduction

1349. The primary judge found that ABN Amro contravened ss 1041H and 1041E of the *Corporations Act* and s 12DA of the *ASIC Act* by *causing* or *permitting* the *publication* or *communication* of the fact that S&P had assigned a AAA rating to the Rembrandt 2006-3 notes to a class of potential purchasers of the notes (including the PA Councils) in circumstances where ABN Amro was aware, or ought reasonably to have been aware, that the rating was misleading because the rating conveyed the S&P Representations (see [723] above) on which the PA Councils relied, which were themselves misleading: J[3238] and J[3243]. ABN Amro challenged those findings on appeal: ABN Amro Appeal Grounds Matrix Rows 59-68. Section s 1041H of the *Corporations Act* and s 12DA of the *ASIC Act* will be dealt with together.

4.2 Section 1041H of the *Corporations Act* and s 12DA of the *ASIC Act*

1350. The relevant legislative provisions and applicable legal principles have been addressed earlier: see [724]ff above. It is against that background, that we consider the various Appeal Grounds that ABN Amro pursued on appeal.

1351. First, the findings of the primary judge. The primary judge held:

1. That "it is sufficient if the conduct is misleading whether or not the corporation knew or ought to have known it was misleading": J[3244];

2. ABN Amro promoted and disseminated the rating, which carried with it the S&P Representations which were false and misleading: J[3250];

3. ABN Amro made an implied representation that the rating could be safely relied upon: J[2997(5)], J[2995(6)], J[3088] and J[3097];

4. ABN Amro "went far beyond acting as a mere conduit for S&P's rating. It used the AAA rating as a springboard for its marketing and in so doing both adopted it as its own ... and represented that S&P's opinion could be safely relied on": J[3097];

5. ABN Amro represented to LGFS that the capacity of the Rembrandt notes to pay interest and principal was extremely strong and that the rating could be relied upon (J[3098]-[3099]) and those representations were false (to ABN Amro's knowledge): J[3098];

6. ABN Amro had actual knowledge of the falsity of the AAA rating and the representations ABN Amro made about it: J[3245];

7. Even if the evidence fell short of actual knowledge on ABN Amro's part, it readily supports the inference that ABN Amro ought to have known of the misleading nature of the AAA rating: J[3246];

8. Given what ABN Amro knew it is difficult to see how ABN Amro could have deployed the AAA rating at all without engaging in misleading conduct: J[3174].

1352. ABN Amro's challenges to these findings and the imposition of the contraventions of the statutory provisions are addressed under two headings – (1) ABN Amro's conduct and (2) whether that conduct was misleading.

4.2.1 ABN Amro's conduct

1353. ABN Amro contended that it did not *cause or permit* the publication or communication *to the PA Councils* of the fact that S&P had assigned a AAA rating to the Rembrandt 2006-3 notes.

1354. At trial and again on appeal ABN Amro referred to three matters in support of that contention. First, that ABN Amro had no direct dealings with the PA Councils which could be considered material. Second, that publishing or communicating S&P's rating to the PA Councils was a step LGFS took of its own volition and not in response to any requirement imposed, or even suggested, by ABN Amro and, third, that no permission from ABN Amro was given or required for LGFS to publish or communicate the fact of S&P's rating to the PA Councils (the rating in fact being publicly accessible to any interested person).

1355. **Following paragraph cited by:**

> Postorino v Encryption Technologies Corporation Pty Ltd (19 June 2015) (Lloyd-Jones J)
>
> 151. Postorino argues that Pritchard also represented that ETC was worth $30 million and that he gave the information to Coombs with the intention that Coombs inform Postorino of the asserted value of the company, as Coombs did. Coombs communicated with Postorino for the benefit of Pritchard and for the purposes of promoting the sale of ETC shares by Pritchard's company. The communication was designed to induce Postorino to buy the shares from Pritchard or his company Bond Street, and was made at Pritchard's instigation. By reference to *ABN AMRO Bank NV v Bathurst Regional Council* (supra) at [1355] there is an analogy (ambient not identical) to this matter and Pritchard has already admitted making the representation to Postorino.

None of these matters assist ABN Amro. They do not assist because each is contrary to, or at the very least ignores, the findings in relation to ABN Amro's conduct that have been addressed at Part 3 above. That conduct necessarily includes the circumstances in which LGFS dealt with ABN Amro: see Part 2 , Section 6 and [813] above. As a result of that relationship, and those dealings between ABN Amro and LGFS, ABN Amro knew, or ought to have known, that LGFS would supply the rating to the PA Councils and that the PA Councils would rely upon it: see Part 2 , Section 6 and [813] above. Those facts establish that ABN Amro caused or permitted the publication or communication to the PA Councils of the fact that S&P had assigned a AAA rating to the Rembrandt 2006-3 notes. No other conclusion is open.

1356. As the primary judge said (at J[3243]):

> It may be accepted that ABN Amro had no direct dealings with the councils which can be considered material. The case of the councils against ABN Amro, however, is not confined to the fact that ABN Amro merely engaged S&P to assign the rating. As ABN Amro knew, LGFS intended to market and sell the Rembrandt 2006-3 notes to councils

in New South Wales, a defined (needed, narrow) market. ABN Amro knew that LGFS had made the AAA rating a condition precedent of the purchase of the notes. Whatever else its relevance the communication from Mr Cordeiro of ABN Amro to LGFS of 5 April 2006 disclosed that ABN Amro understood that LGFS's goal was to be able to market to councils a product with a high degree of security and a stable rating. So much must again have been obvious to ABN Amro in respect of the specific Rembrandt 2006-3 product given LGFS's insistence on the assignment of the AAA rating it required before it purchased the notes. It equally must have been obvious to ABN Amro that LGFS needed to be able to communicate to its clients, the councils, the AAA rating. Unless LGFS could do so its arrangement with ABN Amro as reflected in the mandate letter made no sense. ABN Amro thus knew that the AAA rating would be communicated by LGFS to potential council investors. It follows that ABN Amro knew or ought to have known that LGFS would convey to the councils also that the AAA rating meant that the product had a degree of security or default risk commensurate with the AAA rating, at least in the most general sense of the meaning of the rating as the product having an extremely strong capacity to pay interest and principal. Yet, as I have found, ABN Amro in fact knew that the AAA rating was unreasonable and unjustified.

1357. Contrary to ABN Amro's contention, the factual findings establish that ABN Amro caused or permitted the publication or communication of the fact that S&P had assigned a AAA rating to the Rembrandt 2006-3 notes to a class of potential purchasers of the notes (the PA Councils). Indeed, as the PA Councils pointed out, if ABN Amro had told LGFS of the rating but sought to preclude LGFS from telling the PA Councils about it, LGFS would not have bought the product. Why? Because LGFS would not have been able to market it to councils using the rating and the entire purpose of the transaction recorded in the Mandate Letter would have been defeated.

1358. In this context, ABN Amro identified three further matters. First, a pleading point. It submitted that the PA Councils never alleged that ABN Amro misled LGFS or alleged that ABN Amro made any misrepresentation. That submission is rejected. At trial, the PA Councils alleged that ABN Amro knew or ought to have known that LGFS and the PA Councils would rely on statements made, and information provided, by ABN Amro about the notes, that it communicated the fact of the rating to LGFS and the PA Councils with the intention that they would rely on it and failed to disclose to LGFS and the PA Councils that the rating was deficient and could not be relied upon. That pleading formed a sufficient basis for the primary judge's findings.

1359. ABN Amro's contention that the PA Councils did not allege the making of any misrepresentations by ABN Amro misstates the PA Councils' case for another reason. To establish that ABN Amro engaged in misleading and deceptive conduct, the PA Councils were required to prove that ABN Amro promoted and disseminated the rating, which carried with it the S&P Representations (see [723] above) which were false and misleading: see [765]-[773] above. The PA Councils proved those elements and the primary judge made that finding: J[3250]. It was no answer for ABN Amro to say that it told the truth when it conveyed that the Rembrandt notes had been assigned a AAA rating. ABN Amro did not merely pass on the rating "for what it was worth" or disclaim any belief in its truth or falsity (*Yorke* at 666, approved in *Butcher* at 605 [38]-[39] and 629-630 [123]): see [886] above. As the primary judge found, ABN Amro "went far beyond acting as a mere conduit for S&P's

rating, it used the AAA rating as a springboard for its marketing and in doing so both adopted it as its own … and represented that S&P's opinion could be safely relied on": see [881]- [905] above and J[3097]. The rating carried with it the S&P Representations: see [723] above.

1360. ABN Amro further submitted that it did not engage in misleading conduct in relation to LGFS and that LGFS did not rely on any misleading conduct of ABN Amro. Those contentions are wrong. They were addressed and rejected at [906] above.

4.2.2 Was ABN Amro's conduct misleading?

1361. Even if ABN Amro engaged in the impugned conduct (as we have found), ABN Amro submitted that the primary judge erred in finding that that conduct was misleading. ABN Amro submitted the "conduct against ABN [Amro] was of a very narrow and specific kind; namely, that it caused or permitted the publication or communication to the PA Councils of *the fact* that S&P had assigned a AAA rating to the Rembrandt 2006-3 notes where ABN [Amro] knew the rating was misleading".

1362. That contention fails at the first hurdle for the reasons set out at [1349] above – ABN Amro's conduct carried with it the S&P Representations, which were themselves misleading. Next, as the primary judge said, "[g]iven what ABN Amro knew, it is difficult to see how ABN Amro could have deployed the AAA rating without engaging in misleading and deceptive conduct": J[3174]. ABN Amro knew the S&P Representations and ABN Representations to be false: see Part 3 and [906] above. It knew, or at the very least, ought to have known that S&P's AAA rating of the Rembrandt notes was unreasonable and unjustified and therefore misleading: see Part 3 above. ABN Amro knew, or ought to have known, that S&P's rating of the Rembrandt notes was negligent and, further, ABN Amro did not have reasonable grounds for the opinions it expressed through the ABN Representations: see Part 3 above. ABN Amro lacked a reasonable basis for its representations as to the creditworthiness of the notes: see Part 3 and in particular [563] above. ABN Amro lacked a reasonable basis for its representations as to the reliability of S&P's rating: see Part 3 and in particular [563] above. The primary judge was correct to find that ABN Amro in fact knew that S&P's rating was not reliable: see Part 3 and in particular [563] above.

1363. It was in this context, that ABN Amro sought to contend that S&P's rating was reasonable and justified: ABN Amro Appeal Grounds Matrix Row 62A. ABN Amro is not permitted to raise the rebalancing issue on appeal (see [387]-[418] above) and, in any event, its Appeal on the volatility issue is dismissed for the reasons set out at Part 3 above.

1364. That analysis also provides a complete answer to a further ABN Amro Appeal Ground: ABN Amro Appeal Grounds Matrix Row 63. Contrary to ABN Amro's contentions, the primary judge was correct to find that ABN Amro did not care whether S&P's rating of the Rembrandt notes and the S&P Representations were true or false: see Part 3 above.

1365. These Appeal Grounds are dismissed. ABN Amro engaged in misleading conduct in contravention of ss 1041H of the *Corporations Act* and s 12DA of the *ASIC Act* .

4.3 Section 1041E of the *Corporations Act*

1366. The PA Councils' case against ABN Amro under s 1041E of the *Corporations Act* was substantially the same as their case under s 1041H of the *Corporations Act* save that the claim under s 1041E required proof of the necessary mental element. On appeal, ABN Amro sought to advance the same so-called errors as those it advanced in relation to s 1041H of the *Corporations Act*. These Appeal Grounds are rejected for the same reasons as [1350]-[1365] above.

1367. ABN Amro knew, or at the very least, ought to have known that S&P's rating of the Rembrandt notes was unreasonable and unjustified and therefore misleading: see Part 3 above. ABN Amro had actual, or at the very least constructive knowledge, that the rating was misleading and did not care whether the AAA rating itself, and what was conveyed by that AAA rating, was true or false: see Part 3 above.

4.4 Accessorial liability claims

1368. The primary judge found that ABN Amro was knowingly concerned in, or party to, or aided, abetted, counselled or procured, S&P's contraventions of ss 1041E and 1041H of the *Corporations Act* (within the meaning of ss 79 and 1041I of the *Corporations Act*): J[3254]-J[3266]. On appeal, ABN Amro challenged that finding: ABN Amro Appeal Grounds Matrix Rows 66-68.

1369. ABN Amro submitted that it could not be found to have been "involved" in S&P's contraventions unless it had actual knowledge of the essential matters going to them at the time they occurred. As we have seen, that element was established: see Part 3 above. ABN Amro knew that S&P's rating of the Rembrandt notes was misleading: see Part 3 above and J[3264].

5. CAUSATION, RELIANCE AND REMOTENESS

5.1 Introduction

1370. ABN Amro raised three causation issues on appeal.

1371. First, ABN Amro challenged the primary judge's finding that the PA Councils relied on ABN Amro's misleading conduct, in circumstances where ABN Amro contended that the mere reliance on that conduct by LGFS, rather than the PA Councils, would not be capable of establishing causation for the PA Councils (the **Indirect Causation Contention**): ABN Amro Appeal Grounds Matrix Rows 64, 65, 79, 80 and 81.

1372. Second, and in any event, ABN Amro contended that the PA Councils' failed to prove causation because they did not establish that, absent the impugned conduct, they would have adopted some course of action, other than purchasing the Rembrandt 2006-3 notes, as a result of which they would have been better off than they in fact were (the **Alternative Universe Contention**): ABN Amro Appeal Grounds Matrix Rows 82-85.

1373. Third, that the unlawfulness of the conduct of LGFS and the PA Councils in dealing with the Rembrandt 2006-3 notes was the real and effective cause of the PA Councils' losses (the **Unlawfulness Contention**).

5.2 Indirect Causation Contention

1374. The primary judge found that the PA Councils had demonstrated reliance on ABN Amro's conduct: J[3250]-J[3251]. ABN Amro submitted that there were four errors in the primary judge's conclusion that the PA Councils had demonstrated that reliance:

1. The facts did not permit the conclusion;

2. There was no proper basis for concluding that the PA Councils relied on ABN Amro's impugned conduct;

3. The finding was inconsistent with the PA Councils' decisions to invest in the Rembrandt 2006-3 notes, especially the trust and confidence the PA Councils placed in LGFS, not ABN Amro; and

4. In concluding that the PA Councils relied on ABN Amro's impugned conduct, the primary judge was influenced by an irrelevant consideration – that ABN Amro knew or that it was reasonably foreseeable that LGFS would market the Rembrandt notes to the PA Councils on the basis of the representations made by ABN to LGFS. ABN Amro submitted that this misstated the question, which was to be determined by a consideration of the PA Councils' "states of mind", not ABN Amro's.

ABN Amro's case on appeal was fundamentally that the most that could be said was that ABN Amro's conduct contributed to the PA Councils' opportunity to buy the Rembrandt 2006-3 notes, or, in other words, all the PA Councils can rely on is indirect causation. That is, ABN Amro submitted that its representations induced LGFS to buy the notes and, if LGFS had not done so, the PA Councils would never have invested in the notes. Put another way, ABN Amro, like S&P, submitted that its conduct did not cause loss and damage because the impugned conduct was not any statement made to or conduct directed at the PA Councils and it is insufficient that a third party, such as the PA Councils, rely on allegedly misleading conduct which results in loss and damage: see [797] above and *Ingot Capital Investments* at 731-732 [612]-[619].

1375. **Following paragraph cited by:**

Cahill v Kenna (10 December 2014) (McDougall J)

ABN Amro misstates the applicable legal principles and, in any event, the contentions fail on the facts. First, the legal principles. There is no bright-line principle that it is insufficient for a plaintiff to prove that some other person relied on the alleged misleading conduct and that that person's reliance led to the plaintiff suffering loss. *Ingot Capital Investments* does not stand for that proposition. *Ingot Capital Investments* is authority for the proposition that where misleading and deceptive conduct provides the opportunity for an investor to enter into a transaction, that investor will not be entitled to recover where the investor knows the truth of the underlying misrepresentation or was indifferent to its truth and proceeded nonetheless: *Ingot Capital Investments* at 661-662 [19]-[22] and 731-732 [612]-[619]; see also, *Digi-Tech (Australia) Pty Ltd v Brand* (2004) 62 IPR 184 at 212 [159] .

1376. **Following paragraph cited by:**

Wadren Pty Ltd v AIG Australia Pty Ltd (19 December 2024) (Sloss J)
TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Limited (24 October 2019) (Beach J)
Masters v Lombe (Liquidator); In the Matter of Babcock & Brown Limited (In Liq) (18 October 2019) (Foster J)

365. In *Grant-Taylor First Instance*, Perram J considered whether BBL failed to disclose important information to the market in breach of its continuous disclosure obligations under the Act . Justice Perram found that the plaintiffs failed on the question of liability for breach of the Act and, therefore, questions of causation and quantum did not arise (at 764 [211]). His Honour nonetheless dealt with those issues "relatively briefly", concluding that, had it been necessary to reach a view on the issue of causation, his Honour would have likely agreed with the plaintiffs' submissions for the reasons outlined at 765–766 [219], being:

(i) the relevant statutory questions appear in ss 1317HA (the damage resulted from the contravention) and 1325 (loss or damage because of conduct) of the Act ;

(ii) provisions of this kind import a notion of causation;

(iii) while reliance is a sufficient condition for establishing causation it is not a necessary one. Cases involving diversion of customers from one trader to another caused by misleading conduct are one obvious example of this: *Janssen-Cilag Pty Ltd v Pfizer Pty Ltd* (1992) 37 FCR 526; 109 ALR 638 per Lockhart J;

(iv) it is relevant to take into account the underlying context of the alleged infringement. Here s 674 requires disclosure of market sensitive information where it would be expected to affect price (and where the listing rules also require disclosure). The provision assumes the existence of a price effect on the market in general;

(v) a plaintiff may not recover where it knows of the misleading nature of the alleged conduct: *Ingot Capital Investments Pty Ltd v Macquarie Equity Capital Markets Ltd* (2008) 73 NSWLR 653; 252 ALR 659; 68 ACSR 595; [2008] NSWCA 206 at [19]–[22] and [612]–[619] (CA); *Digi-Tech (Aust) Pty Ltd v Brand* (2004) 62 IPR 184; [2004] NSWCA 58 at [159] (CA). But those observations by the Court of Appeal do not preclude a case brought by a council against a ratings agency where the agency had communicated information to the financial services arm of a council association about particular financial instruments and the council had then relied on what the financial services arm had said. The Full Court held that such a case could be maintained: *ABN AMRO Bank AV v Bathurst Regional Council* (2014)

224 FCR 1; 309 ALR 445; 99 ACSR 336; [2014] FCAFC 65 at [1376] (FC) (*ABN AMRO*). See also *Cahill v Kenna* [2014] NSWSC 1763 at [264]–[265] per McDougall J; *McBride v Christie's Australia Pty Ltd* [2014] NSWSC 1729 at [258]–[266] per Bergin CJ in Eq; *Caason Investments Pty Ltd v Cao* [2014] FCA 1410 at [87]–[92] per Farrell J.

(vi) *ABN AMRO* establishes that, at least in principle, where A misleads B and B in consequence misleads C, C is not necessarily precluded from recovering from A;

(vii) the facts on this case are different to those in ABN AMRO to this extent: here it is alleged A misled the market (that is many B's) which then bid up the price which then caused loss to C. This is not the same factual situation as arose in *ABN AMRO* but I do not think it relevantly differs;

(viii) while I accept that generally a plaintiff must show in a misleading conduct case that they would have acted in a particular way but for the conduct (see, for example, *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd (No 1)* (1988) 39 FCR 546 at 559; 79 ALR 83 at 96 (FC); *Metalcorp Recyclers Pty Ltd v Metal Manufactures Ltd* [2004] ATPR (Digest) 46-243 at [50] (CA)) it is artificial to speak of reliance in non-disclosure cases such as the present: *Campbell v Backoffce Investments Pty Ltd* (2009) 238 CLR 304; 257 ALR 610; 73 ACSR 1; [2009] HCA 25 at [143] .

Downer EDI Rail PL v John Holland PL (20 March 2018) (Stevenson J)

Next, the entitlement to recover loss or damage in a case of misleading and deceptive conduct is not confined to persons who relied on the conduct: *Janssen-Cilag Pty Ltd v Pfizer Pty Ltd* (1992) 37 FCR 526. Indeed, a plaintiff need not establish that the plaintiff directly received and relied upon the misrepresentation made by a defendant: see, by way of example, *Hampic Pty Ltd v Adams* (2000) ATPR 41-737. The causation inquiry required to be undertaken for the purposes of s 82(1) of the TPA (and for s 5D of the *Civil Liability Act*) entails a determination of whether the loss or damage is the "real or direct or effective cause of the applicant's loss"; "it must have been 'brought about by virtue of' the conduct which is in contravention of s 52": *Janssen-Cilag* at 530. The inquiry is whether the plaintiff suffered loss or damage by reason of, or as a result of, the contravention: *Janssen-Cilag* at 531.

1377. **Following paragraph cited by:**

Mistrina Pty Ltd v Australian Consulting Engineers Pty Ltd (24 September 2020) (Macfarlan, Ward and Leeming JJA)
Cahill v Kenna (10 December 2014) (McDougall J)

265. In view of the conclusions to which I have come, it is not necessary to delve into this debate. However, it seems to me, the following propositions should govern the inquiry as to causation:

(1) where damages are claimed for misleading or deceptive conduct, in contravention of an applicable statute, the relevant inquiry is whether the plaintiff suffered loss "by" that conduct;

(2) the inquiry must be whether the loss claimed occurred by reason of, or as a result of, that conduct - see *Janssen-Cilag Pty Ltd v Pfizer Pty Ltd* (1992) 37 FCR 526 at 531 ;

(3) thus, what the plaintiff must show is that the conduct in question was an effective or direct cause of the loss - *Janssen-Cilag* at 530;

(4) that conduct may be a direct or effective cause of the loss if it was an essential part of the chain of causal events that, ultimately, led to loss - *ABN AMRO Bank NV v Bathurst Regional Council* (2014) 309 ALR 445 at [1377] ; and

(5) focussing on reliance may divert attention from the statutory requirement: that the loss claimed be caused "by" the contravention of the relevant legislation, and there may be cases in which reliance is inappropriate as a tool for examining the question of causation: *Campbell v Backoffice Investments Pty Ltd* (2009) 238 CLR 304 at [143] (Gummow, Hayne, Heydon and Kiefel JJ).

The PA Councils are entitled to rely upon ABN Amro's conduct in disseminating and promoting the rating to LGFS as a step in the chain of causation that led to their losses. Part of that chain of causation was the PA Councils' reliance upon the AAA rating, which they would never have received had it not been provided by ABN Amro to LGFS, which would not have happened if LGFS had not relied upon the ABN Representations: see [923]ff above. Here, unlike the position in *Ingot Capital Investments*, there was no suggestion that the PA Councils actually knew that the AAA rating was not based on reasonable grounds and was not the product of the exercise of reasonable care and skill or that they were indifferent to the rating.

1378. That brings us to the facts. They have been addressed at Part 2 , Sections 6 and 7, and [813] above.

1379. In this context, it must be recalled that ABN Amro represented to LGFS that the rating could be relied upon and that the rating meant that the CPDO had an extremely strong capacity to meet its obligations (see [881]-[905] above) and that LGFS relied on those representations: see [923]ff above and J[3098]. The ABN Representations were "decisive considerations" in LGFS' decision to purchase the Rembrandt notes from ABN Amro and to sell them to the PA Councils on the basis of the AAA rating: see [919]-[933] above and J[3171]-J[3174]. The rating carried with it the S&P Representations: see [723] above. That was a decisive consideration for the PA Councils in acquiring the Rembrandt notes: see Part 2 , Sections 1 and 7 and Part 8, Section 2.2 above.

1380. The primary judge did not find that the PA Councils knew that ABN Amro made the ABN Representations. Instead, it was LGFS' reliance on those representations which, in turn, caused the PA Councils to rely on the rating. Therefore, the ABN Representations to LGFS, and LGFS' reliance upon them, were a material cause of the PA Councils' decision to invest in the Rembrandt notes: *Ingot Capital Investments* at 659-660 [12]. Consistent with the earlier principles, there did not need to be a direct inducement by ABN Amro, it was sufficient that ABN Amro's representation was material to the decision of the PA Councils to invest, in the sense that "the representation was a link in the causal chain": *Ingot Capital Investments* at 660 [13]. It was: see Part 2 , Sections 1 and 7 and Part 8, Section 2.2 above.

5.3 Alternative Universe Contention

1381. ABN Amro's contentions are rejected for the same reasons that we rejected this contention when it was advanced by S&P: see [1308] above.

5.4 Unlawfulness Contention

1382. ABN Amro adopted S&P's contentions. They fail for the reasons at Part 9, Section 2.5.5 above.

6. LOSS AND DAMAGE: ABN APPEAL GROUNDS MATRIX ROWS 86-88

1383. ABN Amro submitted that the PA Councils had failed to prove their loss because they had adopted an alternative approach to the "rule" in *Potts v Miller* . This approach was also contended for by S&P. On appeal, ABN Amro identified two findings in her Honour's reasons for concluding that the *Potts v Miller* approach did not apply which it contended were in error:

1. That spread-widening, which contributed to the cash out of the Rembrandt notes, was not a supervening or extraneous event: J[3454]-J[3458]; and

2. That as a consequence of ABN Amro's impugned conduct, the PA Councils were effectively locked in to their purchases of the notes until cash out: J[3459]-J[3462].

1384. These contentions have been addressed at [958]- [988] above and are rejected for those reasons. The considerations that were relevant, and applied, to LGFS are equally applicable to the PA Councils. By way of summary:

1. Spread-widening, which contributed to the cash out of the Rembrandt notes, was not a supervening or extraneous event because sustained spread widening was "a central" or "major" risk and "vulnerability" of the Rembrandt notes, which S&P and ABN Amro always knew about: see [974]-[977] above and J[3454];

2. Sustained spread widening, even to an exceptional but plausible extent, ought reasonably to have been at the forefront of S&P's mind when assessing the credit risk of the notes: see [976] above and J[3417] and J[3454];

3. The whole of the loss which the PA Councils suffered was the consequence of the rating being wrong, not only because the PA Councils would not have acquired the Rembrandt notes but for the AAA rating, but also because the loss was caused by sustained spread widening "which was one of the principal risks encompassed by the wrong information as to the creditworthiness of the CPDO": see [976] above and J[3457];

4. As a consequence of ABN Amro's impugned conduct, the PA Councils were effectively locked in to their purchases of the notes until cash out: see [978]-[988] above and J[3459]-J[3462];

5. The principles in *Potts v Miller* do not apply to the damages case because the PA Councils were locked in to their investment in the notes: see [978]-[988] above and J[3458]-J[3462]; and

6. The PA Councils did not suffer loss until the notes cashed out: see [971] and [978] above and J[3407].

1385. At trial and on appeal, ABN Amro submitted that LGFS' non-disclosure to the PA Councils that S&P was reviewing how it rated CPDOs and that ABN Amro would not issue more CPDOs meant that ABN Amro's conduct had no continuing effect on the PA Councils after March 2007. That submission was rejected by the primary judge (at J[3422]) and on appeal: see [980]-[988] above. Neither the PA Councils nor LGFS had any reason to suspect they were the victims of a negligent and misleading rating. As the primary judge said, "it could hardly have been clearer to LGFS that ABN Amro's position was that S&P's new ratings approach did not bear upon the rating of the existing CPDO notes at all": see [142] above and J[3422].

7. COUNCILS' FAILURE TO TAKE REASONABLE CARE AND CONTRIBUTORY NEGLIGENCE

1386. This is addressed in Part 13 below.

8. NO DEDUCTION FOR COUPONS: ABN APPEAL GROUNDS MATRIX ROW 89

1387. This issue has been considered in the context of LGFS at [989] above. It is rejected for the same reasons.

PART 11: BATHURST PURCHASE OF 2006-3 NOTES

1. ABN AMRO'S CLAIMS AGAINST BATHURST

1.1 Tort claims: ABN Amro Appeal Grounds Matrix Rows 59, 59B, 77A and 77D

1388. The primary judge found that ABN Amro owed two duties to Bathurst. The first duty was the same duty it owed to the PA Councils: see [1319] above. ABN Amro challenged the primary judge's findings on the first duty on the same bases as it did with respect to the PA Councils: see [1321] above. We reject that Appeal Ground for the reasons set out at [1326]- [1346] above. The second duty ABN Amro owed to Bathurst was identical to the Second Duty it owed to LGFS: see [803] above. ABN Amro challenged the primary judge's findings on the second duty on the same bases as it did with respect to LGFS: see [862] above. We reject that Appeal Ground for the reasons set out at [864]- [875] above.

1389. ABN Amro raised three further matters which it submitted pointed against the imposition of the Second Duty with respect to Bathurst:

1. ABN Amro had no relevant dealings or relationship of any kind with Bathurst;

2. ABN Amro did not know that LGFS intended to market and sell the Rembrandt 2006-3 notes to Bathurst specifically, and was unable to make any assessment of the sort of investment which would be appropriate for it; and

3. Bathurst was not vulnerable to any want of care on ABN Amro's part because it could have protected itself by the terms on which it contracted to buy the notes from LGFS.

1390. We reject ABN Amro's submissions that the matters raised in (1) and (3) above should negate the imposition of the second duty for the reasons set out at [614]-[616] and [829]-[830] above. In relation to (2), the facts establish that ABN Amro was aware that LGFS would on-sell any financial product it purchased to councils and it used this knowledge in its marketing of the notes to LGFS: see [60] and [1316] above. The fact that it did not know Bathurst specifically does not militate against the imposition of the second duty: see [587]-[595] above.

1391. As with the PA Councils and LGFS, the primary judge found that ABN Amro breached the two duties it owed to Bathurst. On appeal, ABN Amro challenged those findings on the same bases as it challenged the primary judge's findings in relation to the PA Councils and LGFS: see [1347] above in relation to the First Duty and [908] above in relation to the Second Duty: ABN Amro Appeal Grounds Matrix Rows 78A and 78D. For the reasons set out at [1348] and [908]-[910], we reject ABN Amro's challenge to the primary judge's finding that it breached the two duties it owed to Bathurst.

1.2 **Statutory claims:** ABN Amro Appeal Grounds Matrix Row 60B

1392. At trial, Bathurst's case against ABN Amro under ss 1041E and 1041H of the *Corporations Act* and s 12DA of the *ASIC Act* reflected LGFS' case against ABN Amro under those sections. ABN Amro challenged the primary judge's finding that it had breached those sections in relation to Bathurst for the same reasons as it did in its case against LGFS: see [911]-[915] above. We reject that challenge for the reasons [911]-[915] above.

1393. ABN Amro also contended that the primary judge erred in finding that its conduct, or negligence, in making the ABN Representations caused Bathurst loss or damage in circumstances where Bathurst had neither pleaded nor proved that it relied on the ABN Representations or was otherwise induced by them to purchase the Rembrandt 2006-3 notes. ABN Amro again deployed the same arguments in support of that contention as it did in its case against the PA Councils: see [1370]-[1373] above. We reject ABN Amro's contention for the reasons at [1374]- [1382] above.

1394. Finally, ABN Amro contended that the primary judge erred in finding that it was appropriate under s 5D of the *Civil Liability Act* that the scope of its liability for its negligence in making the ABN Representations, and in causing the Rembrandt 2006-3 notes to be issued, extend to any loss suffered by Bathurst in purchasing those notes. It relied on essentially the same argument as it did with respect to the PA Councils: see [1370]-[1373] above. We also reject this contention for the reasons at [1374]- [1382] above.

1.3 **Loss and damage:** ABN Amro Appeal Grounds Matrix Rows 82A, 84A, 86A, 87A and 88A

1395. ABN Amro challenged the primary judge's findings on loss and damage in relation to Bathurst on the same bases as it did in relation to the PA Councils: see [1383] above. We reject that challenge for the reasons at [1384]- [1385] above.

1.4 **Contributory negligence:** ABN Amro Appeal Grounds Matrix Rows 94A-94E and 95A

1396. This is addressed in Part 13 below.

2. S&P'S CLAIMS AGAINST BATHURST

2.1 **Tort claims:** S&P Appeal Grounds Matrix Rows 1-14

1397. The primary judge found that S&P owed the same duty to Bathurst as it owed to the PA Councils: see [1250] above. S&P challenged that finding on the same bases as it did in relation to the PA Councils: see [1251] above. We reject that challenge for the reasons at [1252]- [1303] above.

2.2 **Statutory claims:** S&P Appeal Grounds Matrix Rows 15-30

1398. The primary judge found that S&P contravened ss 1041E and 1041H of the *Corporations Act* and s 12DA of the *ASIC Act* in relation to Bathurst for the same reasons it had contravened those statutory provisions in relation to the PA Councils: see [1304] above. S&P challenged that finding on the same bases as it did in relation to the PA Councils: see [1305]- [1308] above. We reject that challenge for the reasons at [1305]-[1308] above.

2.3 **Causation:** S&P Appeal Grounds Matrix Rows 31-38

1399. The primary judge's findings on the issue of causation in the PA Councils' case against S&P applied equally to Bathurst's case against S&P: see [1309] above. S&P challenged those findings on the same bases as it did in relation to the PA Councils: see [1309] above. We reject that challenge for the reasons at [1309] above.

2.4 **Loss and damage:** S&P Appeal Grounds Matrix Rows 47-56

1400. S&P challenged the primary judge's findings on loss and damage in relation to Bathurst on the same bases as it did in relation to the PA Councils: see [1311] above. We reject that challenge for the reasons at [1311]- [1312] above.

2.5 **Contributory negligence:** S&P Appeal Grounds Matrix Rows 39-46

1401. This is addressed in Part 13 below.

3. LGFS' CLAIMS AGAINST BATHURST

1402. The analysis and findings made in Part 8 with respect to the PA Councils apply equally to Bathurst.

4. RESCISSION CLAIMS – SECTION 925A OF THE *CORPORATIONS ACT*

1403. Bathurst contends that the primary judge erred in dismissing its claim that, pursuant to ss 925A and 925B of the *Corporations Act* , it was entitled to a declaration that it had rescinded, by notice dated 6 May 2009 (the **Rescission Notice**), its agreement made on or about 20 December 2006 to purchase a Rembrandt 2006-3 note from LGFS (the **Bathurst Agreement**): J[3288]- [3307]. The PA Councils did not press their Appeal Grounds concerning the same issue as it related to the Rembrandt 2006-3 notes purchased by them.

1404. The reasons of the primary judge concerning this question generally refer to the Councils. Where appropriate we have done likewise. However, we have generally adopted her Honour's reasons as referable only to Bathurst, it being the only council which maintains its cross-appeal on this issue.

1405. The primary judge correctly found that the requirements of s 924A of the *Corporations Act* we re satisfied and that ss 925A and 925B were engaged: J[3289]. No issue as to this arises in the cross-appeal.

1406. Section 925A(2) provides that the "client" (Bathurst) "may only give a notice under this section within a reasonable period after becoming aware of the facts entitling the client to give the notice".

1407. Following a ratings downgrade of the Rembrandt notes, a meeting took place on 9 April 2008 (the **9 April meeting**) attended by representatives of a number of the Councils, including Bathurst, and LGFS. Thereafter, it was determined that legal advice should be obtained about potential claims by the Councils against LGFS. Bathurst first retained lawyers in April 2008. More than one year later, on 6 May 2009, on its behalf, they sent a letter to LGFS, part of which contained the Rescission Notice.

1408. The case at trial was that the Councils, including Bathurst, gave notice of rescission within 3-4 months or less of learning of the right to rescind and that such a period, for the purposes of s 925A(2) , was reasonable: J[3295]- [3296].

4.1 The trial judgment

1409. Bathurst's case, as with the other Councils, depended on the drawing of inferences about its state of awareness based on the need for legal advice for them to have become aware of the right to rescind. However, the primary judge held that awareness of the right to rescind was not the statutory question but that, upon its proper construction, s 925A(2) requires only awareness of the facts entitling the giving of the notice to rescind: J[3299] and J[3301]. Accordingly, the primary judge proceeded upon a different construction in the application of s 925A(2) .

1410. **Following paragraph cited by:**

> Woodlawn Capital Pty Ltd v Motor Vehicles Insurance Ltd (09 March 2016)
> (Macfarlan, Ward and Gleeson JJA)

The primary judge found that the facts, the awareness of which entitled Bathurst to give a written notice stating that it wished to rescind the Bathurst Agreement pursuant to s 925A(1) were as follows (at J[3299]):

1. That LGFS did not hold an AFSL covering the provision of financial services in relation to the Rembrandt 2006-3 notes;

2. That LGFS was not exempt from the requirement to hold an AFSL covering the provision of the financial service in relation to the Rembrandt 2006-3 notes;

3. The terms of LGFS' AFSL (which did not permit it to deal in derivatives); and

4. The legal character of the Rembrandt 2006-3 notes (that the notes were not a debenture and were a derivative in which LGFS had no licence to deal).

1411. It is important to understand that these “facts”, because of the construction applied by the primary judge, did not include any facts as to when Bathurst became aware of its right to give the Rescission Notice. The 9 April meeting is of some significance as there is an issue in the cross-appeal as to whether the primary judge found that it was likely that Bathurst was aware of the facts set out in the preceding paragraph by the time of that meeting and, if so, whether that finding was erroneous.

1412. Her Honour may, in her reasons, particularly at J[3305], have concluded, relevantly, that Bathurst knew the relevant facts, for the purposes of s 925A , by the time of the 9 April meeting. However, her reasons on this question might be thought to be equivocal. We do not think they are when seen in context.

1413. The apparently equivocal nature of her Honour's reasons is principally due to the different legislative constructs in play: that contended for by Bathurst and that as found by the primary judge. This difference, as we have explained, informs the relevant “facts” for the purposes of s 925A .

1414. It is necessary to understand that the primary judge was weighing up inferences that might be drawn, under the construction adopted by her Honour, in competition with those contended for by Bathurst and the other Councils under their postulated different construction. Her conclusion at J[3304] was that there were other equally, if not more, persuasive inferences available on the *whole* of the evidence *including* the evidence of the 9 April meeting. She then posited that it was equally, if not more, likely that Bathurst, relevantly, knew of the facts, on her construction, entitling it to give the Rescission Notice, even if it did not know of the entitlement to give the Rescission Notice itself, by the time of the 9 April meeting: J[3304]-J[3305].

1415. Her Honour continued in this provisional manner at J[3306], that “[i]f the [C]ouncils became aware of the facts entitling them to give the notice by 9 April 2008 (as may well be the case) then the giving of notice a total of 11 months later (at best) … is not a reasonable period". This observation proceeded from her Honour's consideration of what inferences were capable of being drawn because there was no relevant direct evidence.

1416. At trial, Bathurst did not lead any direct evidence, on its case and under its construction, as to when and how it became aware of the facts entitling it to give the Rescission Notice. In particular, it led no direct evidence as to what, if anything, it had learned from its own research, or had been advised by experts or lawyers, bearing on this issue. Bathurst put on an affidavit which identified the dates on which solicitors, and then counsel and an expert, had been retained, but nothing which went directly to the awareness requirement found in s 925A . This evidence, such as it was, was all directed to the construction formulated by Bathurst.

1417. Bathurst asked the Court to infer that it had only received advice to seek rescission shortly before the Rescission Notice was sent.

1418. Importantly, her Honour found at J[3306] that she was not satisfied as to the date on which, relevantly, Bathurst became aware of the facts entitling it to give the Rescission Notice under s 925A under the construction adopted by her. It followed necessarily from this finding that, as the primary judge stated at J[3306], it was not possible to be satisfied that, relevantly, Bathurst had given the Rescission Notice within a reasonable period after becoming so aware.

4.2 The appeal

1419. Significantly for this appeal, as we have mentioned, the primary judge found that Bathurst had not discharged its onus to prove when it became aware of the relevant facts (J[3304]-[3306]) and accordingly that it was not possible to be satisfied that the Rescission Notice was given within a reasonable period after Bathurst became so aware, which is the statutory requirement under s 925A(2) for the giving of a notice. Bathurst accepts, on appeal, that it did carry such an onus at trial. Three questions arise on appeal. The first concerns the proper construction of s 925A(2) .

1420. This, in part, will inform the answer to the second question. The second, which is in two parts, is whether the primary judge erred in finding that Bathurst failed to discharge its onus as to when it became relevantly aware and, if so, when was it that her Honour should have found it was so aware? The third, assuming such error and that the evidence was capable of establishing when Bathurst became relevantly aware, is whether the Rescission Notice was sent within a reasonable period after that time.

1421. If the construction of the primary judge is correct and her Honour was also correct in finding that Bathurst had not discharged its onus, as described, then that will be sufficient to dismiss Bathurst's cross-appeal.

4.3 Consideration

1422. In our opinion, the construction given to s 925A(2) by the primary judge was correct. The conditioning facts before a notice may be given pursuant to the provision are twofold. First, when did the client become aware of the facts entitling it to give a notice. This says nothing about awareness of any right to rescind, that is an awareness of the meaning and effect ss 924A and 925A of the *Corporations Act* as applicable to the relevant facts. It is merely the client's awareness of "the facts" giving rise to such an entitlement which is required. The facts are those, proof of which, in combination, are capable of establishing the matters set out in s 924A (1) . The second condition is that the notice be given within a "reasonable period" after the client became relevantly aware.

1423. The "facts", in this case, are those identified by the primary judge at J[3299] which we have set out at [1410] above and indeed which, as we will explain, were, in substance, identified also by Bathurst in its Rescission Notice.

1424. This construction reflects the plain and ordinary meaning of the language in s 925A(2) . The provision does not contemplate, expressly or by necessary implication, that the client should be aware of its entitlement to give the notice. Such, had the legislature intended, could have been stated, in which case the words "the facts" would have been unnecessary. All that would have been required were words, for example, as to the client becoming aware of the client's entitlement to give the notice.

1425. Cases such as *Ellison v Lutre Pty Ltd* (1999) 88 FCR 116 concerning the loss of a contractual right to rescind by conduct including delay giving rise to an inferred election to affirm a contract are of no assistance to the statutory requirements in the present case. Section 925A it seems, although it is unnecessary to decide, is a codification of the right to rescission of such agreements. For example, s 925A(3) provides for a statutory bar to rescission in this context, in the event of relevant affirmation. The statutory right to rescission is unequivocal: it requires the client "becoming aware of the facts entitling the client to give the notice". Of course, all of the relevant circumstances will need to be considered in each particular case.

1426. Bathurst submitted that the relevant "facts" for the purposes of s 925A are complex constructs of the legal system that reference complex constructs developed in the world of commerce and investment. That this was so was illustrated at length in Bathurst's written submissions. Such facts, it contends, are far removed from the sort of "facts" about which the referenced clients could be ordinarily expected to make reliable judgments without considerable and highly technical expert assistance and analysis. We do not accept this submission as apt. Matters of complexity in relation to a particular agreement are no doubt a factor in the length of time it might take for a client to become relevantly aware. However, that is not the statutory inquiry under s 925A which is directed implicitly, as a starting point, to when it was that the client first became aware of all the relevant facts which, as we have explained, are those, proof of which is necessary to establish the matters set out under s 924A . The length of the journey, and the reasons contributing to that length, before the client reaches the relevant state of awareness do not touch on the initial question which focusses on the journey's end. It is a simple question of fact capable, ordinarily, of direct proof: when did the client become aware of the relevant facts? The question then is whether the notice was given within a reasonable period from that time.

1427. Bathurst also challenges the findings of the primary judge at J[3303] that at the 9 April meeting, the issues discussed included whether the Rembrandt notes, of which the Rembrandt 2006-3 note was one, were a "credit derivative", as well as LGFS' lack of capacity to deal in derivatives.

1428. We have concluded that the evidence, on the balance of probabilities, fell short of establishing these facts and, to that extent, the primary judge was in error. It is unnecessary to descend into the detail of why that is so because the error is immaterial to the disposition of the cross-appeal.

1429. The crucial findings by the primary judge at J[3306], which proceeded from her Honour's construction of s 925A(2) , are that her Honour was not satisfied as to when it was that, relevantly, Bathurst became aware of the facts entitling it to give notice under s 925A(1) and therefore that it was not possible for her Honour to be satisfied that Bathurst gave notice within a reasonable period after becoming so aware. Consideration of the second requirement necessarily demands proof of the former.

1430. Bathurst submits that the only sensible inference open to be drawn on the uncontroversial evidence adduced by it is that it did not become relevantly aware until after counsel was briefed and an expert was retained "to assist the lawyers in understanding various technical aspects of the documents and the nature of the referenced financial products on which the performance of the notes apparently depended". Bathurst submits that this proceeds from the unchallenged evidence from its employee Mr Robert Roach, Bathurst's Director of Corporate Services and Finance, as to what occurred between December 2008 and March 2009.

1431. It must, however, be understood that this submission, as at the trial, proceeds upon an incorrect construction of s 925A(2) and is directed to a different set of relevant facts, in part, to those identified correctly by the primary judge. Nonetheless, we will consider the evidence relied upon by Bathurst which it contended, by inferential reasoning, was capable of establishing that it became aware of its right to give the Rescission Notice only after it received legal advice and that this occurred shortly before it gave the Rescission Notice.

1432. Mr Roach deposed that Mr Campion, Bathurst's representative at the 9 April meeting, told him that "the meeting had no outcomes". Mr Roach said that, in his view, there was a need for Bathurst to obtain legal advice in relation to the investments made and that he did so on its behalf within 7 days of the 9 April meeting. He then deposed to what occurred thereafter, including correspondence between Bathurst's solicitors and ASIC, the retention of counsel, his attendance at conferences with the solicitors and counsel and the retention of an expert to assist the lawyers in understanding various technical aspects of the documents and the nature of the referenced financial products. He concluded by stating that he reviewed and authorised service of the Rescission Notice to LGFS shortly after 29 April 2009.

1433. The Rescission Notice was not a stand-alone document. It forms part of a letter from Bathurst's solicitors to LGFS dated 6 May 2009. The main part of the letter sets out allegations as against LGFS that Bathurst had been the subject of a series of misrepresentations concerning the Rembrandt 2006-3 note. These, in part, referred to misrepresentations by S&P.

1434. However, these allegations, which are found on the first 9 pages of the letter, did not directly go to the grounds under s 924A(1) upon which a notice may be given under s 925A(1) . Those were dealt with on pages 9-11 of the letter under the heading "Statutory Rescission – Corporations Act Section 925A ". This part of the letter constituted the Rescission Notice.

1435. The Rescission Notice confined itself, appropriately, to the following assertions:

1. Such authorisation as LGFS had could only depend upon cl (b)(i) of Australian Financial Services Licence No 245642 effective 5 November 2004.

2. The Rembrandt 2006-3 note could not be characterised as a "debenture" as defined in s 9 of the *Corporations Act* .

3. The Rembrandt 2006-3 note was, if relevant, not a "security" within the meaning of the *Corporations Act* and in particular s 761A .

4. The Rembrandt 2006-3 note was a "derivative" for the purposes of Chapter 7 of the *Corporations Act* : s 761D.

5. In these premises, LGFS was not authorised under its licence to deal in the Rembrandt 2006-3 note.

1436. The assertions relied upon did not depend on the alleged misrepresentations, to which we have referred, although it may be accepted that there is, to an extent, some factual overlap. They broadly coincide with the facts identified by the primary judge to which we have already referred as being those, the awareness of which entitled Bathurst to give a notice of rescission: J[3299]. The Rescission Notice then asserted that, taking the above matters together, the requirements of s 924A were met and were a warrant for the notice of rescission.

1437. Just when it was that Bathurst knew these confined facts, relevant to s 924A(1) , giving it warrant to give a notice under s 925A(1) , is not capable of being established on the evidence. It may have been shortly after Bathurst engaged its lawyers in April 2008. It may not have been then. However, it should not have been left to inference, nor could it have been, when there were other, at least equally competing inferences which would not assist Bathurst. As her Honour correctly stated at J[3300], it was, relevantly, for Bathurst to adduce sufficient evidence to enable a finding to be made by way of properly drawn inference about the date upon which it became aware of the relevant facts and that LGFS could not know or advance relevant evidence about Bathurst's state of awareness. Neither Mr Roach nor any witness, on behalf of Bathurst, gave evidence of when Bathurst became aware of the facts entitling it to give the Rescission Notice, even on Bathurst's construct of s 925A(2) . That no such direct evidence was called to demonstrate the actual position no doubt gave the primary judge comfort in concluding, as she did, that the evidentiary burden on Bathurst had not been discharged. Such a consideration is evident from her Honour's observations at J[3303] as to her concern about the chain of inference sought to be invoked by the Councils when it was always in their power to have adduced direct evidence of their awareness.

1438. This result follows even if the construction of s 925A contended for by Bathurst was adopted. There was no direct evidence as to when it was that Bathurst became aware of its entitlement to give the Rescission Notice. As the primary judge observed at J[3302], proof of the relevant state of awareness, on Bathurst's case, depended on a series of inferences that it would have reached this state of awareness only on receipt of legal advice and not otherwise.

1439. As the primary judge correctly observed at J[3302], there was no reason not to expect the adducing of direct evidence from a relevant officer or officers about when Bathurst first became aware of the facts entitling it to give the Rescission Notice or, for that matter, the facts it relied upon under its construction of s 925A(2) . It was entirely reasonable for her Honour to conclude that the inferences sought by Bathurst, on its construction, collapsed into mere suspicion: J[3302]. Other at least equally compelling inferences were available. Bathurst, it might be open to infer, had the relevant awareness early on after first taking legal advice but, for any number of reasons, did not act on it by giving a notice. For example, it may have deferred giving the Rescission Notice, despite having relevant awareness of the facts until after it had advice on the raft of other issues which form the major part of the letter of 6 May 2009. Such matters, which are directed to the express statutory question should not, where direct evidence is available, as usually it will be in such cases, be left to inference. No error by her Honour in this respect has been established. The cross-appellant had an onus which it failed to discharge.

1440. The primary judge, as we have mentioned, did not base her conclusion on the construction under s 925A(2) proposed by Bathurst. However, given her Honour's conclusions to which we have referred in the previous paragraph, even if she had adopted this construction, it is apparent that she would not have drawn the inferences contended for by Bathurst, and which would have been necessary to make out its case.

1441. There is one remaining matter to consider. At trial, the issue around s 925A , framed by Bathurst, and as the primary judge observed, concerned when it was that it became aware of its legal right to rescind under s 925A . Bathurst submitted that at trial its representative at the 9 April meeting was not cross-examined as to any awareness of the "section 925A facts" as a result of his attending that meeting. Nor, it was said, was any similarly focussed cross-examination conducted in relation to Mr Roach. It says that at no time during the case did LGFS suggest that Bathurst had become aware of facts entitling the client to give notice at any time prior to solicitors being retained.

1442. These submissions are misconceived, proceeding as they do on a wrong construction of s 925 A(2) and further on the assumption that it was for LGFS to both raise and prove the facts as to Bathurst's relevant awareness, even on Bathurst's case. It carried no such burden as Bathurst concedes. It is no error on the part of the primary judge that she determined the issue upon a proper construction of s 925A where that was at odds with the incorrect construction framed by Bathurst in the prosecution of its claim.

1443. The primary judge correctly identified that awareness of the right to rescind is not the statutory question but rather s 925A requires only awareness of the facts entitling the giving of the notice to rescind: J[3299].

1444. It is unnecessary, in light of our conclusions to consider what remedial orders might have been made under s 925D(1) had the cross-appeal been successful.

1445. The cross-appeal is dismissed.

PART 12: CROSS CLAIMS

1. ABN AMRO CLAIM AGAINST S&P

1446. At trial, ABN Amro cross claimed against S&P in the Corowa and Bathurst Proceedings alleging that any liability ABN Amro was found to have to the PA Councils, Bathurst and/or LGFS was caused by its reliance on S&P's misleading conduct and/or negligence in assigning a rating of AAA to the Rembrandt notes.

1447. The primary judge dismissed ABN Amro's cross-claims against S&P: J[3471]-J[3482]. The reason for dismissing ABN Amro's cross-claims was that ABN Amro knew or ought to have known that S&P's rating was misleading, and so did not rely on it "in any way capable of founding liability on S&P's part to [ABN Amro]": J[3481]. Moreover, notwithstanding this knowledge, ABN Amro chose to deploy the rating. As the primary judge stated, ABN Amro's cross claims failed "for lack of reliance and thus lack of any causal connection between S&P's conduct and any loss of ABN Amro by reason of [the] proceedings": J[3481]. ABN Amro appealed against the dismissal of its cross-claims: ABN Amro Appeal Grounds Matrix Rows 99-103.

1448. ABN Amro submitted that there were two flaws in the reasoning of the primary judge. First, that ABN Amro did not know, nor ought it to have known, that S&P's rating of the notes was misleading. That contention is wrong: see Part 3 above. ABN Amro knew, or ought to have known, that S&P's rating was misleading. As the primary judge stated, ABN Amro "knew all S&P did and more": J[3523].

1449. Second, ABN Amro submitted that if it did not know, but ought to have known, that S&P's rating was misleading, that would only have warranted a reduction in S&P's liability to ABN Amro for ABN Amro's contributory negligence, not S&P's liability. In other words, ABN Amro submitted that if ABN Amro did *not* have actual knowledge, it was still capable of relying on S&P's conduct.

1450. That contention is rejected. ABN Amro did have actual knowledge that S&P's rating was misleading and, further, having regard to ABN Amro's knowledge, the primary judge correctly concluded that it could *not* have relied on the rating: see Part 3 above. Put simply, S&P's conduct did not *cause* any loss or damage suffered by ABN Amro.

1451. It was common ground that ABN Amro's claims against S&P were premised on indirect causation. S&P submitted that its conduct did not cause loss and damage because the impugned conduct was not any statement made to or conduct directed at ABN Amro and it is insufficient that a third party, such as ABN Amro, rely on allegedly misleading conduct which results in loss and damage: *Ingot Capital Investments* at 731-732 [612]-[619]; see also J[2877]-J[2881] and J[2920].

1452. ABN Amro accepted that it must demonstrate reliance on S&P's conduct. The question was whether ABN Amro relied on S&P's conduct. The fact that it knew that the rating was misleading necessarily means that it did not (and could not) rely on S&P. ABN Amro knew the truth and was not misled. These Appeal Grounds are dismissed.

2. S&P CLAIM AGAINST ABN AMRO

1453. At trial, S&P cross-claimed against ABN Amro in the Corowa and Bathurst Proceedings for contribution, alleging that ABN Amro had engaged in misleading or deceptive conduct against it by representing to LGFS, the PA Councils and Bathurst that the Rembrandt notes were:

1. The product of the exercise of due care and skill;

2. Suitable for investment by LGFS and councils in New South Wales; and

3. Fit for the purpose for which they were supplied, that is, to be purchased by LGFS and on-sold to councils in New South Wales.

S&P also said that in publishing S&P's rating of the Rembrandt notes, ABN Amro represented to LGFS that the rating could be relied on as investment, financial or other advice and that that representation was misleading or deceptive by reason of the various disclaimers and qualifications employed by S&P.

1454. The primary judge dismissed S&P's cross-claims against ABN Amro: J[3471]-J[3475], J [3480] and J[3482]. The reason for dismissing S&P's cross-claims was that S&P knew or ought to have known of the misleading and deceptive nature of S&P's representations about the AAA rating (i.e., the S&P Representations). Despite its knowledge, it authorised ABN Amro to deploy the misleading and deceptive rating in its dealing with investors. S&P knew ABN Amro was intending to make representations about the meaning of the rating in the Surf Presentation (that presentation having been provided to S&P). S&P's knowledge about the misleading and deceptive nature of its rating meant that it knew that the Surf Presentation was itself misleading in respect of all matters in connection with the rating. The primary judge found that, in these circumstances, S&P could "hardly complain about ABN Amro's deployment of the AAA rating and information based on that rating (such as the 0.728% rating quantile or default probability)": J[3482].

1455. S&P submitted that the primary judge erred given the nature of her findings in relation to ABN Amro's conduct: S&P Appeal Grounds Matrix Row 58E. It also relied on the same matters as it did at trial. Further, it submitted that ABN Amro owed a duty of care to exercise care and skill in relation to the notes, which included a duty to supply potential purchasers with information that was accurate and sufficient to allow them to determine whether or not to purchase the Rembrandt notes.

1456. These contentions are rejected. The primary judge's findings about the nature of ABN Amro's misleading and deceptive conduct in relation to LGFS, the PA Councils and Bathurst support, rather than undermine, her finding that S&P knew or ought to have known that ABN Amro was going to engage in that conduct. S&P's reliance on the arguments it advanced at trial is also of little assistance as they do not demonstrate any error in her Honour's findings. Finally, whatever may be said about whether ABN Amro had a "duty to supply potential purchasers with information that was accurate and sufficient to allow them to determine whether or not to purchase the Rembrandt notes", S&P's reliance on that duty to support its cross-claims is untenable in circumstances where it allowed ABN Amro to deploy the rating without limitation and without requiring ABN Amro to provide particular information to investors.

PART 13: CONTRIBUTORY NEGLIGENCE, APPORTIONMENT, PREJUDGMENT INTEREST AND COSTS

1. CONTRIBUTORY NEGLIGENCE]

1.1 Introduction

1457. There were two allegations of contributory negligence – against LGFS and against the Councils. S&P and ABN Amro contended at trial that LGFS failed to take reasonable care of its own interests or was guilty of contributory negligence. The primary judge rejected that contention: J[3354]-J[3360], especially at J[3356]. In relation to the Councils, S&P, ABN Amro and LGFS contended that the Councils failed to take reasonable care of their own interests or were guilty of contributory negligence. The primary judge rejected that contention: J[3344]-J[3350]. These findings were challenged on appeal. It will be necessary to deal with each set of claims in turn.

1.2 Rembrandt 2006-3 – LGFS contributorily negligent?: ABN Amro Appeal Grounds Matrix Rows 94M-Q and S&P Appeal Grounds Matrix Rows 40A-40B and 46C-46D

1458. This section will address the statutory framework and then the relevant Appeal Grounds.

1.2.1 Statutory framework

1459. ABN Amro and S&P's contributory negligence defences are statutory: s 9 of the *Law Reform (Miscellaneous Provisions) Act 1965* (NSW) (the **1965 Act**) read with s 5R of the *Civil Liability Act* , s 1041I(1B) of the *Corporations Act* and s 12GF(1B) of the *ASIC Act* . That statement requires further explanation.

1460. First, the relevant provisions of the *Civil Liability Act* . By s 5A(1) of the *Civil Liability Act* , Part 1A of that Act "applies to any claim for damages for harm resulting from negligence, regardless of whether the claim is brought in tort, in contract, under statute or otherwise".

1461. Section 5R deals with contributory negligence:

> (1) The principles that are applicable in determining whether a person has been negligent also apply in determining whether the person who suffered harm has been contributorily negligent in failing to take precautions against the risk of that harm.
>
> (2) For that purpose:
>
> > (a) the standard of care required of the person who suffered harm is that of a reasonable person in the position of that person, and
> >
> > (b) the matter is to be determined on the basis of what that person knew or ought to have known at the time.

1462. Section 5S provides that "[i]n determining the extent of a reduction in damages by reason of contributory negligence, a court may determine a reduction of 100% if the court thinks it just and equitable to do so, with the result that the claim for damages is defeated".

1463. Part 4 of the *Civil Liability Act* concerns proportionate liability. Part 4 includes s 34, which provides as follows:

> (1) This Part applies to the following claims (***apportionable claims***):

(a) a claim for economic loss or damage to property in an action for damages (whether in contract, tort or otherwise) arising from a failure to take reasonable care, but not including any claim arising out of personal injury,

(b) a claim for economic loss or damage to property in an action for damages under the *Fair Trading Act 1987* for a contravention of section 42 of that Act (as in force before its repeal by the *Fair Trading Amendment (Australian Consumer Law) Act 2010*) or under the *Australian Consumer Law (NSW)* for a contravention of section 18 of that Law.

(1A) For the purposes of this Part, there is a single apportionable claim in proceedings in respect of the same loss or damage even if the claim for the loss or damage is based on more than one cause of action (whether or not of the same or a different kind).

(2) In this Part, a ***concurrent wrongdoer*** , in relation to a claim, is a person who is one of two or more persons whose acts or omissions (or act or omission) caused, independently of each other or jointly, the damage or loss that is the subject of the claim.

…

1464. Section 35 provides:

(1) In any proceedings involving an apportionable claim:

(a) the liability of a defendant who is a concurrent wrongdoer in relation to that claim is limited to an amount reflecting that proportion of the damage or loss claimed that the court considers just having regard to the extent of the defendant’s responsibility for the damage or loss, and

(b) the court may give judgment against the defendant for not more than that amount.

(2) If the proceedings involve both an apportionable claim and a claim that is not an apportionable claim:

(a) liability for the apportionable claim is to be determined in accordance with the provisions of this Part, and

(b) liability for the other claim is to be determined in accordance with the legal rules, if any, that (apart from this Part) are relevant.

(3) In apportioning responsibility between defendants in the proceedings:

(a) the court is to exclude that proportion of the damage or loss in relation to which the plaintiff is contributorily negligent under any relevant law, and

(b) the court may have regard to the comparative responsibility of any concurrent wrongdoer who is not a party to the proceedings.

(4) This section applies in proceedings involving an apportionable claim whether or not all concurrent wrongdoers are parties to the proceedings.

(5) A reference in this Part to a defendant in proceedings includes any person joined as a defendant or other party in the proceedings (except as a plaintiff) whether joined under this Part, under rules of court or otherwise.

1465. Section 9 of the 1965 Act provides:

(1) If a person (the ***claimant***) suffers damage as the result partly of the claimant's failure to take reasonable care (***contributory negligence***) and partly of the wrong of any other person:

(a) a claim in respect of the damage is not defeated by reason of the contributory negligence of the claimant, and

(b) the damages recoverable in respect of the wrong are to be reduced to such extent as the court thinks just and equitable having regard to the claimant's share in the responsibility for the damage.

(2) Subsection (1) does not operate to defeat any defence arising under a contract.

(3) If any contract or enactment providing for the limitation of liability is applicable to the claim, the amount of damages recoverable by the claimant by virtue of subsection (1) is not to exceed the maximum limit so applicable.

Section 9 of the 1965 Act applies to claims in tort and in contract insofar as the contractual duty was concurrent and co-extensive with the tortious duty: s 8 of the 1965 Act.

1466. The statutory test has been described as "whether a reasonable person in the position of [LGFS], i.e., having the knowledge which [LGFS] had or ought to have had, was negligent": *Origin Energy LPG Ltd v Bestcare Foods Ltd* [2012] NSWCA 407 at [217] .

1.2.2 Appeal Grounds

1467. ABN Amro and S&P contended that the primary judge's finding that LGFS was not contributorily negligent was erroneous because the primary judge adopted an overly narrow focus by limiting her analysis to the question whether LGFS was contributorily negligent in its purchase of the Rembrandt notes (as opposed to its sale of those notes to the Councils. In particular, ABN Amro and S&P contended that the primary judge failed to have any, or any reasonable, regard to the following facts:

1. LGFS purchased the notes for the purposes of on-selling them to the Councils; and

2. LGFS ought to have known that the notes were not suitable for that purpose particularly because they were derivatives, the on-selling of which was in breach of its AFSLs (and thus the *Corporations Act*) and because of the notes' complexity and volatility.

1468. The matters identified in (2) above reflect, more broadly, ABN Amro's and S&P's complaint that LGFS should have been found to have been contributorily negligent because, in marketing and selling the notes, LGFS had contravened its AFSL and the *Corporations Act* , b reached its fiduciary duties to the Councils, engaged in misleading conduct and failed to disclose risks to the Councils which had been disclosed to LGFS. They will be dealt with under the broader argument as to the suitability of the notes. Each of the facts listed above and identified by ABN Amro and S&P will be addressed in turn.

1.2.2.1 Purchased notes for on-sale to councils

1469. ABN Amro and S&P referred to, and placed considerable reliance upon, the primary judge's finding that LGFS purchased the notes for on-sale to local councils: J[1290], J[1292], J [2166], J[2315], J[2486] and J[3243]. Although acknowledging that LGFS was prepared to hold the notes it was unable to on-sell, they contended that that was not the purpose for which the notes were acquired. Instead, LGFS' objective was to on-sell *all* of the notes to councils and to be left holding as few as possible.

1470. **Following paragraph cited by:**

Touch for Health Pty Ltd as Trustee for Knight Superannuation Fund v Property Mentors Australia Pty Ltd (No 3) (02 December 2024) (Neskovcin J)

The error in ABN Amro's and S&P's submissions stems from their failure to refer to all of the relevant findings on this issue. The findings relied upon by ABN Amro and S&P (and summarised in [1469] above) were incomplete. For example, LGFS knew that it may not sell all the notes and in relation to those that it did not sell, the evidence was that it intended to keep them: J[1182], J[2486] and J[3359]. Next, LGFS' carelessness in selling the notes did not increase the number of LGFS Retained Notes. The negligence in selling was not causally significant to the losses suffered on the LGFS Retained Notes. The statutory bases for reducing LGFS' entitlement to damages are limited to an "amount reflecting that proportion of the damage or loss claimed" and to an "extent as the court thinks just and equitable having regard to the claimant's share in the responsibility for the damage". The "damage" here was the damage caused by S&P and ABN Amro to LGFS in LGFS' purchase of the Rembrandt notes. LGFS was not careless in making the decision to buy the Rembrandt notes. Other findings were important. They included that: (1) LGFS undertook a due diligence of the notes, a finding not challenged: J[3357] and [72]-[82] above; (2) LGFS was under no obligation to, and had no ability to, effectively "double guess" the rating: J[3356]; and (3) LGFS did not exhibit any lack of care in buying the notes, only in selling the notes: J [3358]. The primary judge correctly identified the inquiry she was required to undertake.

1.2.2.2 The notes were not suitable for on-selling

1471. The premises which underpin these contentions have been addressed earlier: see Part 2 , Sections 6 and 7 (which set out the facts pertinent to the sale of the notes to LGFS and to the Councils) and Parts 4-6 (LGFS' claims against S&P and ABN Amro).

1472. Each of the matters identified by S&P and ABN Amro was not causative of LGFS' loss (or the Councils' loss). Each of the matters is addressed as follows:

1. The notes were derivatives: see Part 4 , Section 1.1.4.4 above;

2. The on-selling of the notes was in breach of LGFS' AFSLs (and thus the *Corporations Act*): see Part 4 , Section 1.1.4.4 above;

3. The notes' complexity and volatility: see Part 3 above.

None of these matters was causally significant to the losses suffered on the Rembrandt notes.

1.2.3 Conclusion

1473. The primary judge was correct to find that LGFS was not guilty of contributory negligence in connection with its losses. These Appeal Grounds are dismissed.

1.3 Rembrandt 2006-2 – LGFS contributorily negligent?: ABN Amro Appeal Grounds Matrix Rows 94F-94K and S&P Appeal Grounds Matrix Rows 40B and 46B

1.3.1 Appeal Grounds

1474. ABN Amro and S&P submitted on appeal that the primary judge erred in failing to find that in purchasing the Rembrandt 2006-2 notes on behalf of StateCover (see Part 7 above), LGFS had not taken reasonable care of its own interests or had been contributorily negligent in circumstances where:

1. LGFS purchased the notes on behalf of StateCover in contravention of the terms of its AFSL and the *Corporations Act* ;

2. StateCover was not permitted to invest in the notes under its investment policy with which LGFS was intimately familiar; and

3. Purchase of the notes on behalf of StateCover was brought about by LGFS' misrepresentations, by LGFS' failure to disclose to StateCover risks in relation to the notes which had been disclosed to LGFS and by LGFS' breaches of its duty to provide investment management services to StateCover with due care and skill.

1.3.2 Analysis

1475. These contentions fail. The submissions assume that LGFS was liable to StateCover for all of the reasons alleged by StateCover in its pleading. Although the primary judge considered that LGFS would have difficulty in defending the StateCover claim, liability was not established by the evidence, or by the settlement.

1476. Next, LGFS accepts that the Rembrandt 2006-2 notes were not suitable for StateCover. That lack of suitability arose for a *number* of reasons. One (but not the only) important reason (and as with the Councils the reason directly connected to loss) was that the risk of loss was much greater than that of a genuine AAA rated instrument. That is, each of ABN Amro, S&P and LGFS were responsible for the loss, and ABN Amro's and S&P's wrong was directly causally connected to the loss. Finally, as with the Councils' claims, the rating directly influenced Mr Hilder's beliefs and conduct which resulted in LGFS' negligent act in causing StateCover to purchase the notes: see Part 2 , Section 6 above.

1477. ABN Amro contends that it is much less at fault than S&P. As Part 3 above has demonstrated, that contention fails on the facts. Each has a considerable degree of responsibility for LGFS' loss and those responsibilities are interrelated. LGFS was not contributorily negligent and there is no basis for adjusting the apportionment imposed by the primary judge.

1.4 Councils contributorily negligent?: ABN Amro Appeal Grounds Matrix Rows 90, 91, 92, 93, 94, 94A-94E; LGFS Appeal Grounds Matrix Rows 110-111 and S&P Appeal Grounds Matrix Rows 39-40 and 41-46

1.4.1 ***Introduction***

1478. At trial, each of ABN Amro, S&P and LGFS submitted that the Councils had been guilty of contributory negligence in purchasing the Rembrandt 2006-3 notes. The primary judge rejected those submissions: J[3344]-J[3350] and J[1407]-J[1474].

1479. The primary judge found that the Councils had not failed to take reasonable care of their own interests in deciding to invest in the Rembrandt 2006-3 notes and that the relevant statutory provisions for reducing the Councils' entitlement to damages were not engaged because there was no failure to take reasonable care or contributory negligence by the Councils: see J[3345] and J[3350].

1480. **Following paragraph cited by:**

Stav Investments Pty Ltd v Taylor (09 March 2022) (Ward CJ in Eq)

The primary judge's findings included that:

1. "A prudent person will ordinarily have available the defence that 'they had selected a reasonably careful person and acted upon the skilled advice that they had received upon such a question': *Learoyd v Whiteley* (1887) 12 AC 727 at 730-1)": see also *NMFM Property* at 380-381 [494] and J[3347]- [3348].

2. The S&P Reports did not identify the key risks of the product or explain its structure, other than explaining cash in and cash out in an obscure way: see [49]-[50] and [1176]-[1177] above and J[1320], J[1340]-J[1345], J[1377(5)], J[1387] and J[3345(8)].

3. The LGFS Community Income Notes Brochure "was a wholly one sided description of the potential benefits of investing in a product said to have been arranged by LGFS without any accompanying disclosure of the potential risks which LGFS itself knew about": J[1637].

4. The Councils were entitled to accept "LGFS's words and deeds at face value" and in those circumstances the Councils could never have formulated the relevant questions to ask LGFS in order to obtain relevant information: J[1639].

1481. Each of ABN Amro, S&P and LGFS has appealed. It is necessary to address each "error" relied upon by one or more of ABN Amro, S&P and LGFS in support of the contention that the Councils failed to take reasonable care and did not act prudently in deciding to invest in the Rembrandt 2006-3 notes. There are seven.

1.4.2 *Standard by which Councils' conduct to be assessed: S&P Appeal Grounds Matrix Rows 39 and 41*

1482. S&P submitted that the primary judge erred in finding that the standard by which the Councils' conduct should be judged was that of an ordinary reasonable investor, rather than that of the prudent, wise cautious and judicious investor (S&P Appeal Ground Matrix Row 39): J[1409]-J[1474], J[2483]-J[2484] and J[3344]-J[3350]. S&P further submitted that the primary judge erred in finding that the Councils' concession that they were required to read the documents provided to them was not relevant and argued that this issue raised "fundamental policy concerns in relation to the extent to which guardians of public money are required to take appropriate steps when investing that money on behalf of public authorities": S&P Appeal Grounds Matrix Row 41.

1483. These Appeal Grounds fail. They misstate the primary judge's finding and at least one of the bases on which the trial was conducted. The primary judge concluded that the standard of care applicable was that of an ordinary reasonable investor. Her Honour, however, went further. The primary judge also found that if her Honour was incorrect about the applicable standard, the Councils had in any event acted as a prudent person would: see J[2467]-J[2484] and J[3345]-J[3350]. That conclusion is reinforced by the fact that, at trial, the Councils accepted that what were described as the "Legislative Boundaries" imposed an obligation on them to act as a prudent person would and that they had complied with that standard. That was referred to and accepted by the primary judge: see J[1447]-J[1448], J[2483]-J[2484] and J[3345]-J[3348]. Further, we do not accept that the context of this proceeding raises any "fundamental policy concerns" of the type identified by S&P. The Councils could not replicate or "second-guess" the rating: see [1211] above. Their reliance on the rating, and the advice of their advisors, was entirely proper.

1.4.3 *Councils' reliance on LGFS: S&P Appeal Grounds Matrix Row 46 and ABN Amro Appeal Grounds Matrix Rows 90-91*

1484. The primary judge found that the Councils were entitled to rely on the advice of LGFS in relation to, and S&P's rating of, the Rembrandt notes: J[3346]-J[3348], J[3350], J[2467]-J [2484], J[1422] and J[1451].

1485. S&P contended that the primary judge failed to have sufficient regard to the "evidence of standard industry" that the Councils were required to personally understand the products in which they invested and were not entitled to rely on LGFS to identify the risks and the appropriateness of the investment for each Council. That submission is rejected. ABN Amro submitted that the Councils should have been found to have failed to exercise reasonable care even though they had a financial adviser. It argued that the primary judge appeared to have assumed that a plaintiff cannot be guilty of contributory negligence where a professional has breached its duty to the plaintiff (citing *Astley v Austrust Ltd* (1999) 197 CLR 1). That submission is also rejected.

1486. These submissions fail on the facts and are inconsistent with the law. The contention that the Councils had failed to make reasonable efforts to understand the risks of the Rembrandt notes before investing was contrary to the following findings:

1. The Councils could never have done anything which would have enabled them to discover that LGFS had failed to disclose all the risks of the notes to them, nor that S&P's credit rating was not based on reasonable grounds: see Part 3 and [1125]-[1128] above;

2. The Councils relied on LGFS, their trusted financial adviser and confidant, to identify risks and assess the appropriateness of the investment for each of the Councils: see Part 2 , Sections 1, 2, and 7 above, and Part 8, Section 2.2.5.1 above;

3. The Councils relied on the AAA rating from S&P, which they understood from the Investment Guidelines to be the "best independent information available" as to the creditworthiness of an investment: see Part 2 , Sections 1, 2 and 7, [580], [784], [1292] and Part 9 above;

4. The Councils understood the product was a structured credit product which was liquid and had a high level of security consistent with a AAA rating from S&P, and believed such information to be from reliable sources (that is, LGFS and S&P): see [130] above;

5. The Councils were not obliged to understand the mechanics of credit default swaps and the integers of the Rembrandt notes in order to act as a prudent person, which was acknowledged in the Investment Guidelines by the fact that ratings were stated to be the best independent information available as to the creditworthiness of an investment: see Part 2 , Section 3.1 and [1292] above;

6. The Councils would not have gained an understanding from reading the Pre-Sale Report and the Post-Sale Report of the risks of the notes, as S&P acknowledged that many principal risks were not disclosed (see [1029], [1056], [1167]-[1178] and [1268] above) and in any event, any reasonable investor acting prudently would have been satisfied that S&P, an expert ratings agency, had

assessed all of those risks and concluded that the capacity of the Rembrandt notes to pay interest and principal was consistent with a AAA rating: see Part 2 , Section 5 above;

7. The Councils would have been misled, if they had read the Pre-Sale Report (see [49]-[50] above) and the Post-Sale Report (see [53] above) in full, as to one of the key risks of the notes by the misleading statement that "spread widening, and no corresponding defaults, is beneficial to the structure": see [1029], [1056], [1167]-[1178] and [1268] above; and

8. The Councils would never have been able to understand the ABN Amro term sheet and LGFS did not suggest to them that they needed to read it: see [1029], [1056], [1167]-[1178] and [1268] above.

1487. In that context, it is important to recall that a prudent person will ordinarily have available the defence that they had selected a reasonably careful person and acted upon the skilled advice that they had received upon such a question: see [1480(1)] above. Here, that is what the Councils did. As the primary judge found, the Councils "trusted LGFS as experts in investments by local government and, in every case, were led to believe by LGFS that this AAA rated investment was a suitable one for a council to make": see Part 8, Section 2.2.1 above and J[1422]. In those circumstances, the Councils discharged their obligation to act as a prudent person by relying upon the advice of their trusted investment adviser, LGFS, which professed to be an expert in the local government investment industry.

1488. Finally, it is necessary to address the fact that although the Councils were not in the business of investing, each employed an officer responsible (among other responsibilities) for investments: J[1418]-J[1422] and J[1446]. That fact is neutral. As the Councils submitted, they were empowered to exercise their functions, including their investment function, in a number of possible ways. There was no requirement that the Councils, having obtained independent financial advice in relation to the Rembrandt notes, second-guess that advice in order to act as a prudent person. Moreover, this was not a case where they had delegated their entire responsibility to a third party; nor in any event, did the third party (LGFS) draw to the Councils' attention any material error in the rating: *Australian Securities and Investments Commission v Healey* (2011) 196 FCR 291 at 342 [215] . ABN Amro's submission that the primary judge appears to have made an assumption that a plaintiff cannot be guilty of contributory negligence where a professional has breached its duty to the plaintiff is without warrant. The primary judge's findings make it clear that her Honour was addressing the Councils' position in the context of their factual circumstances, not by the general overarching "assumption" ABN Amro seeks to have attributed to her.

1.4.4 *Councils' consideration of the Pre-Sale Report and the Post-Sale Report and other documents: S&P Appeal Grounds Matrix Rows 41 and 42 and ABN Amro Appeal Grounds Matrix Rows 90, 91 and 94*

1489. The primary judge accepted that many Council officers did not read or understand the documents in relation to the Rembrandt notes that LGFS provided to them: see [1029], [1056], [1167]-[1175], [1178] and[1268] above and J[1422]. The primary judge rejected, however, the contention that the Councils' failure to read was a "substantial failure to exercise care on the part of the decision makers".

1490. S&P challenged the latter finding. S&P contended that the primary judge erred because the Councils' failure to read such material constituted a failure to comply with their obligation to understand the nature of the investment that they were making when purchasing the Rembrandt notes. ABN Amro made a similar submission. In support of that contention, S&P referred to *Wingecarribee Shire Council* at [1166]-[1167] where Rares J said that "a reasonable person [(let alone a prudent person)] … ought to have looked at [a] document and at least begun to read it to understand why it had been sent and what it was conveying about the potential … investment".

1491. The primary judge provided extensive reasons for rejecting the contention that the Councils' failure to read was a "substantial failure to exercise care on the part of the decision makers". J [1455]-J[1467], J[2467]-J[2484] and especially at J[2471]. S&P did not address these extensive reasons but chose to challenge this aspect of the reasons and a statement by the primary judge that S&P had no expectation that the S&P Reports would be read. That statement must be understood in the context in which it was made. For example, the primary judge stated:

> 1465 Once this evidence is taken into account certain other propositions become apparent and undermine S&P's contention of imprudence on the part of the [C]ouncil officers for not having read and understood the S&P [R]eports. The propositions are these:
>
> (1) S&P published a system of stand alone ratings where the relevant information for an investor was contained in the rating itself and the accompanying definition S&P assigned to the rating.
>
> (2) S&P took no step to ensure that a person relying on its rating did so only in the context of whatever report S&P might happened to have published at the same time.
>
> (3) S&P seems to have had no system to ensure that it did not assign a rating unless it had also published an accompanying report (and the present case shows this to be so).
>
> (4) S&P did not refer to its reports in its formal letters assigning ratings.
>
> (5) S&P did not take any step to ensure that the person who had obtained the rating ensured that they gave to any prospective investor any S&P report which explained how S&P had reached the rating.
>
> 1466 The inferences to which these facts lead are inescapable:
>
> *(a) S&P never expected that investors would all obtain, read and understand those reports, and*
>
> (b) S&P did not believe it was necessary for investors to do so in order to understand S&P's rating.

> 1467 In these circumstances the fact that LGFS provided the S&P [R]eports to many of the councils (not all before they decided to invest), wrongly believing it to explain the structure and the risks of the investment, does not support the contention of imprudence. S&P, the author of the reports, did not consider that investors had to read the reports in order to understand the rating.
>
> (Emphasis added.)

As is readily apparent, the statement in italics was just part of the primary judge's reasons.

1492. S&P then took issue with the last sentence – "S&P, the author of the reports, did not consider that investors had to read the reports in order to understand the rating". S&P again took that sentence out of context. On appeal, S&P contended that the primary judge had proceeded on a misconception that its reports were not necessary in order to understand the rating that was assigned to the Rembrandt notes and there was no system in place that required the report to accompany the rating: see J[1465]-J[1467]. That assertion, without more, is rejected and irrelevant. The question was not whether a prudent (or alternatively reasonable) person would have read the S&P Reports in making an investment decision. The question was and remains whether the Councils had in any event acted as a prudent person (or alternatively reasonable person) would. Here, in the circumstances, the answer was and remains yes. For example, it must be recalled that the S&P Reports were published after ABN Amro was authorised to disseminate the rating (see [49]-[55] above) and there was no requirement for the S&P Reports to be communicated to potential investors who relied on the AAA rating: see [55], [744] and [752] above.

1493. Indeed, it would not have mattered if all the Councils' witnesses had read the S&P Reports. The S&P Reports did *not* disclose all of the risks of the Rembrandt notes: see [1176]-[1177] above. If they had read it, it would not have caused the Councils to conclude that the Rembrandt notes, with a AAA rating from S&P together with LGFS' recommendation, were not a suitable investment for the Councils: J[2467]-J[2484].

1.4.5 *Council Officers' understanding of the Rembrandt notes: S&P Appeal Grounds Matrix Rows 43 and 44 and ABN Amro Appeal Grounds Matrix Row 91*

1494. S&P and ABN Amro submitted that the primary judge erred in failing to find that although industry practice *required* the Councils to understand the nature of the investments they made, the Council officers failed to exercise reasonable care by failing to understand one or more of the basic risks of the Rembrandt notes or in failing to take adequate steps to understand the risks. These Appeal Grounds are rejected.

1495. First, the "requirement". S&P submitted that the requirement was contained in the Investment Guidelines: see Part 2 , Section 1.3 above. Those Guidelines were as their name suggests – guidelines. ABN Amro relied instead on the NSW Local Government Investments Best Practice Guide, and in particular the caution contained within that document that Councils should "not invest in products [they] do not understand and take the time to learn/understand available products": see [25] above. Both documents had no official status and did not contain a binding legal obligation. There was no failure to exercise due care because, after the product failed, it was established that the Councils did not understand some aspect or aspects of the product. The Councils knew and understood that the Investment Guidelines and the Best Practice Guide warned the Councils not to invest in products that they did not understand. The Councils' evidence was that they believed that they understood the product sufficiently at the time that they invested in it (J[2484]), that they were entitled to rely upon LGFS' advice and that they reasonably believed that they knew everything about the product that they needed to know: J[1472], J[1473], J[2484], J[1451 and J[3345(5)]. The Council officers recognised their own limitations in understanding financial products and relied on a trusted adviser, LGFS, so that their limitations should not deprive them of suitable investment opportunities.

1496. As the Councils submitted:

1. The Councils relied on LGFS, their trusted financial adviser and confidant, to identify risks and assess the appropriateness of the Rembrandt notes for each of the Councils: J[3345].

2. The Councils were entitled to rely on that advice in establishing that they acted with reasonable care (*NMFM Property* at 380-381 [494] and *Learoyd v Whiteley* at 730-731): J[3348].

3. The Councils could never have done anything which would have enabled them to discover that LGFS had failed to disclose all the risks of the notes to them, nor that S&P's rating was not based on reasonable grounds: J[2769], J[2773] and J [2775].

4. The Councils would not have gained an understanding from reading the S&P Reports of the risks of the notes, as S&P acknowledged that many principal risks were not disclosed, and, in any event, any reasonable investor acting prudently would have been satisfied that S&P, an expert ratings agency, had assessed all of those risks and concluded that the capacity of the notes to pay interest and principal was consistent with a AAA rating: J[3345(5)] and J[1461].

5. The Councils were not obliged to understand the complex structure and risks of Rembrandt notes in order to act as a prudent person. The Councils understood, from what they believed to be reliable sources, that the product was highly liquid (as LGFS had offered a 24 hour guarantee) and had a high level of security consistent with a AAA rating from S&P: J[3345(3)].

1497. In all the circumstances, these Appeal Grounds fail. As we have said on more than one occasion, the witnesses' evidence made clear that "they did not know what they did not know" and thus could never have asked the right questions to obtain the relevant information: see J[1620], J[1639] and [1177] above.

1.4.6 *Hindsight evidence as to what the Councils would have done: S&P Appeal Grounds Matrix Row 45*

1498. On appeal, S&P took issue with the primary judge's finding that the evidence of the majority of the council officers that they would not have invested in the notes if they had read the material provided to them by their financial adviser or understood one or more basic matters in relation to the notes should be disregarded as "hindsight": J[1422], J[1425] and J [1429]. S&P submitted that "a majority of the Councils' witnesses said that they would not have purchased the Rembrandt 2006-3 notes if they had read one or more items of the material that was provided to them or if they had understood one or more basic risks in relation to the notes". Indeed, S&P went so far to submit that "[t]hese admissions carry considerable weight and, if they are to be displaced, require 'a convincing explanation of how they came to be made' which justifies this course (*Voulis v Kozary* (1975) 180 CLR 177 at 193 ; see also *Scalise v Bezzina* [2003] NSWCA 362 at [66] …".

1499. S&P's submissions misstated the evidence. Four of the 12 PA Councils gave evidence that they did not read the Pre-Sale Report – Moree, Murray, Oberon and Orange. Mr Bokeyar of Parkes could not recall reading the Pre-Sale Report but he was not the decision maker: see T1680.32-34 and T1629.33-1631.16. The remaining Councils' witnesses either read the Pre-Sale Report (Cooma (T456-T457), Deniliquin (T811), Eurobodalla (T1147), Narrandera (T1277-T1278) and Ryde (T1793) or could not recall doing so: Corowa (T621-622) and Narromine (T1356-1357).

1500. No less importantly, the Council officers' evidence was that if the risks in the Pre-Sale Report had been *explained* to them, or had they known at the time of investing what they subsequently learnt about the risks attached to the notes, they would not have invested in them: see [1125], [1195], [1198]-[1202] and [1230]-[1235] above. That was not, and is not, surprising.

1501. In the end, this Appeal Ground may be put to one side. As the primary judge identified at J [2484], whether the Councils acted reasonably in purchasing the notes and satisfied their obligations to understand the products in which they invested is a matter for objective, not subjective, determination having regard to all the facts and circumstances at the relevant time.

1.4.7 *Councils breached the Local Government Act : ABN Amro Appeal Grounds Matrix Rows 92 and 94C*

1502. ABN Amro made a further submission that the Councils should have been found to have been contributorily negligent in circumstances where the Rembrandt notes were not "securities" within the terms of the Ministerial Order and, therefore, investment in them was prohibited. We reject these Appeal Grounds for the reasons at [1272]- [1301] above.

1.4.8 *LGFS' Appeal Grounds: LGFS Appeal Grounds Matrix Rows 110 and 111*

1503. LGFS challenged the primary judge's finding that the Councils had not failed to take reasonable care and were not contributorily negligent for the following reasons:

1. The Councils did not make an assessment of risk;

2. The Councils did not ask LGFS about risks associated with volatility and complexity;

3. The Councils failed to read the Pre-Sale Report and thus failed to appreciate or ask about facts of which they ought reasonably to have had notice;

4. The Councils failed to adopt policies to ensure that they did not invest in products where liquidity was an issue;

5. The NRB Councils did not make it clear to LGFS that they were relying on LGFS; and

6. The Councils did not tell LGFS of their difficulties in understanding structured products or the documents provided to them.

1504. These Appeal Grounds are without foundation and are dismissed for the reasons in this Part (Part 13, Section 1) and Part 8 above.

1.4.9 *Conclusion*

1505. The detailed elaboration in the Appeal Grounds of supposed error by the primary judge (none of which was established) was misplaced. Merely selecting, or emphasising, one or more considerations over others that were properly taken into account in reaching the conclusion does not demonstrate error. The Councils did not fail to take reasonable care and were not contributorily negligent.

2. APPORTIONMENT

2.1 Introduction

1506. This section of the judgment concerns apportionment of the losses suffered by the Councils and LGFS. The primary judge held:

1. Each of LGFS, S&P and ABN Amro liable for one-third of the losses of the Councils; and

2. Each of S&P and ABN Amro liable for one-half of LGFS' losses.

1507. ABN Amro challenged these findings: ABN Amro Appeal Grounds Matrix Rows 95, 95A, 95B and 95C. LGFS challenged these findings: LGFS Appeal Grounds Matrix Rows 106-108. S&P challenged these findings: S&P Appeal Grounds Matrix Rows 46I and 46J.

2.2 Apportionment of the losses

2.2.1 Applicable Principles

1508. The question of apportionment of loss is a matter of judgment and discretion on which reasonable minds might differ.

1509. In *Podrebersek v Australian Iron and Steel Pty Ltd* (1985) 59 ALJR 492 at 493-494, the High Court stated, in context of contributory negligence, that:

> A finding on a question of apportionment is a finding upon a "question, not of principle or of positive findings of fact or law, but of proportion, of balance and relative emphasis, and of weighing different considerations. It involves an individual choice or discretion, as to which there may well be differences of opinion by different minds": *British Fame (Owners) v Macgregor (Owners)* (1943) AC 197, at p 201. Such a finding, if made by a judge, is not lightly reviewed.

1510. Here, the primary judge assessed the correct questions, principally:

1. The relative culpability of the conduct of each of LGFS, S&P and ABN Amro. In other words, the nature of each one's wrongdoing and its seriousness relative to that of the others; and

2. The relative importance of the conduct of each of those parties in causing the loss.

1511. The losses in issue are those of the Councils and LGFS.

2.2.2 Councils' losses

1512. ABN Amro's contention on appeal was that the primary judge erred in failing to find that the culpability and causative effect of the conduct of LGFS and S&P was significantly greater than that of ABN Amro. LGFS submitted that the primary judge erred in not finding that ABN Amro and S&P were responsible for a greater proportion of the Councils' losses than LGFS. S&P's position on appeal was that if its liability to the Councils and LGFS was affirmed on appeal (as it has been), then the primary judge's allocation of responsibility for loss should not be disturbed. S&P submitted that not only was it open to the primary judge to find that LGFS, S&P and ABN Amro were equally responsible for any losses suffered but that finding was preferable on the evidence. We agree with S&P. The primary judge's allocation of responsibility for loss should not be disturbed.

2.2.3 LGFS' losses

1513. As we have said, each of S&P and ABN Amro was found liable for one-half of LGFS' losses. LGFS' losses included its settlement payment to StateCover. There is no basis for distinguishing between their respective responsibilities. The assessment of their respective positions demonstrates that their degree of culpability and responsibility for LGFS' losses is not shown to be other than equal. The detailed elaboration in the Appeal Grounds of supposed error by the primary judge (none of which was established) is not directed at questions of principle. Instead, S&P and ABN Amro impermissibly seek to invoke a judgment different from that formed by the primary judge by emphasising one or more considerations over others that were properly taken into account in forming the ultimate conclusion.

2.3 AHAC's submissions: AHAC Appeal Grounds Matrix Rows 12-16 and 20-22

1514. AHAC submitted that LGFS' liability should be reduced with the result that it reduce the amount LGFS was entitled to recover from AHAC: AHAC Appeal Grounds Matrix Rows 12-16 and 20-22.

1515. In particular, AHAC submitted that:

1. The primary judge erred in failing to find that LGFS was entitled to damages payable by S&P and ABN Amro in a sum which equated to the amount which LGFS was liable to pay to the Councils in respect of its breach of fiduciary duty in each case: AHAC Appeal Grounds Matrix Row 12;

2. Alternatively, the primary judge erred in not holding that the Councils' claims against LGFS for breach of fiduciary duty was to be treated as apportionable claims based upon the reasoning set out at J[3485]: AHAC Appeal Grounds Matrix Row 13;

3. Alternatively, the primary judge erred in holding that the effect of the proportionate liability provisions of the *Civil Liability Act* was to defeat the entitlement of LGFS for a full indemnity by way of damages from S&P and ABN Amro in respect of its loss which consisted of the sums which it was liable to pay to the Councils: AHAC Appeal Grounds Matrix Row 14;

4. The primary judge erred in failing to find that LGFS was entitled by way of damages from S&P and ABN Amro to a full indemnity in respect of the amounts it was found liable to pay to the Councils: AHAC Appeal Grounds Matrix Row 15;

5. Alternatively, the primary judge erred in finding that the liability of LGFS in respect of the Councils' claim should be in the proportion of one-third, when that liability ought to have been held to be a substantially lesser proportion: AHAC Appeal Grounds Matrix Row 16;

6. The primary judge erred in holding that the effect of the proportionate liability provisions of the *Civil Liability Act* was to defeat the entitlement of LGFS for a full indemnity by way of damages from S&P and ABN Amro in respect of its loss which consisted of the sum which it was liable to pay to StateCover: AHAC Appeal Grounds Matrix Row 20;

7. The learned primary judge erred in failing to find that LGFS was entitled by way of damages from S&P and ABN Amro to a full indemnity in respect of the amount it was liable to pay to StateCover: AHAC Appeal Grounds Matrix Row 21; and

8. Alternatively, the primary judge erred in finding that the liability of LGFS in respect of the StateCover settlement should be in the proportion of one-third, when that liability ought to have been held to be a substantially lesser proportion: AHAC Appeal Grounds Matrix Row 22.

1516. None of these Appeal Grounds were addressed by AHAC in their written or oral submissions. In the matrix, AHAC referred to LGFS Appeal Grounds Matrix Rows 106-108 and stated that it relied on LGFS' submissions in relation to those Appeal Grounds. Those Appeal Grounds have been addressed in Part 13, Sections 2.1 and 2.2 above and are rejected for the same reasons.

3. PROPORTIONATE LIABILITY UNDER the *CORPORATIONS ACT* AND THE *ASIC ACT*

3.1 Introduction

1517. The damages awarded in favour of the PA Councils were apportioned as between LGFS, S&P and ABN Amro under the proportionate liability provisions of the *Corporations Act* and the *AS*

IC Act . The PA Councils contend that this should not have occurred and that they should have the benefit of joint and several judgments in each case: PA Councils Appeal Grounds Matrix Rows 132-133.

1518. The primary judge found that each of ABN Amro, S&P and LGFS contravened s 1041E of the *Corporations Act* : J[2239] (with respect to LGFS), J[3178] and J[3246] (with respect to ABN Amro), and J[2905]-J[2910] and J[3339] (with respect to S&P). Her Honour also found that each also contravened s 1041H . The finding of combined contraventions is at J[3339]. However, neither there nor elsewhere is it possible to discern clearly the particular findings directed only to the contraventions of s 1041H . This is significant in the resolution of the cross-appeal.

1519. Findings at J[3339] against each of LGFS, S&P and ABN Amro of contravention of s 12DA of the *ASIC Act* were also made. This is the general provision prohibiting conduct in relation to financial services that is misleading or deceptive or likely to mislead or deceive. Accordingly, the provisions of s 12GF(1) of the *ASIC Act* were engaged. The PA Councils' submissions were directed to the provisions of the *Corporations Act* .

1520. The primary judge (at J[3485]) held, correctly in our opinion, that damages for contravention of s 1041E of the *Corporations Act* were not apportionable. However, her Honour held that in this case, those claims arose from the same facts as the contraventions of s 1041H which are apportionable, adopting the reasoning of Barrett J (as his Honour then was) in *Reinhold v New South Wales Lotteries Corporation (No 2)* (2008) 82 NSWLR 762.

1521. The PA Councils contend that the damages awarded should not have been apportioned under the relevant provisions of the *Corporations Act* . It is evident from the PA Councils' submissions that they have proceeded on the footing that the primary judge found that the claims under s 1041E were apportionable. We do not think this was the case although it is not, in part, entirely free from doubt. The primary judge at J[3485] plainly said to the contrary. It seems her Honour proceeded on the basis that the facts which established contraventions of s 1041E also make out contraventions of s 1041H of the *Corporations Act* and s 12DA of the *ASIC Act* . However, in doing so, her Honour placed reliance on the reasoning in *Reinhold.* As we will explain, this was misplaced. To the extent that her Honour did so we have concluded that she was in error. Even if it were accepted that the contraventions of ss 1041E and 1041H were founded on the same facts, we consider that the damages from the cause of action founded on the contraventions of s 1041E ought not to have been apportioned as between LGFS, S&P and ABN Amro. Rather, each ought to have been jointly and severally liable for those damages. We have also concluded that the finding that the facts were the same in relation to both sets of contraventions was erroneous.

1522. To the extent that there were also contraventions of s 1041H of the *Corporations Act* and s 12DA of the *ASIC Act* it is not, in her Honour's reasons, possible to separate the facts supporting these from the facts sustaining the non-apportionable claims for contravention of s 1041E . However, the claims made, as pleaded, differentiated the facts relied upon as between s 1041E and s 1041H . Whilst there is some overlap, there were additional facts pleaded, which required to be proved, to establish the claim made under s 1041E .

1523. The damages caused by these contraventions of ss 1041E or 1041H and s 12DA of the *ASIC Act* are the same. Where damages, in those circumstances, proceed from an apportionable claim (s 1041H) or alternatively a non-apportionable claim (s 1041E) then the remedies, to that extent, available to the PA Councils are mutually inconsistent. This gives rise to an election on the part of the PA Councils. Plainly, by bringing this cross-appeal the PA Councils elect the remedy of judgment for damages without apportionment proceeding from the cause of action founded on the contraventions of s 1041E .

1524. It will be sufficient for our analysis to focus on the provisions of the *Corporations Act* althoug h our reasoning and conclusions are apt also for the proportionate liability provisions under the *ASIC Act* , *mutatis mutandis.* We have come to these conclusions for the reasons which follow.

1525. The PA Councils contend that on a proper construction of s 1041L, including the exclusion of s 1041E from the definition of apportionable claims, claims for loss or damage arising out of a contravention of s 1041E are not apportionable. We do not understand, in the way already explained, that the primary judge held otherwise.

1526. Conversely, LGFS, S&P and ABN Amro submit that the PA Councils' claim based on conduct done in contravention of s 1041E of the *Corporations Act* was both an apportionable claim and a claim to which the ordinary principles of contributory negligence applied. As we have said, this is not the approach that was taken by the primary judge.

1527. Accordingly, it will be necessary to consider the proper construction of the proportionate liability provisions in the *Corporations Act* as well as the *ASIC Act* and their application to the facts in this case.

3.2 Proportionate liability

1528. Proportionate liability and contributory negligence provisions were introduced by the Commonwealth, States and Territories following an inquiry established by the Attorneys-General of the Commonwealth and New South Wales in 1994.

1529. The inquiry was the result of growing concerns as to the rise in litigation against professional people, and auditors in particular, who were being pursued, not by reason of their greater culpability, which may not have been great, but rather because they carried professional indemnity insurance with cover sufficient to meet large damages awards: the so-called "deep pockets syndrome". This in turn had led to a significant rise in premiums for such insurance cover.

1530. Proportionate liability broadly means that liability rests with all defendants in proportion to their contribution to the plaintiff's loss.

1531. The Commonwealth amended the *Corporations Act* and the *ASIC Act* , responding to draft model provisions. The States and Territories also agreed to introduce amending legislation. The intent was to achieve a nationally consistent regime in relation to proportionate liability. The contributory negligence provisions may be regarded as part of such a regime.

1532. This objective has not been achieved. There are important differences between the Commonwealth provisions, found variously in the *Corporations Act* , the *ASIC Act* and the *Competition and Consumer Act 2010* (Cth) . Those differences are significant in the context of this cross-appeal.

3.3 Statutory framework

1533. Part 7.10 Div 2 of the *Corporations Act* contains provisions for prohibited conduct concerning financial products, financial services and financial markets other than insider trading provisions.

1534. Under this division, ss 1041A, 1041B, 1041C, 1041D and 1041E proscribe conduct including market manipulation, false trading, market rigging, dissemination of information about illegal transactions, and false or misleading statements. Failure to comply with any of these sections is an offence and, with the exception of s 1041E , each is also a civil penalty provision. Section 1041F prohibits a person from inducing another person to deal in financial products. Section 1041G prohibits dishonest conduct in relation to a financial product or a financial service. Contravention of either s 1041F or s 1041G is an offence.

1535. By contrast, s 1041H proscribes conduct in relation to a financial product or a financial service that is misleading or deceptive conduct. However, failure to comply with this provision is neither a criminal offence nor a civil penalty provision although it may lead to civil liability under s 1041I .

1536. Section 1041I provides relevantly:

Civil action for loss or damage for contravention of sections 1041E to 1041H

(1) A person who suffers loss or damage by conduct of another person that was engaged in in contravention of section 1041E, 1041F, 1041G or 1041H may recover the amount of the loss or damage by action against that other person or against any person involved in the contravention, whether or not that other person or any person involved in the contravention has been convicted of an offence in respect of the contravention.

(1A) Subsection (1) has effect subject to section 1044B.

Note: Section 1044B may limit the amount that the person may recover for a contravention of section 1041H (Misleading or deceptive conduct) from the other person or from another person involved in the contravention.

(1B) Despite subsection (1), if:

(a) a person (the ***claimant***) makes a claim under subsection (1) in relation to:

(i) economic loss; or

(ii) damage to property;

caused by conduct of another person (the ***defendant***) that was done in contravention of section 1041H ; and

(b) the claimant suffered the loss or damage:

(i) as a result partly of the claimant's failure to take reasonable care; and

(ii) as a result partly of the conduct referred to in paragraph (a); and

(c) the defendant:

(i) did not intend to cause the loss or damage; and

(ii) did not fraudulently cause the loss or damage;

the damages that the claimant may recover in relation to the loss or damage are to be reduced to the extent to which the court thinks just and equitable having regard to the claimant's share in the responsibility for the loss or damage.

1537. Division 2A provides for proportionate liability for misleading and deceptive conduct.

1538. Section 1041L provides:

Application of Division

(1) This Division applies to a claim (an ***apportionable claim***) if the claim is a claim for damages made under section 1041I for:

(a) economic loss; or

(b) damage to property;

caused by conduct that was done in a contravention of section 1041H .

(2) For the purposes of this Division, there is a single apportionable claim in proceedings in respect of the same loss or damage even if the claim for the loss or damage is based on more than one cause of action (whether or not of the same or a different kind).

(3) In this Division, a ***concurrent wrongdoer*** , in relation to a claim, is a person who is one of 2 or more persons whose acts or omissions (or act or omission) caused, independently of each other or jointly, the damage or loss that is the subject of the claim.

(4) For the purposes of this Division, apportionable claims are limited to those claims specified in subsection (1).

(5) For the purposes of this Division, it does not matter that a concurrent wrongdoer is insolvent, is being wound up or has ceased to exist or died.

1539. Section 1041M provides:

Certain concurrent wrongdoers not to have benefit of apportionment

(1) Nothing in this Division operates to exclude the liability of a concurrent wrongdoer (an ***excluded concurrent wrongdoer***) in proceedings involving an apportionable claim if:

(a) the concurrent wrongdoer intended to cause the economic loss or damage to property that is the subject of the claim; or

(b) the concurrent wrongdoer fraudulently caused the economic loss or damage to property that is the subject of the claim.

(2) The liability of an excluded concurrent wrongdoer is to be determined in accordance with the legal rules (if any) that (apart from this Division) are relevant.

(3) The liability of any other concurrent wrongdoer who is not an excluded concurrent wrongdoer is to be determined in accordance with the provisions of this Division.

1540. Section 1041N provides:

Proportionate liability for apportionable claims

(1) In any proceedings involving an apportionable claim:

(a) the liability of a defendant who is a concurrent wrongdoer in relation to that claim is limited to an amount reflecting that proportion of the damage or loss claimed that the court considers just having regard to the extent of the defendant’s responsibility for the damage or loss; and

(b) the court may give judgment against the defendant for not more than that amount.

(2) ...

(3) In apportioning responsibility between defendants in the proceedings:

(a) the court is to exclude that proportion of the damage or loss in relation to which the plaintiff is contributorily negligent under any relevant law; and

(b) the court may have regard to the comparative responsibility of any concurrent wrongdoer who is not a party to the proceedings.

(4) This section applies in proceedings involving an apportionable claim whether or not all concurrent wrongdoers are parties to the proceedings.

(5) A reference in this Division to a defendant in proceedings includes any person joined as a defendant or other party in the proceedings (except as a plaintiff) whether joined under this Division, under rules of court or otherwise.

1541. Section 1041O provides:

Defendant to notify plaintiff of concurrent wrongdoer of whom defendant aware

(1) If:

(a) a defendant in proceedings involving an apportionable claim has reasonable grounds to believe that a particular person (the ***other person***) may be a concurrent wrongdoer in relation to the claim; and

(b) the defendant fails to give the plaintiff, as soon as practicable, written notice of the information that the defendant has about:

(i) the identity of the other person; and

(ii) the circumstances that may make the other person a concurrent wrongdoer in relation to the claim; and

(c) the plaintiff unnecessarily incurs costs in the proceedings because the plaintiff was not aware that the other person may be a concurrent wrongdoer in relation to the claim;

the court hearing the proceedings may order that the defendant pay all or any of those costs of the plaintiff.

(2) The court may order that the costs to be paid by the defendant be assessed on an indemnity basis or otherwise.

1542. Section 1041P provides:

Contribution not recoverable from defendant

A defendant against whom judgment is given under this Division as a concurrent wrongdoer in relation to an apportionable claim:

(a) cannot be required to contribute to any damages or contribution recovered from another concurrent wrongdoer in respect of the apportionable claim (whether or not the damages or contribution are recovered in the same proceedings in which judgment is given against the defendant); and

(b) cannot be required to indemnify any such wrongdoer.

1543. Section 1041R provides:

Joining non-party concurrent wrongdoer in the action

(1) The court may give leave for any one or more persons to be joined as defendants in proceedings involving an apportionable claim.

(2) The court is not to give leave for the joinder of any person who was a party to any previously concluded proceedings in respect of the apportionable claim.

3.4 The proportionate liability provisions under Div 2A of the *Corporations Act*

1544. Sections 1041L-1041S introduced a significant change, for those cases covered by them, in relation to the recovery of damages. Joint and several liability in effect was removed and certain concurrent wrongdoers rendered liable, in relation to a claim, limited to an amount reflecting that proportion of the damage or loss claimed that the court considers just having regard to the extent of the defendant's responsibility for the damages or loss.

1545. Its application is mandatory. The court may give judgment against the defendant for not more than that amount: s 1041N(1)(b).

1546. Other Commonwealth legislation introduced proportionate liability regimes: the *ASIC Act* (Subdiv GA) and the *Competition and Consumer Act* (Pt VIA). We will consider these in due course.

1547. Similar but different legislation has been introduced in the States and Territories. It is sufficient to mention two of these: the *Civil Liability Act* (Pt 4) and the *Wrongs Act 1958* (Vic) (Pt IVAA).

1548. The provisions in the *Civil Liability Act* (s 34(1)) and the *Wrongs Act* (ss 24AF and 24AG) are in substance of similar effect. They provide that the apportionable claim provisions apply to a claim for economic loss or damage to property in an action for damages (whether in tort, in contract, under statute or otherwise) "arising from a failure to take reasonable care". Claims for damages for personal injury are excluded.

1549. Section 1041L(1) of the *Corporations Act* contains significant differences. For example, s 1041L(1) defines an apportionable claim as being a claim for damages made under s 1041I for economic loss or damage to property caused by conduct that was done in a contravention of s 1041H . Section 1041L(4) limits apportionable claims to those specified in subs (1). It is a claim "made", not a claim "established", which meets this description. It is not necessary to await the judgment of a court in respect of such a claim before it is afforded the status of an "apportionable claim": cf *Reinhold* at 769 [18]-[22] . Obviously the assessment of proportionate liability, if any, must necessarily be the product of relevant findings of fact and law by the court. Thus s 1041N(1) provides that "[i]n any *proceedings* involving an apportionable claim" the *liability* of a defendant who is a concurrent wrongdoer in relation to that claim is limited to the proportion of the damage or loss claimed which the court considers just having regard to the extent of the defendant's responsibility for the damage or loss.

1550. It may be that although being an apportionable claim no apportionment in fact is made where it is not established in the proceedings by judgment that there is a concurrent wrongdoer. On the other hand, it may be established that there is a concurrent wrongdoer but, by reason of the exclusion in s 1041M , that person does not have the benefit of apportionment. Despite either of these circumstances, the claim made would be, from the outset, an apportionable claim but as it transpired not one resulting in apportionment.

1551. Section 1041O provides for a potential adverse costs order against a defendant in proceedings "involving an apportionable claim" in relation to failing to notify the plaintiff "as soon as practicable" of a person who the defendant has reasonable grounds to believe may be a concurrent wrongdoer. A defendant, in those circumstances, must be able to identify that the claim is an "apportionable claim" in order to be in a position to give such notice. They cannot wait until judgment in the proceedings. The claim is identifiable as an apportionable claim because it is "a claim for damages made under section 1041I … caused by conduct that was done in a contravention of section 1041H ": s 1041L(1).

1552. The judgment in *Reinhold*, relied upon in this respect by her Honour, and the decision of the Victorian Court of Appeal in *Godfrey Spowers (Victoria) Pty Ltd v Lincolne Scott Australia Pty Ltd* (2008) 21 VR 84, upon which LGFS, S&P and ABN Amro rely, accordingly must be considered bearing these differences in mind.

3.5 The cross-appeal by LGFS, S&P and ABN Amro

1553. The first question in this cross-appeal is whether, as LGFS, S&P and ABN Amro contend, a claim for damages made under s 1041I for economic loss caused by conduct that was done in contravention of s 1041E may fall within the definition of an apportionable claim as defined in s 1041L. However, even if that question is answered adversely to them, further questions fall to be considered. They arise from the way we apprehend the primary judge approached and determined the issue of apportionment.

1554. The questions are these:

1. Was the conclusion of the primary judge at J[3485] that the (pleaded) contraventions of ss 1041H and 1041E arose from the same facts erroneous?

2. Whether or not the primary judge was in error in concluding that the contraventions of ss 1041H and 1041E arose from the same facts, did she, in any event, err in entering a judgment which apportioned the damages equally as between LGFS, S&P and ABN Amro? Should the judgments, rather, have been joint and several?

3.6 Consideration

1555. The starting point with respect to the first question is the text and context and purpose of the provisions of the *Corporations Act* to which we have referred: *Project Blue Sky* at 381 [69] .

1556. Each of LGFS, S&P and ABN Amro made submissions but it will be convenient to consider these in a composite manner. That said, S&P seems to want to run with the hares as well as the hounds on this issue. In other submissions (dated 5 December 2013, at [26] on the issue between it and LGFS concerning whether damages awarded against LGFS for breach of fiduciary duty are apportionable under s 1041L of the *Corporations Act*) it appears to support the construction for which the PA Councils contend in their cross-appeal.

1557. LGFS, S&P and ABN Amro contend that the ordinary meaning of s 1041L makes clear that a claim for contravention of s 1041E that is founded on the same conduct that gives rise to a contravention of s 1041H will mean that both claims will be apportionable.

1558. Their submission is that s 1041L focuses on a claim that is "caused by conduct that was done in a contravention of section 1041H " and that the use of the word "conduct" in the section is important because it focuses attention on the physical acts that give rise to a claim under s 1041I , rather than the legal label that is attached to that conduct. Accordingly, they contend, in determining whether there is an apportionable claim, the relevant inquiry is whether the damage claimed under s 1041I was caused by misleading or deceptive conduct. The result, they submit, is that if it is established that there is a claim under s 1041I for damages that was caused by misleading or deceptive conduct then the claim will be apportionable irrespective of whether the claim is formally framed by reference to ss 1041E, 1041F, 1041G or 1041H .

1559. They further submit that had the legislature intended to limit the operation of s 1041L only to contraventions of s 1041H there would have been no need to use the words "conduct that was done in" in s 1041L, and that in accordance with ordinary rules of statutory interpretation these words should be given meaning. They contend that the construction of s 1041L advanced by them does so.

1560. We do not accept these submissions for the reasons which follow.

1561. Nor do we accept their submission that the absence, in the text of s 1041IL , of an express exclusionary provision relating, relevantly, to s 1041E , or for that matter ss 1041F or 1041G tells in favour of their construction. To the contrary, we regard the absence of those sections and the reference only to s 1041H as pointing to a construction that it is only claims made for damages for loss or damage "caused by conduct that was done in a contravention of section 1041H " which are apportionable claims. When s 1041L(1) is read together with s 1041I(1) it is apparent that claims for damages made for loss or damage caused by conduct that was done in contravention of ss 1041E, 1041F and 1041G are, by implication, excluded.

1562. Section 1041L does not apply merely to a claim alleging misleading or deceptive conduct and which might point to contravention of a number of provisions answering that general rubric ranging from s 1041A through to s 1041H . Rather, it specifically requires that the claim be a claim for damages made under s 1041I for relevant loss or damage caused by conduct "that was done in a contravention of section 1041H ". It is this expressly identified conduct which is the subject of a claim made that meets the statutory definition of an "apportionable claim". No other conduct meets the definition.

1563. It is important to appreciate that s 1041I expressly enables civil action for contraventions of ss 1041E, 1041F, 1041G or 1041H but it is only s 1041H which is expressly identified in s 1041L. So, too, is the position in relation to the contributory negligence provisions found in s 1041I(1B)(a) . Significantly, within s 1041I itself, a distinction is drawn between the four provisions identified under s 1041I(1) as giving rise to civil actions whereas under s 1041I(1B)(a) it is only a claim made in respect of conduct done in contravention of s 1041H which attracts the contributory negligence provision. This same distinction is carried through to s 1041L(1). These support the narrow reach of s 1041L(1) to conduct done in contravention of s 1041H and not any other of the sections identified in s 1041I(1) .

1564. Nothing in s 1041L(1) turns on the use of the words "conduct that was done in a contravention of …". This merely picks up the same language used in s 1041I in respect of each of the four sections there expressly identified.

1565. **Following paragraph cited by:**

Williams v Pisano (29 June 2015) (Bathurst CJ, McColl and Emmett JJA)

There are evident policy considerations why the proportionate liability scheme is limited to claims for damages made under s 1041I for loss or damage caused by conduct in contravention of s 1041H . As we have explained, conduct done in contravention of any of ss 1041E, 1041F and 1041G , which are each expressly identified in s 1041I , constitutes an offence. That is not the case with conduct done in contravention of s 1041H . This alone provides sufficient reason to understand why s 1041L is confined to conduct done in contravention of s 1041H .

1566. Apportionment of a damages award meets the objective of confining the liability of concurrent wrongdoers to an amount reflecting that proportion of the damage or loss that the court considers just having regard to the defendant's responsibility for the damage or loss: s 1041N(1)(a). However, apportionment may work hardship on a successful applicant who finds one or more concurrent wrongdoers unable to meet their portion of the damages awarded.

1567. LGFS, S&P and ABN Amro submit that the explanatory material for the proportionate liability regime evidences no legislative intention to exclude s 1041E from the operation of the proportionate liability regime. Rather, they contend, the explanatory material indicates that the only class of conduct that the legislature intended to exclude from the operation of the proportionate liability regime was "intentional torts and claims involving fraud" (see *Explanatory Memorandum to the Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Bill 2003* (Cth) at [5.352]) and that this exclusion of such claims was expressly given effect by s 1041M(1) of the *Corporations Act* .

1568. The aim evidently is to exclude conduct involving particular moral culpability. Certainly s 1041M(1) reflects this objective. Likewise, ss 1041I(1B)(a) and 1041L(1) exclude from the benefit of contributory negligence and proportionate liability those concurrent wrongdoers who contravene the offence provisions, ss 1041E, 1041F and 1041G , with their attendant mental elements of moral culpability.

1569. Contravention of any of those provisions constitutes an offence. Section 1041E concerns the making of a statement or disseminating information that is false in a material particular or is materially misleading in circumstances when the offending person does not care whether the statement or information is true or false, or the person has actual or putative knowledge of those matters. Section 1041F contains elements of knowing or reckless conduct which is misleading, false or deceptive. Section 1041G involves dishonest conduct. Legislative policy points to conduct which, under Div 2, constitutes an offence being excluded from the proportionate liability regime and, in our opinion, s 1041L(1) and also s 1041I(1B)(a) upon our construction achieve that end.

1570. Section 1041H , by contrast, contains no necessary element of knowledge or dishonesty. It does not require proof of a mental element: *Australian Securities and Investments Commission v Stone Assets Management Pty Ltd* (2012) 205 FCR 120 at 129 [33] and [36] . A person may innocently contravene the proscription against engaging in conduct in relation to a financial product or a financial service that is misleading or deceptive or likely to mislead or deceive.

1571. LGFS, S&P and ABN Amro submit that the words "conduct that was done in a contravention of section 1041H " should be given their plain meaning: that is, as including any conduct that contravenes s 1041H (even if it also contravenes another provision, such as s 1041E). They contend that the evident purpose behind s 1041L(1) was to include all conduct that meets the description of conduct that is "misleading or deceptive or is likely to mislead or deceive" (s 1041H(1)) unless the conduct is expressly excluded. For example, s 1041M excludes from the scope of Div 2A a concurrent wrongdoer who intended to cause or fraudulently caused the economic loss or damage and s 1041H(3) excludes from the scope of s 1041H conduct contravening certain other provisions. They submit that if it were intended that s 1041L exclude conduct that contravenes s 1041E that could have been expressly stated.

1572. We do not agree. The reason for the excision of these sections from the reach of s 1041H was explained by Lander J in *Selig v Wealthsure Pty Ltd* (2013) 94 ACSR 308 at 453 [1089] -[1091] . We respectfully agree with his Honour's analysis and conclusions.

> [1089] Specifically, however, s 1041H(3) provides that conduct that contravenes s 670A (misleading or deceptive takeover document) or s 728 (misleading or deceptive fundraising document) or conduct in relation to a disclosure document or statement within the meaning of s 953A or conduct in relation to a disclosure document or statement within the meaning of s 1022A is not conduct that contravenes s 1041H .
>
> [1090] The reason why conduct of the kind mentioned in s 1041H(3) is not conduct which s 1041H(1) proscribes is because each of those sections have their own section that provides for a remedy for contraventions, independently of s 1041H . Section 670B provides a remedy for a contravention of s 670A against the persons mentioned in the table to s 670B(1). A remedy is given for a contravention of s 728 by s 729, but only as against the persons mentioned in the table in s 729(1). The remedy for

failing to comply with s 953B(1)(b) is given by s 953B(2) but only against the persons mentioned in s 953B(3). The remedy for failing to comply with s 1022B(1) is given by s 1022B(2) but only against the persons mentioned in s 1022B(3). A person who suffers damage as a result of a contravention of any of ss 670A, 728, 953B(1) and 1022B(1) is given a remedy, but only against the persons mentioned in the sections giving the remedies.

[1091] There is no need for s 1041H to proscribe the conduct contemplated in ss 670A, 728, 953B(1) and 1022B(1) because that conduct is already proscribed and the persons who suffer damage already have a statutory remedy, although only against the particular persons who are identified in the sections giving the remedy. Because these sections target particular persons, it would be inappropriate to proscribe that conduct in general terms because it would apply to any person who has engaged in the proscribed conduct.

1573. **Following paragraph cited by:**

Rivercity Motorway Finance Pty Limited (Administrators Appointed) (Receivers and Managers Appointed) v AECOM Australia Pty Ltd (No 2) (18 July 2014) (Nicholas J)
McGraw-Hill Financial Inc v City of Swan (24 June 2014) (Jacobson J)

While amendments were introduced to s 1041H(3) in July 2013, the provision in this case is the same as it was in the case before Lander J. These aspects of the decision of Lander J were overturned on appeal, by majority (Mansfield and Besanko JJ): *Wealthsure Pty Ltd v Selig* [2014] FCAFC 64. With respect to Mansfield and Besanko JJ, for the reasons just stated we agree with the conclusion reached by White J in *Wealthsure* on appeal that the expression in s 1041L that “the claim for the loss and damage is based on more than one cause of action (whether or not of the same or a different kind)” refers only to causes of action which are themselves apportionable claims.

1574. Indeed s 1041M is consistent with these policy considerations underpinning the construction we have given to s 1041L. As we have observed, s 1041M expressly excludes the liability of a concurrent wrongdoer in proceedings involving an apportionable claim if that concurrent wrongdoer intended to cause the economic loss or damage to property that is the subject of the claim or where the concurrent wrongdoer fraudulently caused the economic loss or damage to property that is the subject of the claim. Thus, as we earlier explained, even a claim made under s 1041I for loss or damage caused by conduct in contravention of s 1041H rendering it an apportionable claim may not result in an apportionment of liability where the provisions of s 1041M are applicable.

1575. **Following paragraph cited by:**

Rivercity Motorway Finance Pty Limited (Administrators Appointed) (Receivers and Managers Appointed) v AECOM Australia Pty Ltd (No 2) (18 July 2014) (Nicholas J)

> 71. In *ABN AMRO* the Full Court drew attention at [1575] to significant differences between relevant provisions of the Corporations Act and the NSW Act. There are, for example, significant differences between s 1041L(1) of the Corporations Act and s 34(1) of the NSW Act. There are also significant differences between s 87CB(1) of the TPA and s 34(1) of the NSW Act. However, none of these differences provide any sound basis for distinguishing *Reinhold* when it comes to determining the amount for which judgment may be given against the defendant in accordance with s 87CD(1) of the TPA.

The cases involving State legislation such as *Reinhold* and *Godfrey Spowers* take a different approach, but that is because of the significant textual and contextual differences in the apportionment provisions of that legislation from that found in the *Corporations Act*, the *ASIC Act* and other Commonwealth legislation.

1576. It is of assistance to consider the proportionate liability regimes under the *ASIC Act* as well as the *Competition and Consumer Act*. As we will explain, they have adopted, in substance, the same framework, although with some structural differences, as that found in the *Corporations Act*.

1577. The proportionate liability provisions under Subdiv GA in Pt 2, Div 2 of the *ASIC Act* apply to actions for damages made under s 12GF for economic loss or damage to property, which covers conduct of a wide range, the subject of discrete sections (Subdiv C, ss 12CA to 12CC and Subdiv D, ss 12DA to 12DN): s 12GP of the *ASIC Act*.

1578. However, as under the *Corporations Act*, the proportionate liability provisions are confined under s 12GP to claims referrable to conduct done in contravention of the general misleading and deceptive conduct provision – s 12DA. Contravention of s 12DA, unlike contravention of other provisions in Subdivs C and D, does not require any unconscionability, and is neither an offence nor capable of attracting the imposition of pecuniary penalties: ss 12GB and 12GBA of the *ASIC Act*.

1579. Such is the same in relation to the *Competition and Consumer Act*, which provides for the application of proportionate liability under Pt VIA, s 87CB to claims for damages under s 236 of the Australian Consumer Law (**ACL**). Section 236 provides that a claimant may recover damages if he or she has suffered loss or damage because of conduct in contravention of a provision of Ch 2 or 3 of the ACL, which covers a wide range of conduct.

1580. However, again, as under the *Corporations Act*, the proportionate liability provisions are confined under s 87CB to claims referrable to conduct in contravention of but one provision – here, s 18 of the ACL, which again is the general misleading and deceptive conduct provision. This provision, unlike the majority of the other provisions in Chs 2 and 3 (other exceptions being, for example, ss 85, 96(2), 132A), is neither capable of attracting the imposition of a pecuniary penalty under s 224(1) for contravention, nor requires proof of the unconscionability of the conduct to establish contravention. While offences are dealt with in a separate chapter, s 225 contemplates that conduct which may attract a pecuniary penalty under s 224(1) may also constitute an offence and prevents "double punishment" of such conduct. The general misleading and deceptive conduct provision (s 18) is not included in s 224(1), and is thus distinguished from conduct marked by the statute as worthy of punishment.

1581. Section 87CC of the *Competition and Consumer Act* and s 12GQ of the *ASIC Act* are also very similar to s 1041M of the *Corporations Act* , and their inclusion is consistent with an approach excluding deliberate wrongdoing or unconscionable behaviour from the benefit of the proportionate liability regime. Under s 87CC and s 12GQ , concurrent wrongdoers who intended to cause the economic loss or damage to property or who fraudulently caused the loss or damage are excluded from the proportionate liability provisions.

1582. Provision for damages under s 12GF of the *ASIC Act* is also similar to the *Corporations Act* in that s 12GF , as with s 1041I of the *Corporations Act* , provides that damages are available for contravention of a range of provisions, but also contains subs (1B) dealing with contributory negligence, in which it is stipulated that damages for economic loss or damage to property caused by conduct in contravention of s 12DA (the generic misleading and deceptive conduct provision) are to be reduced to the extent the court thinks just and equitable having regard to the claimant's share in the responsibility.

1583. Section 137B of the *Competition and Consumer Act* provides for a reduction in the amount of damages recoverable in circumstances of contributory negligence where a claim is made under s 236(1) of the ACL in relation to economic loss or damage to property as a result of the defendant's conduct in contravention of s 18 of the ACL.

1584. **Following paragraph cited by:**

Ramadan v ACN 098 408 176 Pty Ltd (31 August 2023) (Livesey P; Doyle and Bleby JJ)

Nothing stated by Middleton J in *Dartberg* is contrary to the views we have expressed as to the meaning and effect of the proportionate liability provisions in the *Corporations Act* . Indee d, when referring to these in passing at 456-457 [18]-[19] his Honour appears to have accepted, as we do, that the regime applies to causes of action pleaded. This gives meaning to the words "claim for damages made" found in s 1041L(1). This is to be distinguished from his Honour's analysis of Pt VIAA of the *Wrongs Act* , which was relevantly involved. As was observed by Middleton J at 458 [29]-[31]:

> [29] As the respondents observed, in drafting the provisions of Pt VIAA of the *Wrongs Act* , the legislature deliberately chose to define "apportionable claim" by reference to an action for damages arising from a failure to take reasonable care. The provisions do not require that the claim itself be a claim in negligence or for a breach of duty - it only requires that the claim arise from a failure to take reasonable care. The expressions "arising from" or "arising out of" are of wide import - see the discussion in Stephenson A, "Proportional Liability in Australia - The Death of Certainty

in Risk Allocation in Contract" (2005) 22(1) ICLR 64 at 71–73, and generally McDonald B, "Proportionate Liability in Australia: the Devil in the Detail" (2005) 26(1) ABR 29.

[30] In my view, Pt IVAA could apply in the circumstances of this proceeding according to its own terms. Where a claim brought by an applicant does not have as one of its necessary elements any allegation of failing to take reasonable care, an additional enquiry into the failure to take reasonable care may become relevant in the course of a trial to determine the application of Pt IVAA. Even though the claims in this proceeding themselves do not rely upon any plea of negligence or a "failure to take reasonable care" in a strict sense, a failure to take reasonable care may form part of the allegations or the evidence that is tendered in the proceedings. At the end of the trial, after hearing all the evidence, it may be found that Pt IVAA applies.

[31] In these circumstances, where a respondent desires to rely upon Pt IVAA of the *Wrongs Act* , it will need to plead and prove each of the statutory elements, including the failure to take reasonable care. In a proceeding where the applicant does not rely upon any such failure, then the need for a particularised plea by a respondent may be particularly important for the proper case management of the proceedings: see eg *Ucak v Avante Developments Pty Ltd* [2007] NSWSC 367 at [41] . It would be desirable at an early stage of proceedings for a respondent to put forward the facts upon which it relies in support of the allocation of responsibility it contends should be ordered. If a respondent calls in aid the benefit of the limitation on liability provided for in Pt IVAA of the *Wrongs Act* , then the respondent has the onus of pleading and proving the required elements. The court, after hearing all the evidence, will then need to determine, as a matter of fact, whether the relevant claim brought by the applicant is a claim arising from a failure to take reasonable care.

1585. These observations concerning the *Wrongs Act* have no application to the relevant provisions of the *Corporations Act* or the other Commonwealth legislation we have considered.

1586. **Following paragraph cited by:**

Latteria Holdings Pty Ltd v Corcoran Parker Pty Ltd (No 2) (19 December 2014) (Mortimer J)

Finkelstein J, correctly in our view, when considering the proportionate liability scheme under Pt VIA of the then TPA in *BHPB Freight Pty Ltd v Cosco Oceania Chartering Pty Ltd (No 2)* [2008] FCA 1656, accepted that an "apportionable claim" was limited to one brought for damages pursuant to s 82 TPA for a contravention of s 52. This reflects the confined language of s 87CB(1) of the TPA in the same vein as s 1041L of the *Corporations Act* limits an apportionable claim to one made under s 1041I for conduct in contravention of s 1041H .

1587. Likewise, Lander J in *Selig* (at 445 [1045]) concluded in relation to s 1041I(1B) (the contributory negligence provision) that it had been deliberately drawn to only apply to a claim made under s 1041H and that the other sections, including s 1041E , for which s 1041I provides a statutory cause of action, had been deliberately omitted in a consideration of s 1041I(1B) . We respectfully agree. His Honour, unsurprisingly, came to the same view concerning Div 2A . In that respect, he stated (at 452 [1084]) that this division only applies where there has been a contravention of s 1041H and has no application where the plaintiffs have succeeded on other statutory and common law causes of action. Again we agree.

1588. It follows that the primary judge erred in applying *Reinhold.* For the same reasons we do not consider that *Godfrey Spowers* assists the proper construction of s 1041L.

1589. **Following paragraph cited by:**

In the matter of Mediation & Online Dispute Resolution Operating Network Pty Ltd (23 February 2022) (Rees J)

Accordingly, in our opinion, the omission of s 1041E from the definition of apportionable claims in s 1041L reflects the legislature's intention that conduct prohibited by s 1041E , the making of a false or misleading statement or dissemination of information which the person knows or ought to have known is false or misleading, or otherwise does not care whether the statement or information is true or false, should be treated differently to conduct contravening s 1041H . Liability under s 1041H , as we have explained, may arise even where the conduct is innocent and there is no allegation that the defendant knew or ought to have known that the conduct it engaged in was misleading or deceptive. By contrast, s 1041E imposes a mental requirement of involving actual or constructive knowledge or recklessness. The legislature has deliberately excluded defendants whose conduct contravenes s 1041E from having the benefit of apportionment provided for by s 1041N. For the same reasons, the legislature also excluded contraventions of s 1041F and s 1041G from the definition of apportionable claims.

1590. It also follows, for the same reason, that only claims made under s 1041I in respect of conduct in contravention of s 1041H may be subject to the contributory negligence provisions under s 1041I(1B) . Furthermore, as we mentioned at the outset, these conclusions apply, *mutatis mutandis*, to the relevant provisions of the *ASIC Act* .

3.6.1 What facts established contraventions of s 1041E and s 1041H

1591. The primary judge expressly accepted that the proportionate liability provisions in ss 1041L-1041S do not apply to a finding of conduct done in contravention of s 1041E : J[2124] and J[3485]. However, at J[3485] her Honour was persuaded by LGFS' submission that the s 1041E claims arose from the same facts as the contraventions of s 1041H which are apportionable. LGFS relied on what Barrett J had said in *Reinhold* to suggest that because the s 1041E cause of action "arises from the same facts and relates to the same loss as the s 1041H cause of action" then it too is apportionable. This same path of reasoning was followed in relation to the findings of contravention of s 1041E and s 1041H as against each of ABN Amro and S&P. In so doing her Honour was led into error.

1592. It is not correct to say that the s 1041E claims arose from the same facts as the contraventions of s 1041H . The latter claims, as we have explained, do not require proof of the mental elements which are the subject of s 1041E namely, that the person (defendant) when they made the statement or disseminated the information either did not care whether the statement or information was true or false, or alternatively, the person knew or ought reasonably to have known that the statement or information was false in a material particular or was materially misleading. Those additional facts were pleaded by the PA Councils in their statement of claim as against the cross-respondents, as we will shortly explain.

1593. In the same vein, use of language such as "arises from the same facts" is not apt in the present case. It no doubt emanated from the language of s 34(1)(a) of the *Civil Liability Act* – "claim … in an action for damages…arising from a failure to take reasonable care …". However, for reasons we have explained, the language of s 1041L and its statutory context are materially distinguishable from the *Civil Liability Act* which was the subject of the decision in *Reinhold* .

1594. **Following paragraph cited by:**

Davis v Wilson (21 February 2025) (Shariff J)

The facts required to be established to make out a breach of s 1041H may form part of those necessary to prove a claim under s 1041E . However, to make good a claim in respect of conduct done in contravention of s 1041H it would not be necessary to plead or to prove that the statement or information was "false in a material particular" or "materially misleading" or that when that person made the statement or disseminated the information they did not care whether the statement or information was true or false or that they knew or ought reasonably to have known that the statement or information was false in a material particular or is materially misleading: s 1041E . In other words, to make out a contravention of s 1041H will ordinarily require fewer facts to be established than in a case founded on contravention of s 1041E and such was the case here.

1595. Section 1041L identifies what is an apportionable claim. Such a claim as we have observed is one "made under section 1041I " for loss or damage "caused by conduct that was done in a contravention of section 1041H ". It is important then to see just what claims were made by the PA Councils as against each of LGFS, S&P and ABN Amro.

1596. This requires consideration as to the way the PA Councils pleaded their cases against each of LGFS, S&P and ABN Amro.

1597. At statement of claim (**SOC**) [93]-[94] there are rolled up allegations of conduct by LGFS in contravention of ss 1041E and 1041H of the *Corporations Act* as well as s 12DA of the *ASIC*

Act . The material facts pleaded with particulars alleged, again in a rolled up fashion, that LGFS made statements that were false in a material particular and materially misleading, for example SOC [94.5], and that LGFS knew or should have known certain things.

1598. However, at SOC [94B] the allegations concerning each of the pleaded misrepresentations are expressed in the language of s 1041E and said to be in contravention of only that provision. Se ction 1041H is not there pleaded.

1599. In the alternative at SOC [95] there is pleaded certain disclosure failures on the part of LGFS which it is alleged LGFS must have known were relevant to the PA Councils' assessment of the investment. This was said to be in contravention of s 1041H . Of course, there was no need to prove such alleged knowledge to make out a contravention of s 1041H . Proof of the failure to disclose would be enough.

1600. The same allegations were alleged to be in contravention of s 1041E using the language of that provision. Those allegations were irrelevant to a case founded on conduct in contravention of s 1041H .

1601. The separation of the facts pleaded as against S&P is clearer. At SOC [121], broadly, it is alleged that S&P engaged in conduct in contravention of s 12DA of the *ASIC Act* and s 1041H of the *Corporations Act* by communicating to the PA Councils that the Rembrandt notes were AAA rated.

1602. At SOC [122] the very same allegations of fact are made in support of the allegations of contravention of s 1041E but then *additionally*, relevantly, it is pleaded that the circumstances set out under SOC [113] constituted the making of a statement and/or the disseminating of information that was materially misleading and it was likely to induce persons in Australia to apply for or acquire Rembrandt notes in circumstances where S&P ought reasonably to have known that the statement or information was materially misleading. These additions were necessary factual allegations for establishing a contravention of s 1041E but not, as the pleader understood, necessary for the case, pleaded at SOC [121], based on a contravention of s 1041H .

1603. The very same distinction as between s 12DA of the *ASIC Act* and s 1041H of the *Corporation s Act* on the one hand and s 1041E of the *Corporations Act* on the other, is drawn in the pleading against ABN Amro at SOC [134]-[135].

1604. It is convenient then to consider the relevant findings of contravention of provisions of the *Cor porations Act* in relation to each of LGFS, S&P and ABN Amro and how these respond to the construction we have given to the proportionate liability provisions.

1605. LGFS was found to have contravened s 1041H and, to a limited extent, also s 1041E . The latter contravention was causative, even if not solely, of the PA Councils acquiring the CPDOs. As the primary judge stated the statements made to Corowa, Orange, Moree, Oberon, Deniliquin, Murray, Cooma, Narromine and Ryde were false in a material particular and materially misleading and likely to induce those Councils into acquiring the product and were intended by LGFS to do so: J[2238]. Those findings by her Honour were not necessary to make out the s 1041H contravention. However, the reasons for judgment do not distinguish the facts in this way.

1606. The findings against S&P and ABN Amro in favour of the PA Councils was that their conduct contravened s 1041E as well as s 1041H : J[3339]. Again, the findings supporting the contraventions of each provision were not the subject of discrete findings by the primary judge.

1607. However, findings of contravention in relation to s 1041E and s 1041H should properly be tied to the facts relied on in the pleadings. This is necessary in order to establish just what conduct was done in contravention of each section. This has implications for a proper assessment of proportionate liability should it arise. Once this is done, it becomes apparent that the facts sustaining the contravention of each provision could not be the same.

3.6.2 Joint and several or apportioned damages awards

1608. To the extent that each of LGFS, ABN Amro and S&P were concurrent wrongdoers in the claims for economic loss suffered by the PA Councils caused by their respective conduct in contravention of s 1041H , those fell to be treated as apportionable claims and to be determined in accordance with the provisions of Div 2A : s 1041N(2)(a). To the extent that they were each found liable for the same economic loss caused by their conduct in contravention of s 1041E these were not apportionable claims. Under s 1041N(2) the former are to be determined in accordance with the provisions of Div 2A and the non-apportionable claims are to be determined in accordance with the legal rules that, apart from Div 2A , are relevant.

1609. That being so the PA Councils in relation to their claims for damages for economic loss would be entitled to joint and several judgments against each cross-respondent in respect of the damages flowing from their conduct in contravention of s 1041E and for judgments involving apportionment, as provided for in s 1041N(1), in respect of the conduct done in contravention of s 1041H . The contraventions of s 1041E cannot be ignored, which, in effect, is what the primary judge did.

1610. Whilst the damages assessed in respect of each cause of action would be in the same amount, by reason of the proportionate liability provisions and to that extent, the damages remedies for these two separate causes of action brought pursuant to s 1041I are mutually inconsistent. This entitles the PA Councils to elect the remedy they want. Self-evidently, by bringing this cross-appeal they have made their election clear: that available for making out their cause of action based in the contraventions of s 1041E .

1611. Accordingly, ABN Amro and S&P will each be liable for 100% of the PA Councils' losses for the conduct they engaged in in contravention of s 1041E . LGFS will be liable for 100% of the losses caused to Cooma, Corowa, Deniliquin, Moree, Murray, Narromine, Oberon, Orange and Ryde to whom it represented that the Rembrandt notes were tailored for local councils, that being the conduct that the primary judge found was a contravention of s 1041E .

4. PRE-JUDGMENT INTEREST

1612. These issues were addressed by the primary judge in a separate judgment dated 1 March 2013 (the **March Judgment**): [2013] FCA 144 . The primary judge found that the Councils and LGFS were entitled to pre-judgment interest on their assessed damages at the rate of 4% above the cash rate last published by the Reserve Bank of Australia as set out in Practice Note CM16 – Pre-judgment Interest.

1613. ABN Amro, S&P and LGFS appealed these findings. ABN abandoned its Appeal Grounds: ABN Appeal Grounds Matrix Rows 96-98B. S&P maintained its Appeal Grounds: S&P Appeal Grounds Matrix Rows 57, 57A and 57B. However, these Appeal Grounds do not arise because they were consequential on S&P succeeding in its other Appeal Grounds. None of those Appeal Grounds were upheld.

1614. LGFS' Appeal Ground was consequential on the Appeal Grounds of ABN Amro and S&P succeeding: LGFS Appeal Grounds Matrix Row 121. ABN Amro abandoned its relevant Appeal Grounds and S&P's Appeal Grounds were dismissed. This Appeal Ground therefore fails.

5. COSTS

1615. In the March Judgment, the primary judge made various costs orders. ABN Amro and S&P appealed against some of those orders.

1616. ABN Amro appealed the finding that LGFS' costs of defending StateCover's claims were recoverable against ABN Amro: ABN Amro Appeal Grounds Matrix Row 98C. This Appeal Ground was consequential on ABN Amro succeeding in its Appeal Grounds in the StateCover Proceedings in relation to equitable contribution. Those Appeal Grounds failed. Therefore, this Appeal Ground also fails.

1617. S&P appealed the findings that it was liable to pay the Councils' costs and LGFS' costs: S&P Appeal Grounds Matrix Rows 58 and 58A. Again, these Appeal Grounds do not arise because they were consequential on S&P succeeding in its other Appeal Grounds, which have been dismissed.

PART 14: INSURANCE ISSUES – APPEALS BY AHAC AGAINST LGFS

1. INTRODUCTION

1618. AHAC relevantly insured LGFS for the period 30 June 2007 to 30 June 2008 under a claims notified contract of insurance entered into on 31 August 2007 (**Insurance Contract**): J [3537]. AHAC denied liability under the Insurance Contract.

1619. The policyholder under the Insurance Contract is FuturePlus. The "Insured", relevantly, is defined to mean the policyholder and the policyholder's subsidiaries existing at the inception of the policy period, noted under Endorsement Number 12 as including LGFS.

1620. LGFS in its cross-claim against AHAC alleged that LGFS was entitled to indemnity from AHAC in respect of LGFS' liability to StateCover and the Councils under the Insurance Contract. AHAC had denied cover to LGFS primarily on the basis of it failing to comply with its alleged duty of disclosure under s 21 of the *Insurance Contracts Act 1984* (Cth) (the **ICA**). AHAC contended that before entry into the Insurance Contract LGFS knew that its AFSL did not permit LGFS to deal in or give advice in respect of derivatives, that the Rembrandt notes were or might have been derivatives, and that no compliance procedures of LGFS or FuturePlus had been invoked to attempt to determine whether the Rembrandt notes were or might have been derivatives. AHAC had contended that LGFS knew that these matters were relevant to the decision of AHAC whether to accept the insurance risk in relation to LGFS and that LGFS did not disclose them. Alternatively, AHAC's case was that a reasonable person in the circumstances could be expected to know that the matters were so relevant.

1621. The primary judge held AHAC liable to indemnify LGFS.

1622. The issues raised by AHAC's appeal are as follows.

1623. First, AHAC claims that its liability was reduced to nil by s 28 of the ICA because of a non-disclosure by LGFS, in breach of the duty created by s 21 of the ICA : AHAC Appeal Grounds Matrix Rows 1-6.

1624. Second, AHAC relies on the exclusions in Endorsements 16 and 17 and, in relation to StateCover, cl 3.3 of the Insurance Contract. The primary judge held none of the exclusions applied.

1625. Third, AHAC contends that the settlement of StateCover's claim against LGFS, for which the primary judge held AHAC was liable to indemnify LGFS, was not reasonable.

1626. However, there are two threshold issues which arise on LGFS' notice of contention. LGFS contends that it did not owe any such duty of disclosure. LGFS also contends that even if there was a duty, the non-disclosure case fails at the outset if its AFSL authorised it to sell and advise in relation to the Rembrandt notes, which turns on whether the Rembrandt notes were "debentures" as defined by s 9 of the *Corporations Act* . LGFS contends that the primary judge should have held that the Rembrandt notes were "debentures". We will deal with these two issues first.

2. LGFS' NOTICE OF CONTENTION

2.1 Did LGFS owe the s 21 of the ICA duty of disclosure?: LGFS Appeal Grounds Matrix Row 125 and AHAC Appeal Grounds Matrix Row 24

1627. LGFS had argued successfully that it was not a party to the Insurance Contract: J[3614]-J[3620]. AHAC submits that this argument was not open to LGFS because it had not been raised by the LGFS pleading, and that the primary judge should not have permitted it to be advanced. We agree with the reasons of the primary judge as to this pleading point set out at J[3614]-J[3615]. There is no need to repeat these.

1628. AHAC submits that LGFS was a "party" to the Insurance Contract because FuturePlus acted as its agent. We do not agree. The evidence does not support a conclusion that FuturePlus was acting in the negotiation for, and entry into, the Insurance Contract as agent for LGFS or any of its other subsidiaries. Rather, it acted as principal and was the contracting party. By definition, under the Insurance Contract, LGFS was one of the "Insured". It thus was a beneficiary under the Insurance Contract but contractually so, not as a party by operation of the law of agency. Additionally, although not a party, it had, as we will explain, a right to recovery under the Insurance Contract, pursuant to s 48 of the ICA .

1629. Section 48 of the ICA provides that a person who is not a party to the contract but is specified or referred to in the contract, relevantly here, by name, as a person to whom the insurance cover under the contract extends, has a right of recovery under the contract. Endorsement Number 12 is in terms that "[i]t is hereby noted and agreed that the following Subsidiaries shall be included in this policy". Only FuturePlus completed a proposal form for the insurance cover. The Insurance Contract was made between AHAC and FuturePlus. They are the "parties" to the Insurance Contract. That, by definition, LGFS is an "Insured Entity" and therefore one of the "Insured" does not affect this result. A party to a contract of insurance, depending on the particular kind of policy, need not necessarily be an insured person under it. Likewise an insured person need not be a party, as is the case here in relation to LGFS.

1630. Nonetheless, the primary judge held that LGFS owed a duty of disclosure to AHAC under s 21 of the ICA by virtue of ss 48(2) and (3) of that Act: J[3620]. LGFS challenges this conclusion. It submits that the term "insured" in s 21 means an insured who is a party to the contract, not an insured who is not a party to the contract, and that the s 21 duty of disclosure did not extend to it, a conclusion unaffected by s 48(3) of the ICA . LGFS relies on the reasons of Clarke JA (Meagher JA agreeing) in *CE Heath Casualty & General Insurance Ltd v Grey* (1993) 32 NSWLR 25 at 46. Accordingly, LGFS submits that it did not owe a duty of disclosure, and that the non-disclosure case fails as the statutory basis is not enlivened.

2.2 Discussion

1631. Section 11 of the ICA provides that:

> ***insured*** and ***insurer*** include a proposed insured and a proposed insurer, respectively.

1632. Section 21 of the ICA relevantly for this purpose provides:

> **The insured's duty of disclosure**
>
> (1) Subject to this Act, an insured has a duty to disclose to the insurer, before the relevant contract of insurance is entered into, every matter that is known to the insured, being a matter that:
>
> (a) the insured knows to be a matter relevant to the decision of the insurer whether to accept the risk and, if so, on what terms; or
>
> (b) a reasonable person in the circumstances could be expected to know to be a matter so relevant.

1633. Section 48 provides:

> **Entitlement of named persons to claim**
>
> (1) Where a person who is not a party to a contract of general insurance is specified or referred to in the contract, whether by name or otherwise, as a person to whom the insurance cover provided by the contract extends, that person has a right to recover the amount of the person's loss from the insurer in accordance with the contract notwithstanding that the person is not a party to the contract.
>
> (2) Subject to the contract, a person who has such a right:

(a) has, in relation to the person's claim, the same obligations to the insurer as the person would have if the person were the insured; and

(b) may discharge the insured's obligations in relation to the loss.

(3) The insurer has the same defences to an action under this section as the insurer would have in an action by the insured.

1634. Whilst *obiter*, we, nonetheless, respectfully agree with the general observations of Clarke JA in *Grey* at 45-46 that the ICA in using the words "insurer" and "insured" is speaking to the parties to the contract and that there is a clear dichotomy between a party and a person who is not a party but who is entitled to benefit under the policy. That said, it needs to be borne in mind that "insured" and "insurer" includes, by definition, a "proposed insured" and a "proposed insurer". Thus, "insured" under s 21 , which provides for the pre-contractual duty of disclosure, has the extended meaning of "proposed insured". The "insured" in s 48 is the insured who is the party to the contract.

1635. This dichotomy is particularly evident when s 48 of the ICA is considered, where the distinction is drawn between, on the one hand, a "person who is not a party to a contract" who is, relevantly, named as a person to whom the insurance cover provided by the contract extends and, on the other hand, the "insured". .

1636. We do not think that the use of the word "insured" in s 21 of the ICA rather than "party to the contract of insurance" affects this conclusion. This is so because when the duty of disclosure under s 21 arises and endures there are no parties to a contract of insurance. No such contract has been entered into. In s 21 "the insured" having the duty of disclosure "before the relevant contract of insurance is entered into" means, as defined, the "proposed insured" who is proposing to enter into a contract of insurance with the insurer, meaning, as defined, the "proposed insurer". This description fits FuturePlus as the insured but not LGFS.

1637. There would be no need for Endorsement Number 12 if LGFS and the other subsidiaries were parties to the Insurance Contract. The agreement noted in the preface to Endorsement Number 12 that the subsidiaries "shall be included in this policy" is an agreement reached between AHAC and FuturePlus. The expression "shall be included in this policy" meets the statutory description in s 48(1) of the ICA of, relevantly, a person who is not a party to the contract specified by name as a person to whom the insurance cover provided by the contract extends.

1638. It matters not that LGFS was, by definition, under the Insurance Contract, one of the "insured". We are concerned with the meaning of "insured" on the proper construction of the I CA , not the Insurance Contract.

1639. Section 48(2) imposes on the person who is not a party to the contract, but who has a right of recovery, the same obligations to the insurer as the person would have if the person were the insured. In a similar vein, under s 48(3) the insurer has the same defences to an action under s 48 as the insurer would have had in an action by the insured.

1640. It was upon this basis that the primary judge concluded that LGFS was placed in the same position as FuturePlus and subject to the same duties of disclosure as FuturePlus. This was an implicit reference to the s 21 duties of disclosure.

1641. We have reached a different conclusion. Section 48(2) confines the person's obligations to those which are "in relation to the person's claim". We do not regard this as referrable to the pre-contractual obligations of FuturePlus under s 21 of the ICA .

1642. The distinction has important ramifications, not only in relation to identifying who it is that owes the s 21 duty of disclosure, but also in identifying the remedies available to the insurer under the ICA for non-disclosure. The insurer has no other remedies outside of the ICA in relation to a failure by the insured to disclose a matter to the insurer before the contract was entered into: s 33.

1643. We would adopt, respectfully, what Clarke JA stated in *Grey* at 46:

> Accordingly where s 21 speaks of the duty of an insured to disclose the matters set out in s 21(1) it is talking about the party who proposes to enter into a contract of insurance in the context of those provisions in the Act which spell out the consequences of the failure by a person who has entered into the contract to comply with that duty. A similar approach is taken in those sections which deal with misrepresentation.
>
> The remedies offered to an insurer where an insured fails to comply with the duty of disclosure, or makes a misrepresentation before entering into the contract, are contained in s 28 . Broadly, if the failure was fraudulent or the misrepresentation was made fraudulently the insurer may avoid the contract, that is, avoid it from its inception (s 28 (2); s 11(1)) . If the failure or misrepresentation was not fraudulent there is no right to avoid the contract but the liability of the insurer may be reduced under s 28(3) . Further s 31 empowers the court in the circumstances set out there to disregard the avoidance but only in "proceedings by the insured", and s 33 provides that Div 3 of Pt IV (ss 28-33) is, in effect, a code.
>
> What is clear from these provisions is that the obligation to disclose, and not to make misrepresentations, is cast upon a person intending to enter into a contract of insurance and the consequences of non-compliance are visited only upon persons who actually enter into such a contract. What is of greater importance is the fact that there is no obligation to disclose, or not misrepresent, before a contract is entered into, imposed upon a person entitled to recover the amount of a loss pursuant to s 48(1) . Nothing in s 28 provides that anything he or she does, or fails to do, before the contract is concluded in any way disentitles him or her from successfully maintaining a claim.

1644. **Following paragraph cited by:**

Montclare v Metlife Insurance Ltd (25 June 2015) (Ginnane J)

> We do not think it was intended that where a non-party who is, under the contract, defined as one of the insured failed, fraudulently, to comply with the duty of disclosure under s 21 , this could result in the avoidance of the contract between the insurer and the innocent insured, the other party to the contract.

1645. Nothing in *Advance (NSW) Insurance Agencies Pty Limited v Matthews* (1989) 166 CLR 606 at 616 detracts from these conclusions. We agree with the observation of the primary judge at J [3574] that *Matthews* relates to a question of duty of disclosure where there is more than one insured who is a party to the contract of insurance and not, as here, an insured who is not a party to the contract.

1646. AHAC contends that its construction of s 21 and s 48 removes the injustice which would exist if an entity which intended to be covered by a contract of insurance and knew of the existence of a duty of disclosure was relieved of the consequence of non-disclosure because, on a basis which might properly be described as technical, it did not become a party to the contract of insurance.

1647. We do not consider that this follows. In this case, AHAC, before entering into the Insurance Contract, knew which entities were to be covered by it including LGFS which it named as a subsidiary in Endorsement Number 12. It chose to deal only with FuturePlus as the putative policyholder or, in the language of the ICA , the "proposed insured". It could easily have required that all of the subsidiaries, including LGFS, which were intended to be covered become parties to the contract and therefore liable to the s 21 disclosure regime. It did not do so.

1648. Alternatively, it could have advanced a case before the primary judge that FuturePlus failed in its obligations to make full s 21 disclosure in relation, relevantly, to LGFS. No such case was advanced by AHAC.

1649. AHAC contends that its construction of s 48(3) would not have the effect of imposing an obligation of disclosure on entities which had no opportunity to consider the question of disclosure prior to the formation of the contract of insurance. This, it submits, is so because the duty of disclosure under s 21 is subject to the giving of a warning by the insurer as required by s 22. This, too, does not follow. The s 22 obligation required AHAC to give the notice to FuturePlus, the "insured" for the purposes of that provision, consistent with its meaning in ss 21, 28 , and 48, amongst others.

1650. Section 22 imposes an obligation on the insurer to inform the insured as to the general nature and effect of the duty of disclosure. Failure to give such notice deprives the insurer of exercising a right in respect of a failure to comply with the duty of disclosure, unless that failure was fraudulent.

1651. Those provisions are directed as between the parties to the contract and not, as here, LGFS, which as the primary judge correctly identified, draws its rights to recovery from s 48 .

1652. Accordingly, for these reasons, no duty under s 21 was imposed on LGFS.

2.3 Were the Rembrandt notes a debenture?: LGFS Appeal Grounds Matrix Row 123 and AHAC Appeal Grounds Matrix Row 23

1653. This issue was considered in Part 4 , Section 1.1.4.4 above and is dismissed for those reasons.

3. AHAC'S APPEALS

3.1 Did LGFS breach its s 21 duty of disclosure?: AHAC Appeal Grounds Matrix Rows 1, 2 and 3

1654. AHAC contends that, assuming that contrary to our finding there was a duty under s 121, the primary judge erred in finding that LGFS did not breach its duty of disclosure pursuant to s 21 (1) of the ICA : J[3621]-J[3630]. Section 21 of the ICA is set out at [1632] above.

1655. LGFS' AFLSs did not permit LGFS to deal in, including selling or giving advice in respect of, derivatives. The primary judge found that LGFS did advise councils to purchase the Rembrandt notes: J[2147]. Her Honour also found that LGFS dealt in the Rembrandt notes: J [2132].

1656. If the Rembrandt notes were derivatives and LGFS both dealt in them and advised in relation to them, it was in breach of its AFSL. The advice and the dealings took place before the entry into the Insurance Contract.

1657. AHAC did not allege directly that LGFS knew that it was not authorised to deal in or advise in relation to the Rembrandt notes. AHAC alleged that the "matter" under s 21(1) of the ICA w hich was known to LGFS and not disclosed comprised the following three alternatives. In each case one of the matters said to be known was that its AFSL did not permit it to advise about, or deal in, derivatives. First, that the Rembrandt notes were "derivatives". Second, that by reason of its knowledge of the terms and characteristics of the Rembrandt notes, that they "might well" be "derivatives". Third, that the effect of the terms of the Rembrandt notes was that their value varied by reference to variations in the value of the underlying credit default swap indices: J[3552]. Thus, on AHAC's case, as the primary judge observed at J[3553], with respect to each alternative the question was whether the combination of the existence of the licence limitation and the existence of the other matter were matters relevant to the decision of the insurer whether to accept the risk and, if so, on what terms.

1658. The primary judge found that LGFS knew that its AFSL did not permit it to deal in derivatives. However, as her Honour noted at J[3622], the starting point in this context was that the AFSLs authorised LGFS to deal in securities which included debentures. Thus the relevant issue for LGFS was always whether it was dealing in securities. If it was, then as the primary judge found, LGFS knew that its activities were authorised by its AFSL. Her Honour then concluded, correctly in our opinion, that LGFS' concern was to ensure that it dealt in securities so it would not have conceived of its responsibility as ensuring that the products it dealt with were not derivatives because, unless they were securities or another nominated exception, many products would satisfy the basic characteristics of a derivative.

1659. LGFS submits that there is no connection between each "matter" alleged to have been known and the terms of LGFS' AFSLs, which permit advice and dealings in "securities", because whether an instrument has the characteristics of a "derivative" says nothing about whether it is a "security". This is so because, as the primary judge correctly observed at J[3622], the AFSL authorised LGFS to deal in securities which included debentures and under the *Corporations Act* securities are an exception to the meaning of derivatives. We accept this submission.

1660. The primary judge found that Mr Hilder and Mr Tischler, the relevant minds of LGFS, did not know that the Rembrandt notes were derivatives and did not suspect that they were derivatives: J[3621]. The latter finding appears to be in response to the case of AHAC that Mr Hilder and Mr Tischler knew that the Rembrandt notes may well be derivatives because they had the characteristics of derivatives.

1661. In relation to the issue whether LGFS had breached s 912A(1) of the *Corporations Act* by failing to maintain necessary competence, her Honour said the following at J[2947]:

> … It is apparent from the evidence that LGFS simply never turned its mind to the question whether the product was a derivative or not when there were numerous indicators that should have alerted LGFS to this possibility. LGFS knew that the value of the Rembrandt notes varied by reference to the value of the underlying credit default swap indices which, of itself, should have raised the question of the legal character of the product in LGFS's mind, given that it knew that its AFSL did not authorise it to advise about or deal in derivatives. So too for the fact that LGFS knew that credit default swaps are themselves derivatives and that the product involved credit default swaps, albeit notional ones. Mr Tischler described the product as involving exposure to "credit derivatives" yet said he never turned his mind to the prospect that such a product was probably also a derivative and thus outside the scope of LGFS's AFSL. On these grounds it is difficult not to conclude that LGFS did not maintain the competence required to provide the financial services covered by its licence because it did not have the competence to realise when there was a real and obvious question about whether a product was covered by its licence at all.

1662. In a different context, her Honour said at J[3531]:

> Apart from these considerations I do not accept that LGFS knew that it was acting in breach of its AFSL when it marketed and sold the notes to the councils. This issue is resolved in the context of the dispute between LGFS and AHAC in LGFS's favour. LGFS ought to have known this to be so but it did not in fact know the Rembrandt CPDO notes were a derivative.

1663. Her Honour rejected the AHAC case regarding non-disclosure insofar as it concerned the actual knowledge of LGFS: J[3622]-J[3629]. AHAC submits that there are a number of flaws both in the fact-finding and regarding the approach her Honour took.

1664. AHAC's submissions on this point attempt to discredit the evidence of both Mr Tischler and Mr Hilder to a significant extent based on what AHAC contends they knew, should have known and what they should have done in assessing whether the Rembrandt notes were derivatives. However it was that each of them reasoned the question, even accepting that it was only Mr Hilder who, in terms, thought the Rembrandt notes were securities, the fact is each gave evidence that they did not consider that the Rembrandt notes were derivatives. Derivative here is used in the sense that it was not a security.

1665. The findings and observations of the primary judge concerning the attack made upon the credit of each of Mr Tischler and Mr Hilder are expressed in strong terms. Her Honour found as a fact "the proposition that LGFS knew that the Rembrandt notes were derivatives or suspected they were but deliberately refrained from finding out [is] fanciful": J[3621]. This finding refers inclusively to the Rembrandt 2006-3 notes. The third alternative "matter" is but a subset of the second. In a similar vein, her Honour considered that the attacks on their credibility should be given “short shrift”: J[3624]. Her Honour, in this respect, believed the evidence of Mr Hilder and Mr Tischler (at J[3621]-J[3622] and J[3624]-J[3628]), each of whom was cross-examined for a number of days. She had the well-known advantage of a trial judge and her finding is not “glaringly improbable”: *Fox v Percy* at 128 [29] , citing *Brunskill v Sovereign Marine & General Insurance Co Ltd* (1985) 62 ALR 53 at 57.

1666. AHAC’s submissions attribute to LGFS conduct which it characterises as either deliberately or recklessly in breach of the *Corporations Act* , and to Mr Hilder and Mr Tischler at least reckless conduct during 2006 and dishonesty when giving evidence. Section 140(2) of the *Evidence Act 1995* (Cth) applies. We accept LGFS’ submission that, even without giving appropriate weight to the advantage of the primary judge, the evidence upon which AHAC relies falls well short of the quality of evidence required to establish such serious allegations. This is particularly so when regard is had not just to their evidence but the evidence as a whole. Other reasons apart, neither Mr Hilder nor Mr Tischler had any personal interest in the litigation. Mr Hilder was retired and had no ongoing connection to LGFS when giving evidence.

1667. Importantly, as the primary judge correctly observed at J[3628]:

> Moreover, as LGFS said, the characterisation of the product as not a debenture and thus not a security and thus a derivative in which LGFS was not authorised to deal is hardly a straightforward process, as the competing submissions of the parties and my reasons for concluding against LGFS on this issue disclose.

1668. That this was so seems to have been accepted by AHAC which made the submission that the resolution of the question whether the Rembrandt notes were a derivative or, alternatively, a debenture and therefore a security, involved complex legal questions. However, it then submitted that this runs counter to the argument accepted by the primary judge and not in favour of it. The first part of this submission accords with the finding of the primary judge. However, the second part does not. This is perhaps due to a misunderstanding on its part as to what it was that the primary judge in fact concluded at J[2947] and J[3531]. We do not apprehend her Honour to be stating that LGFS knew or ought to have known that, properly analysed, the Rembrandt notes were a derivative and not a debenture and therefore not a security and therefore outside LGFS’ AFSLs.

1669. The reasons must be read as a whole. Her Honour, as we have said, observed how complex the resolution of those questions was. We understand her Honour to be saying no more, in the context of considering alleged breaches of s 912A(1) of the *Corporations Act* , than that LGFS ought to have known that the Rembrandt notes had certain characteristics of a derivative. The question is what flows from this? As her Honour correctly observed at J [3622] speaking of Mr Holder and Mr Tischler:

> … LGFS’s concern was to ensure it dealt in securities so it would have conceived of its responsibility as ensuring that the products it dealt in were securities. It would not have conceived of its responsibility as ensuring that the products it dealt in were not derivatives because, unless they were securities or another nominated exception, *many products would satisfy the basic characteristics of a derivative.*
>
> (Emphasis added.)

and then at J[3630] her Honour went on to say:

> … Having characteristics of a derivative …. did not indicate [that] the product was not a security.

1670. Her Honour's finding that LGFS breached, on competency grounds, s 912A(1) of the *Corporations Act* because those involved were not alert to the *possibility* that (upon detailed analysis) the notes *possibly* were derivatives must be seen in this light.

1671. In other words, Mr Hilder and Mr Tischler should have seen this possibility. This was no warrant for disbelieving their evidence as to what they knew concerning the Rembrandt notes.

1672. **Following paragraph cited by:**

Carter v Chubb Insurance Australia Ltd (14 November 2024) (Halley J)

812. The meaning of "known to the insured" for the purposes of s 21(1) of the Insurance Contracts Act is well settled: *ABN AMRO Bank NV v Bathurst Regional Council* (2014) 224 FCR 1; [2014] FCAFC 65 at [1672] (Jacobson, Gilmour and Gordon JJ) ; *All Class Insurance Brokers Pty Ltd (in liq) v Chubb Insurance Australia Limited (No 2)* (2021) 154 ACSR 78; [2021] FCA 782 at [159] (Allsop CJ). The following authoritative statements as to its construction can be distilled from those authorities:

(a) the term "known" in the phrase "every matter that is known to the insured" has its ordinary English language meaning: *Commercial Union Assurance Co of Australia Ltd v Beard* (1999) 47 NSWLR 735 at 745 [37] (Davies AJA, Meagher JA agreeing);

(b) "knows" means considerably more than believes or suspects, or even strongly suspects: ***Permanent Trustee** Australia Limited v FAI General Insurance Company Limited (in liquidation)* (2003) 214 CLR 514; [2003] HCA 25 at [30] (McHugh, Kirby and Callinan JJ); and

(c) constructive knowledge is insufficient; actual knowledge is required: *CIC Insurance Ltd v Midaz Pty Ltd* [1999] 1 Qd R 279; (1998) 10 ANZ Ins Cas 61-394 (Pincus JA, Moynihan and Byrne JJ agreeing).

The term "known" in the phrase "every matter that is known to the insured" has its ordinary English language meaning: *Commercial Union Assurance Co of Australia Ltd v Beard* (1999) 47 NSWLR 735 at 745 [37] (Davies AJA, Meagher JA agreeing). In s 21 of the ICA "knows" means considerably more than believes or suspects: *Permanent Trustee Australia Limited v FAI General Insurance Company Limited (in liquidation)* (2003) 214 CLR 514 at [30] (McHugh, Kirby and Callinan JJ).

1673. The primary judge rejected the allegation of actual knowledge of the matters alleged or even that LGFS had suspicions to that end, even assuming that suspicions may constitute a matter.

1674. AHAC's submissions have an underlying theme that the Rembrandt notes were derivatives, as though this were obvious and beyond doubt. The primary judge ultimately arrived at a conclusion that they were, but did not, as we have explained, consider this to be obvious or beyond doubt but rather as the product of her distillation of complex matters of fact and law. After detailed consideration, although, to some extent for different reasons, we have come to the same conclusion. However, this conclusion is neither obvious nor self-evident.

1675. We have given careful consideration to the many submissions of AHAC attacking the credibility of Mr Hilder and Mr Tischler, as well as the detailed and lengthy responsive submissions by LGFS on the evidence. These detailed countervailing contentions on the evidence were placed before the primary judge. Nothing put by AHAC demonstrates any of the findings were glaringly improbable or contrary to compelling inferences: *Fox v Percy* at 128 [29] .

1676. The core submissions are set out and reasoned at J[3621]-J[3630] and, contrary to AHAC's submissions, we find her Honour's reasons cogent and persuasive. We have considered these in detail and agree with her Honour's findings and the reasons for them. There is no need to rehearse them here. Her acceptance of the evidence of each of Mr Hilder and Mr Tischler is founded upon extremely strong grounds which are articulated in the trial judgment. There is no basis for interfering with those findings. We find no appealable error in respect of her findings.

3.2 **LGFS' knowledge:** AHAC Appeal Grounds Matrix Rows 3 and 4

1677. This ground argues that the primary judge erred in finding that a reasonable person in the circumstances of LGFS would not have known that the matters set out in (a) and (b) below were matters relevant to the decision of AHAC whether to accept the risk of insuring LGFS and, if so, on what terms.

(a) that the AFSL of LGFS did not permit LGFS to advise about or deal in derivatives; and

(b) the Rembrandt notes which had been sold by LGFS and about which LGFS advised may well be derivatives, because they had the characteristics of a derivative.

1678. AHAC's case about the knowledge of LGFS was based on LGFS' asserted knowledge that its AFSL did not permit it to deal in derivatives combined with asserted knowledge of three alternatives: that LGFS knew the Rembrandt notes were derivatives; or LGFS knew the Rembrandt notes may well be derivatives; or LGFS knew the characteristics of the Rembrandt notes which were characteristics of a derivative. AHAC Appeal Grounds Matrix Row 4 also relates to each of these three alternatives, but with the provisions of s 21(1)(b) of the ICA in mind.

1679. It is important to appreciate just what knowledge it is that s 21(1)(b) concerns. Davies AJA (Meagher JA agreeing) explained this in *Beard* at 745 [38]-[39] .

> [38] Section 21(1)(a) of the Act looks to two aspects of the knowledge of the insured: first, knowledge of a matter and, secondly, knowledge that the matter is relevant to the decision of the insurer whether to accept the risk.
> …
>
> [39] If the insured did not know that the matter was relevant to the decision of the insurer whether to accept the risk, then par (b) comes into operation. It applies when there was a matter known to the insured and a reasonable person in the circumstances could have been expected to know that the matter was so relevant.

1680. This, we apprehend, is also the approach adopted by Einstein J in *Green in his capacity as liquidator of Arimco Mining Pty Ltd (in liq) v CGU Insurance Ltd* (2008) 67 ACSR 398 at 421 [91] . Likewise, Young J in *Advance (NSW) Insurance Agencies Pty Ltd v Matthews* (1987) 4 ANZ Insurance Cases ¶60-813 stated at 74,998 :

> Although the language of sec. 21 is awkward, in my view it means that if a reasonable person in the circumstances could be expected to know that a matter is relevant it must be disclosed and whether that be the case or not, if the insured actually knows the relevant thing, that is enough. However, the insured must have actual knowledge of the thing, the mere fact that he ought in the ordinary course of business to have known is insufficient. In this respect I agree with Tarr on *Australian Insurance Law* at p 85.

1681. In the same vein, Rolfe J stated in *Thompson v Government Insurance Office of New South Wales* (Unreported, Supreme Court of New South Wales, Rolfe J, 15 June 1994) at 63-64 :

> The duty of disclosure extends to every matter specified in subs (a) and subs (b) provided it is a matter known to the insured. To fall within subs (a) the matter must be that which the insured knows to be a matter relevant to the decision of the insurer.
>
> …
>
> However a different test is propounded in subs (b). One moves from actual knowledge, save that the matter must still be known to the insured, to a deemed knowledge in the insured, as a reasonable person in the circumstances.

1682. Lastly, as Tadgell J explained it in *Prime Forme Cutting Pty Ltd v Baltica General Insurance Co Ltd* (1991) 6 ANZ Insurance Cases ¶61-028 at 76,877 :

> … one is concerned only with the existence of matters that were known to the insured before the contract of insurance was entered into, and not with matters of which he ought to have known. Those matters alone are to be disclosed that, being known to the insured at the relevant time, fall within para (a) or para (b) of s 21(1) .

1683. Were it necessary it is also supported by the Second Reading Speech of the Insurance Contracts Bill 1984 which included:

> Clause 21 … clearly states that the insured’s duty is only to disclose those facts which he knew, or which a reasonable person in the circumstances could be expected to have known, to be relevant to the insurer’s assessment of the risk.

Paragraphs 61-62 (Pt IV – Disclosures and Misrepresentations) of the *Explanatory Memorandum to the Insurance Contracts Bill 1984* (Cth) are to like effect.

1684. Nothing in *CGU Insurance Limited v Porthouse* (2008) 235 CLR 103 affects this conclusion.

1685. **Following paragraph cited by:**

Absolute Tiling Solutions Pty Ltd v Certain Underwriters at Lloyds (10 April 2024) (Nixon J)

Accordingly, the inquiry is not whether a reasonable person could be expected to know the "matter" even if the insured did not in fact know the matter. Rather, it is that when a matter is known to the insured, could a reasonable person, in the circumstances, be expected to know that the matter is relevant to the risk decision of the insurer? Thus, breach of s 21 is to be judged against the insured's knowledge of the matter and either their knowledge of its relevance to the decision of the insurer or against the knowledge of that relevance being imputed, employing the objective test of what in the circumstances a reasonable person could be expected to know. The latter deals with a situation where the insured's appreciation of the relevance of a known matter is not reasonable.

1686. In other words, applying this construction, s 21 is not breached by a failure to disclose a matter which is not actually known by the insured.

1687. The primary judge concluded that LGFS did not know the first two alternative matters relied upon: first, that the Rembrandt notes were derivatives and second, that, by reason of its knowledge of the terms and characteristics of the Rembrandt notes, they might well be derivatives. And as we have observed, the third alternative is but a subset of the second.

1688. Given these factual findings no such disclosure was required. LGFS was not required to disclose matters of which it had no knowledge.

1689. It was unnecessary for the primary judge to consider whether a reasonable person could have been expected to know the matters as distinct from the separate question of their relevance to the insurer's decision.

1690. Even if we are wrong as to the proper construction of s 21 in this respect, we agree with the conclusions of the primary judge that a reasonable person could not have been expected to know of the matters asserted by AHAC.

1691. We agree with the primary judge's reasoning at J[3630] that a reasonable person, in the circumstances as at August 2007, could not be expected to have known that the Rembrandt notes were not securities but derivatives in which LGFS was not, by its AFSL, authorised to deal, even assuming this were a matter relevant to the insurer's decision whether to accept the risk.

1692. That a reasonable person in the circumstances knew that the Rembrandt notes were "derivatives", or "may well be" "derivatives" or had the characteristics of a "derivative", was not of itself a fact that was relevant to the risk decision. The fact could be so relevant only if it informed the question of whether LGFS was licensed to deal in, or advise in relation to, the Rembrandt notes. The propositions repeatedly advanced by AHAC based on that fact, assuming it to be a fact, did not inform the risk. This is so because the question relevant to LGFS' AFSLs is whether the Rembrandt notes were "securities", not "derivatives". A reasonable person would have understood that the fact which informed the risk, and thus the fact relevant to AHAC's decision, was whether LGFS was licensed to deal in, or advise about, the Rembrandt notes or, perhaps, whether the Rembrandt notes were "securities".

1693. As to the third alternative, again, the fact that the value of the Rembrandt notes may fluctuate by reference to the underlying credit indices does not speak to the relevant risk, namely that LGFS had sold instruments it was not licensed to sell. A reasonable person in LGFS' position would have considered whether it was licensed to deal in the Rembrandt notes to be relevant, not the fact that the value of the Rembrandt notes may fluctuate by reference to the underlying credit indices.

1694. As her Honour stated, having the characteristics of a derivative, a matter upon which AHAC focussed, did not indicate that the product was not a security: the legal character of the product being obviously contestable.

1695. A reasonable financial adviser no doubt might conclude, whether by reference to their own consideration of the Rembrandt notes or with the benefit of specialist legal advice, that the Rembrandt notes were a derivative in the sense that they were not securities. However, it is at least equally likely that they might conclude that the Rembrandt notes were securities because they were debentures.

1696. We think it correct, as the primary judge said, concerning this legal character of the Rembrandt notes, that a reasonable person is not required always to be right, nor need they always obtain legal advice if there does not appear to be any need to do so. Nonetheless, if they had done so they may well have obtained an opinion that the Rembrandt notes were securities because they were debentures. This is not mere speculation. As it transpired LGFS post-contractually did seek an opinion from Mallesons Stephen Jaques who did give such an opinion that the Rembrandt notes were debentures and thus securities. The submission put to the primary judge, and repeated before us, that a reasonable person could be expected to have known that the Rembrandt notes may well be derivatives ignores these realities. AHAC, in our opinion, has asked the wrong questions and answered them as to what was relevant to the risk for the purposes of s 21(1) of the ICA .

1697. We have already explained that AHAC has misunderstood and overstated the conclusions of the primary judge: J[2947] and J[3531]. Properly understood they are not at odds with what is found at J[3630]. This is just another example of focussing on the question whether the Rembrandt notes were derivatives or had the hallmark of a derivative, rather than whether they were a security.

1698. For these reasons this Appeal Ground fails.

3.3 **Was the duty of disclosure waived?:** AHAC Appeal Grounds Matrix Row 5

1699. AHAC challenges the finding that because it did not require a proposal form from LGFS, it was deemed, pursuant to s 21(3) of the ICA , to have waived compliance by LGFS with its duty of disclosure in respect of the matters set out below:

(a) that the AFSL of LGFS did not permit LGFS to advise about or deal in derivatives; and

(b) the Rembrandt notes which had been sold by LGFS and about which LGFS advised may well be derivatives, because they had the characteristics of a derivative.

1700. AHAC did not require LGFS to complete an insurance proposal form. Rather, it advised FuturePlus' broker by email dated 4 June 2007 that only FuturePlus as the "holding named corporation" was required to fill out the proposal form together with a financial planner's addendum. It also advised that for subsidiaries of FuturePlus what was required were copies of audited financials/management reports and further business details "in your submission". This was referring to the proposal form to be submitted on behalf of FuturePlus. This proposal form was filled out, as requested, only by FuturePlus. FuturePlus was named as the "proposer". It was signed on behalf of FuturePlus by its chair, Mr Peter Woods.

1701. The primary judge concluded at J[3631] that if an insurer does not insist on a completed proposal form from the insured, then the insured has failed to answer any question in a proposal form and thus s 21(3) is engaged. Her Honour also concluded that as the proposal form submitted related only to FuturePlus and only asked about dealings in derivatives, LGFS' argument as to waiver in accordance with s 21(3) should be accepted.

1702. Section 21(3) of the ICA provides that:

(3) Where a person:

(a) failed to answer; or

(b) gave an obviously incomplete or irrelevant answer to;

a question included in a proposal form about a matter, the insurer shall be deemed to have waived compliance with the duty of disclosure in relation to the matter.

1703. We are of the opinion that AHAC did waive any s 21 duty of disclosure on the part of LGFS, but for reasons which differ from those of the primary judge. To the extent that AHAC challenges her Honour's reasons we accept its submissions.

1704. We are of the opinion that before s 21(3) is enlivened there must have been a question in a proposal form which the proposed insured has failed to answer or in respect of which the proposed insured has given an obviously incomplete or irrelevant answer.

1705. “Proposal form” is defined in s 11 of the ICA to include, relevantly, a document containing questions to which a person is asked to give answers (whether in the document or not) where the answers are intended (whether by the person who answered them, by the insurer or by some other person) to be used in connection with a proposed contract of insurance.

1706. The definition is inclusive in nature. Completion of an on-line proposal has been held to constitute a proposal for the purposes of s 21(3) : *Celik v NRMA* [2000] NSWSC 380 at [10] and [29]-[33] .

1707. In *Orb Holdings Pty Ltd v Lombard Insurance Company (Australia) Limited* [1995] 2 Qd R 51 , referring to ss 21(3) and 27 , Fitzgerald P said at 53:

> … The rationale behind those provisions is that obviously incomplete information puts the insurer on inquiry and, if it omits to inquire, it has waived its right to rely upon the insured’s failure to disclose or misrepresentation.

1708. The requirement for a proposal form under s 21(3) is a positive one. The statutory inquiry is not relevant where no proposal form exists. The questions in the proposal form were directed to FuturePlus, not LGFS. It cannot be said that LGFS failed to answer a question or gave an obviously incomplete or irrelevant answer to a question.

1709. However, that is not the conclusion of the matter. Section 21(2)(d) provides that the duty of disclosure does not require disclosure of a matter as to which compliance with the duty is waived by the insurer.

1710. **Following paragraph cited by:**

J&J Richards Super Pty Ltd ATF the J&J Richards Superannuation Fund v Nielsen (18 December 2024) (Halley J)

Section 21(3) provides alternative examples of what will be deemed to be waiver of compliance. This provision is not a codification of circumstances which may constitute a waiver.

1711. **Following paragraph cited by:**

J&J Richards Super Pty Ltd ATF the J&J Richards Superannuation Fund v Nielsen (18 December 2024) (Halley J)

Here, assuming LGFS had the relevant duty of disclosure, compliance with it was waived by the insurer when it made clear that it did not require a proposal form to be filled in by LGFS but required only financial statements. It would be surprising if, assuming the existence of the duty, AHAC could rely on non-compliance by LGFS when it had stated that all that it required were financial statements and that it did not require a proposal form to be completed. That is, beyond what was contained in, relevantly, the financial statements for LGFS, AHAC positively stated that it required no other information.

1712. It follows that, although we disagree with the reasoning of the primary judge, we nonetheless consider that AHAC waived compliance with the statutory duty of disclosure which we have assumed, for present purposes, lay with LGFS.

1713. This Appeal Ground fails.

3.4 Did any non-disclosure have a causative effect?: AHAC Appeal Grounds Matrix Row 6

1714. AHAC challenges the finding that if the matters set out in (a) and (b) below had been disclosed to AHAC by LGFS, AHAC would nonetheless have entered into the Insurance Contract on the same terms and conditions: J[3632]-J[3633]:

(a) that the AFSL of LGFS did not permit LGFS to advise about or deal in derivatives; and

(b) the Rembrandt notes which had been sold by LGFS and about which LGFS advised may well be derivatives, because they had the characteristics of a derivative.

1715. For the purposes of this Appeal Ground, which concerns the provisions of s 28 of the ICA , we have assumed, contrary to our conclusion, that LGFS owed AHAC a s 21 duty of disclosure and breached it as alleged.

1716. The primary judge found for the following reasons that AHAC did not establish that it would have had a lesser liability but for the non-disclosures. AHAC did not prove that, had the alleged facts been disclosed, it would not have entered into the insurance contract on the same terms. Accordingly, s 28(3) of the ICA was not engaged to reduce AHAC's liability to LGFS.

1717. The primary judge's finding is based on her Honour having observed AHAC's witnesses Ms Harvey and Ms Uhrik give evidence. It is correct that her Honour did not conclude that as witnesses they lacked credibility. This is only to say that her Honour found that each was honest in giving their evidence. This is not a reason necessarily to accept their evidence. The primary judge did not accept their evidence on this question because she concluded that it was informed by hindsight and by the way in which AHAC framed its case: J[3633] read with J [3605]-J[3612]. The primary judge's findings appropriately took into account their evidence in cross-examination.

1718. We find no reason to interfere with her Honour's relevant findings of fact. We do not regard as obvious, as AHAC contends, that because the Rembrandt notes "may well have been a derivative" and "therefore outside the scope of LGFS' AFSL" that AHAC would have excluded liability arising from activities concerning those notes. That is the point the primary judge made at J[3632] when she observed, not for the first time, that the fact that the notes had characteristics of a derivative would have been immaterial. AHAC did not advance a case that LGFS knew its AFSL did not permit it to deal in the notes. The inference which AHAC contends is obvious is in effect one which follows only from knowledge that LGFS was not licensed to deal in the notes.

1719. The primary judge concluded that the facts were consistent with the asserted non-disclosure not affecting AHAC's decision to accept the risk: J[3633] (against the background of J[3607]-J[3612]). Those facts support her Honour's findings having observed the witnesses giving evidence.

1720. We will consider the substance of these findings.

1721. The primary judge found that the best evidence of what AHAC would have done following disclosure of the "matter" said to be required is what happened after these claims were notified. After notification of the claims in May 2008, AHAC again insured LGFS for the 2008/09 year on relevantly the same terms as in the 2007/08 policy. AHAC did so without making any further enquiry about the circumstances about which it had been notified although AHAC thought that the Rembrandt notes were a "high-risk instrument", knew LGFS had been dealing in a product described as a "Constant Proportion Debt Obligation" and thought the Rembrandt notes "sounded like a derivative". That AHAC did not consider a dealing in derivatives of itself to relevantly inform the risk, in relation to the FuturePlus group of companies, was, as her Honour concluded, further demonstrated by the fact that when it entered into the 2007/08 policy AHAC knew from answers given by FuturePlus to questions asked in the proposal form to the effect that FuturePlus offered a "third party trading" service, 29% of the income from which was derived from investments in "derivative instruments".

1722. Further, the primary judge found (at J[3608] read with J[3633]) that AHAC would not have understood the allegedly undisclosed facts to be relevant to an assessment of risk as Ms Uhrik and Ms Harvey did not know what a CPDO, a CDO or a "credit index linked floating rate note" was. AHAC's submission is that the knowledge of Ms Uhrik and Ms Harvey of the terms of a CDO, CPDO, or credit index linked floating rate note is irrelevant and that LGFS' submissions overlook the affidavit evidence of Ms Harvey in her first affidavit at paragraph 31:

> If it had been brought to my attention that LGFS had been advising any of its clients to buy notes whose value was determined by reference to two credit default indices, I would have thought that those words, in the context of describing an investment, sounded like the description of a derivative product.

AHAC submits that Ms Harvey was not challenged about this evidence.

1723. However, Ms Harvey could not describe the features of a "derivative" and did not know whether a CDO was a "derivative". From May 2008 she thought CPDOs were a "high risk" product but caused AHAC to insure LGFS, and also knew that FuturePlus had a trading service which dealt in "derivatives". The conclusion of the primary judge that AHAC considered it did not need to know about the products LGFS was selling when deciding to insure FuturePlus at J[3608] read with J[3633] is well supported on the evidence.

1724. Ms Harvey was relevantly cross-examined and she conceded that she could not say that AHAC would have taken any particular action in relation to the 2007/08 policy had AHAC been told that the Rembrandt notes might be a "derivative". That concession by Ms Harvey, of itself, we accept, is fatal to AHAC's appeal on this ground.

1725. AHAC submits that knowledge of Ms Harvey or Ms Uhrik of the terms of the CPDO, a CDO or a "credit index linked floating rate note" is irrelevant. It submits that the real issue is what the underwriters would have done if they had been told that LGFS' AFSL did not permit dealing in derivatives and that the insured was dealing in a product that might be a derivative.

1726. However, as we have already observed, and as the primary judge stated, in this context, at J [3632], the fact that LGFS knew it was dealing in products outside the terms of its AFSL was not one of the asserted facts on which AHAC relied. The non-disclosure case run by AHAC, built on its three alternatives concerning derivatives, did not extend to whether dealing with these was outside the AFSL. It is no answer to this obvious point to say that Ms Uhrik was not cross-examined as to whether AHAC would still have insured LGFS with respect to claims connected to the Rembrandt notes.

1727. As the primary judge accepted, despite knowing these facts, AHAC was so keen to keep FuturePlus' business that it was prepared to cut its premiums to do so: J[3607] read with J [3633]. AHAC was prepared to accept the risk associated with the FuturePlus group dealing in these derivative instruments.

1728. AHAC's approach to insuring the risk is explained as FuturePlus was an important customer of AHAC and Ms Uhrik was concerned that AHAC should insure FuturePlus: J[3609] read with J[3633]. These findings are amply justified.

1729. AHAC submits that Ms Uhrik's evidence, referred to by her Honour at J[3570], was that notwithstanding that FuturePlus was an important customer of AHAC, Ms Uhrik would only accommodate requests to insure if it was the right decision for AHAC to write the piece of business. AHAC further submits that this evidence was not explicitly rejected, even though referred to, by the primary judge and its rejection does not sit with the finding at J[3633] that the evidence of AHAC's witnesses did not lack credibility.

1730. It is not necessary that a trial judge explain every reason or refer to every piece of evidence supporting their findings of fact. As we have explained, her Honour's reasons are cogent and supported by sufficient reasons based in the evidence. We have explained the context and consequences of the credibility finding.

1731. Next, the primary judge found that, for the reasons already identified by her, the facts which AHAC alleged should have been disclosed did not inform the risk AHAC was asked to accept. This was so because, picking up a familiar refrain, as her Honour accepted, whether LGFS was licensed to deal in the Rembrandt notes may have affected that risk but the asserted facts said nothing about whether LGFS was in fact licensed to deal in these notes: J[3610] read with J[3633].

1732. This again emphasises the lack of connection between the non-disclosure alleged and AHAC's submissions. The evidence of each of Ms Uhrik and Ms Harvey, referred to in this context, misses this central tenet of the case run by AHAC at trial.

1733. Moreover, as we mentioned, the primary judge did not accept their evidence on this question for cogent reasons to which we have referred. It was evidence which her Honour concluded was based on hindsight and which should be rejected. There was a clear basis in the evidence for so concluding.

1734. AHAC submits that its "failure" to inquire about LGFS' trading service was irrelevant and that the obligation to disclose falls upon LGFS. AHAC submits that it was not AHAC's responsibility to dig and investigate matters that were either known to LGFS to be relevant to AHAC's decision to insure the risk or a reasonable person would have known to have been so relevant. This finding, it submits, was an error on the part of the primary judge amounting to an impermissible reversal of onus.

1735. We do not agree. Her Honour was there not dealing with a "matter" not disclosed. Rather, in accepting LGFS' submissions, she was describing a circumstance which reinforced her earlier conclusion that, irrespective of facts such as FuturePlus gaining 29% of its third party trading service income from investments in derivative instruments, AHAC was nonetheless keen to keep FuturePlus' insurance business. This finding was descriptive of AHAC's tolerance for risk.

1736. There is a further relevant fact. The primary judge found (at J[3612] read with J[3633]) that AHAC did not concern itself to obtain a copy of LGFS' AFSLs. Nonetheless, AHAC submits that it was entitled to assume that LGFS was acting within its AFSLs, that it had not been told otherwise and that Ms Uhrik had said that she expected there would be disclosure that the activities of the insured were or may have been beyond the terms of its AFSL.

1737. However, as the primary judge repeatedly observed, as have we, evidence of that kind was not relevant to the matters which AHAC asserted, on its case, ought to have been disclosed. AHAC's case is not that LGFS knew it was acting outside the scope of its AFSL, yet that is the fact AHAC says would have caused it to have acted differently.

1738. This Appeal Ground fails.

3.5 Exclusion in Endorsement 17: AHAC Appeal Grounds Matrix Rows 7 and 8

3.5.1 Introduction

1739. AHAC advances two arguments in reliance on Endorsement 17, both of which were rejected by the primary judge at J[3646]-J[3664]. First, AHAC contends that the chapeau to Endorsement 17 is a separate exclusion disconnected from the sub-paras which follow, so that the insurance extends only to financial planning advice and services which are authorised by LGFS' AFSL. Second, AHAC contends that Endorsement 17 excludes any liability arising out of a circumstance, not limited to the occasion identified in the chapeau to Endorsement 17, where LGFS has not disclosed a conflict of interest and contends that LGFS' liability does so arise.

1740. LGFS submits that for the reasons given by the primary judge, AHAC's reliance on Endorsement 17 was correctly rejected for three reasons. First, the effect of the chapeau to Endorsement 17 is that the endorsement applies only to "financial planning advice", which LGFS did not provide to the Councils and the Endorsement is not engaged: J [3658]. Second, the words "financial planning advice and services that the Insured is authorised to provide under an Australian Financial Services License (sic)" in the chapeau to the Endorsement are descriptive of the scope of the exclusion, and are not a separate exclusion to the otherwise broad insuring clause (cl 1): at J[3659]. Third, LGFS did not have a conflict which was not disclosed.

1741. Endorsement 17 is in the following terms:

> The following exclusions apply to **Claims** arising from financial planning advice and services that the **Insured** is authorised to provide under an Australian Financial Services License (sic):
>
> **Commingling** (sic) **of funds**
>
> > arising out of, based upon, attributable to or in any way connected with any actual or alleged commingling (sic) of funds by the **Insured** or any inability or failure of the **Insured** to pay, collect, safeguard or account for client funds.
>
> **Failure to disclose conflict of interest**
>
> > arising out of based upon, attributable to or in any way connected with the failure of any Insured to adequately disclose any conflict of interest.
>
> **Excessive Fees**
>
> > arising out of, based upon or attributable to **Claim** for the reimbursement of fees, commissions, costs or other charges paid or payable to the **Insured**, or any third party claim based upon allegations against the Insured of excessive fees, commissions, costs or other charges.
>
> **Margin lending & gearing**
>
> > arising out of, based upon, attributable to or in any way connected with the actual or alleged giving of any services, advice or recommendations by or on behalf of the **Insured** regarding financing, margin lending, investment gearing or any other of debt.
>
> In all other respects this policy remains unaltered.

3.5.2 Was Endorsement 17 engaged?

1742. AHAC submits that an ordinary reading of the opening words is wider than a mere description as Endorsement 17 is an exclusionary provision in which the opening words prescribe the relevant activity to which the exclusions apply and, relevantly, that activity is required to have been carried on pursuant to authorisations under an AFSL.

1743. The primary judge distinguished the expression “financial planning advice and services” from “financial advice and services”. Her Honour concluded that LGFS was not providing the Councils with financial planning advice and services.

1744. AHAC submits that the reference in the Endorsement to “financial planning advice and services” is intended to refer to “financial services” as defined in the *Corporations Act* , as it is financial services which are the subject of authorisation pursuant to an AFSL.

1745. AHAC relies upon the following findings made by the primary judge which it submits are relevant to the proper construction of Endorsement 17:

1. By s 766A(1) of the *Corporations Act* , a person provides a financial service if they provide financial product advice or deal in a financial product (J[2126]);

2. Financial product advice means a recommendation or a statement of opinion, or a report of either of those things, that is intended to influence a person or persons in making a decision in relation to a particular financial product or class of financial products, or an interest in a particular financial product or class of financial products or could reasonably be regarded as being intended to have such an influence (s 766B) (J[2126]);

3. Dealing in a financial product includes applying for or acquiring a financial product and disposing of a financial product (s 766C) (J[2126]);

4. The Councils' acquisition of the Rembrandt 2006-3 notes from LGFS involved the acquisition of a financial product. In selling the Rembrandt 2006-3 notes to the Councils LGFS was engaged in dealing in a financial product and providing a financial service (J[2132]); and

5. LGFS gave the Councils "financial product advice" both as defined in s 766B of the *Corporations Act* and otherwise in accordance with the ordinary meaning of that phrase, and its advice to the Councils was to invest in the Rembrandt 2006-3 notes (J[2147]).

1746. AHAC submits that the services LGFS was found to have provided to the Councils were provided purportedly pursuant to LGFS' AFSL and that accordingly those services trigger the opening words in Endorsement 17 and the exclusions that follow.

1747. AHAC seeks to rely upon the Code of Professional Practice introduced by the Financial Planning Association of Australia (July 2011 edition), which includes the following definition of "financial planning service":

> Financial planning service:
>
> is a service of which the Member or his or her associates does one or more of the following for a client:
>
> (a) Provides a recommendation, an opinion or a report, that is intended to influence a prospective client or client in making a decision in relation to:
>
> i. a particular product or class of products, or an interest in a particular product or class of products; and/or
>
> ii. a particular strategy in the management of the client's financial circumstances.
>
> (b) Deal in a product or products as a result of a recommendation, opinion or report provided by the Member or his or her associates; and

(c) Deal in a product or products pursuant to an authority provided by the client and includes the authority or power of attorney to operate managed discretionary accounts.

1748. AHAC submits that the Code's definition of "financial planning" is consistent with ordinary usage which does not confine financial planning advice to advice to individuals as opposed to bodies corporate or governmental bodies. Each of the Councils was engaged in planning the investment of its surplus funds in a way which gave a return while allowing for its liquidity requirements. LGFS gave advice in respect of that planning. Thus, AHAC submits, this captures the services which her Honour found that LGFS provided to the Councils.

1749. Consequently, AHAC submits that the primary judge ought to have found that the activities of LGFS fell within financial planning services and that those services were outside the scope of the AFSL by reason of which no cover applied.

1750. LGFS submits that the chapeau to Endorsement 17 confines the exclusions to "financial planning advice and services".

1751. It submits that the concept of "financial planning advice and services" is well understood as a matter of ordinary English language, namely a retail service provided to individuals, and small proprietary companies controlled by individuals as part of their wealth management, in relation to personal and family wealth management. It submits that the service provided by LGFS to the Councils is not of that character, rather, LGFS sold a complex financial instrument to wholesale customers which, as the primary judge held, is not "financial planning". Thus it contends Endorsement 17 is not engaged.

1752. LGFS submits that this construction is reinforced by the following.

1753. First, the immediate context of the words the "financial planning advice and services", namely the four exclusions created by Endorsement 17. Each of those exclusions is directed to the possible conduct of a financial planner. The first exclusion relates to the mixing of what are likely to be trust funds held for a financial planner's client. That exclusion, the mixing of funds, self-evidently has no application to LGFS' business, which includes a deposit taking service. Similarly, the exclusion of claims arising from excessive fees is applicable to what is generally understood to be "financial planning", but has no or limited application to a deposit taking and product sales business. The margin lending exclusion is also an exclusion directed to well-known but sometimes problematic advice given by some financial planners. The failure to disclose a conflict of interest exclusion is of the same character. It is directed to the conflicts that a financial planner may have, such as recommending to a client products for which the planner receives an undisclosed commission. That exclusion has no application to a business of operating in the investment market, which involves borrowing and lending and buying and selling, with a view to profit.

1754. Second, it is wrong to equate "financial planning advice and services" with any "financial service" as defined by the *Corporations Act* . AHAC's construction ignores the word "planning" and in doing so attempts to significantly expand the exclusion. There is no cause to construe an insurance policy other than on the basis that the words used have their well understood meaning. Had the parties intended Endorsement 17 to apply to all "financial services" as defined by the *Corporations Act* , they would have used that language. Instead the Endorsement is expressly directed to a different and narrower concept.

1755. Third, to the extent the Endorsement is ambiguous, extrinsic evidence is admissible to construe Endorsement 17. The extrinsic evidence demonstrates the construction adopted by the primary judge is correct. To AHAC's prior knowledge FuturePlus had, from long before 2007/08, a "substantial" financial planning business: J[3652] and J[3659]. Before entering into the insurance contract for the 2007/08 year AHAC obtained a separate "Financial Planners Professional Liability Insurance Proposal Form" from FuturePlus, which was relevant only to the financial planning part of FuturePlus' business. This is to be distinguished from the Civil Liability Insurance Proposal Form which was also completed by FuturePlus. We note also that the AFSL details in the Financial Planners Professional Liability Insurance Proposal Form concerned not those of LGFS but, unsurprisingly, those of FuturePlus. The licence number provided by FuturePlus was 238445. The licence number for LGFS was 245642. This extrinsic evidence shows that Endorsement 17 applied to the "financial planning" business referred to in the chapeau to Endorsement 17. Further, the limitation of Endorsement 17 to only the "financial planning" part of FuturePlus' business is expressly stated in the proposal sent by AHAC to FuturePlus' broker. The same language was adopted by Marsh, the broker, in the placement slip. The extrinsic evidence shows that Endorsement 17 was not objectively intended to have application to LGFS' conduct in selling products. Moreover, there is no evidence and no finding that LGFS carried on a financial planning business.

1756. We accept these submissions made by LGFS. In doing so we have not had regard to the content of the Code of Professional Practice referred to by AHAC. It was not before the primary judge. In any event, it post-dates the insurance contract by approximately 4 years. The context of the quote is unknown.

1757. It follows that we find no error on the part of the primary judge in this respect. The exclusions had no operation in relation to the claims made by LGFS.

3.5.3 Does the insuring clause apply only to conduct within LGFS' AFSL?

1758. Given our conclusion that Endorsement 17 has no application to LGFS it is strictly unnecessary to consider this point. Nonetheless for the sake of completeness we will do so. It is convenient first to set out the general insuring clause (cl 1):

> **1. Insurance Cover**
>
> The **Insurer** shall pay on behalf of the Insured for any **Civil Liability** and **Defence Costs** arising out of a **Wrongful Act**, which gives rise to a **Claim** made against the **Insured** during the **Policy Period** or the **Discovery Period**.
>
> …
>
> **2.19 Wrongful Act** means any act error or omission committed or attempted or allegedly committed or attempted by the **Insured** or by any other person for whose **Wrongful Act** the **Insured** is legally responsible, arising out of the provision of, or failure to provide, services to third parties provided in the course of the **Insured Entity's** business. All related or continuous **Wrongful Acts** shall be considered a single **Wrongful Act**.

1759. AHAC submits that on its proper construction, Endorsement 17 excludes liability to indemnify in respect of claims arising from financial planning advice and services that the insured is not authorised to provide under an AFSL.

1760. AHAC submits that if this were not the proper construction of Endorsement 17 an anomalous situation arises where, for example, a claim arising out of a failure to disclose a conflict of interest, where the advice being given was authorised by an AFSL would be excluded, but a claim arising out of a failure to disclose a conflict of interest would not be excluded if the advice was not authorised by an AFSL. In AHAC's submission, this demonstrates that the structure of the Endorsement is that it has as a starting point the notion that financial planning advice and services not authorised by an AFSL are excluded from cover. Then, in respect of financial planning advice and services which are authorised, there are specific further exclusions.

1761. AHAC further submits that there is nothing uncommercial or contrary to the objective of an indemnity insurance policy for the policy to have as a starting point that the activities of the insured must be lawful in order to attract indemnity. It points to the following in support of this submission. By s 911A(1) of the *Corporations Act* , a person who carries on a financial services business must hold an AFSL covering the provision of the financial services. Pursuant to s 1311(1) of the *Corporations Act* , a person who provides a financial service which is not authorised by the provisions of an AFSL commits an offence. As discussed above, the existence of the obligation to indemnify in respect of "Civil Liability" hinges upon the commission of a "Wrongful Act". "Wrongful Act" in turn is related to the provision of services to third parties in the course of the insured entity's business. A starting premise that the insured's business is being conducted lawfully is not unusual.

1762. AHAC submits that it is distinctly uncommercial to construe Endorsement 17 on the basis that, provided the insured provides financial planning advice and services unlawfully, that is, outside the scope of its licence, it is covered for all of the activities set out in Endorsement 17 but, if it is licensed, then cover for those activities is excluded.

1763. AHAC's construction is, in effect, that Endorsement 17 requires that the insurance contract not respond to a claim in relation to advice or services which are not authorised by LGFS' AFSL. We agree that this construction requires Endorsement 17 to be read, not as four exclusions but as the chapeau, in effect, being a separate general exclusion. We do not accept that this is the proper construction and agree with the following submissions by LGFS which reflect the reasons of the primary judge at J[3659].

1764. As AHAC would have it, although appearing in an endorsement creating four specific exclusions, the introductory words be read as if part of, or a limitation upon, the insuring clause: J[3654]. The language of Endorsement 17 is inconsistent with AHAC's construction. The Endorsement relevantly reads "[t]he following exclusions apply to Claims arising from financial planning advice and services that the Insured is authorised to provide under an Australian Financial Services [Licence] …". The words in the chapeau after "arising from" are words of limitation. The primary judge's construction gives the words their "natural and ordinary meaning", as is required when construing an insurance contract: *Selected Seeds Pty Ltd v QBEMM Pty Ltd* (2010) 242 CLR 336 at 345 [34] and *Darlington Futures Ltd v Delco Australia Pty Ltd* (1986) 161 CLR 500 at 510. AHAC's construction, in contrast, requires that the words both before and after the phrase “is authorised to provide under an Australian Financial Services [Licence]” be ignored. We observe, in this respect, that Endorsement 17 expressly provides in its concluding words that “[i]n all other respects this policy remains unaltered”. This underlines that the Endorsement is entirely exclusionary in its effect but does not operate otherwise to amend the general insuring clause.

1765. AHAC’s argument requires that either only part of the chapeau is in effect a separate exclusion (that the advice must be within LGFS’ AFSL) or, contrary to the language of the insuring clause, the cover is limited to financial planning advice and services. That is not the intention of the parties as is shown by the language of the insuring clause. AHAC’s construction should be rejected as it disconnects the words AHAC relies on from the context of Endorsement 17.

1766. Further, “whilst regard must be had to the language used in an exclusion clause, such a clause must be read in light of the contract of insurance as a whole, ‘thereby giving due weight to the context in which the clause appears’”: *Selected Seeds* at 344 [29] and *Darlington Futures* at 510. AHAC’s construction requires that words in the chapeau to the Endorsement, which, as a matter of language, describe the occasion on which the exclusions created by the Endorsement will apply, should be read as a general limitation to the insuring clause. That is not the effect of the chapeau, which is rather to delineate the operation of the exclusions in the following paragraphs of the exclusion: J[3655] and J[3659].

1767. The anomaly which AHAC postulates does not arise. Objectively, from the content of the FuturePlus Financial Planners Professional Liability Insurance Proposal Form the parties knew that FuturePlus and two of its subsidiaries (LGSS and Energy Industries Superannuation Scheme Pty Limited) carried on “financial planning” businesses, implicitly, under AFSLs which authorised those entities to carry on those businesses. Against that background, the words in the chapeau to Endorsement 17 are descriptive of the business from which the “Claim” must arise in order for the exclusion to apply. They are words which identify the operation of the exclusion. They do not operate as a general limitation on the insuring clause: J[3656] and J[3659].

1768. The construction reached by the primary judge is commercially sound: J[3657] and J[3659].

1769. The construction contended for by LGFS is consistent with the insuring clause including claims for restitution, which is apt to capture the rescission claim in this case. Against the mutually known background of the *Corporations Act* , the inclusion of an order for “restitution” in the insuring clause is an objective indication that an “unlicensed to deal” claim was intended to be insured.

1770. The primary judge accepted at J[3657] that in the absence of language which directly says so, the parties should not be taken as having objectively intended that the insurance cover be limited to circumstances in which the insured was acting wholly within its AFSL. The potentially considerable limitation on the scope of the cover argued by AHAC should not be introduced by anything less than clear language. That language does not exist in this case.

1771. Accordingly, we are of the opinion that even if Endorsement 17 applied to LGFS it did not operate to exclude liability for the claims made on the basis that LGFS acted outside its AFSL, if that fact be assumed only for this purpose.

3.5.4 Conflict of interest: LGFS Appeal Grounds Matrix Row 124 and AHAC Appeal Grounds Matrix Row 8

1772. Alternatively, AHAC submits that having found that LGFS had a liability to the Councils by reason of a breach of fiduciary duty which involved the failure by LGFS to disclose a conflict of interest, the primary judge erred in finding that Endorsement 17, which excluded the application of the policy to claims arising from financial planning advice and services "arising out of based upon, attributable to or in any way connected with the failure of any Insured to adequately disclose any conflict of interest", did not exclude the claim by LGFS because the advice given by LGFS was not financial planning advice.

1773. This Appeal Ground also fails for the reasons given by the primary judge as we have just explained in relation to the construction issue.

1774. Upon the assumption, contrary to our conclusion, that Endorsement 17 is engaged LGFS submits that it is an exclusion for a "Claim" "arising out of, based upon, attributable to or in any way connected with the failure of [LGFS] to disclose any conflict of interest". The exclusion is engaged by a claim arising out of a failure to disclose a conflict of interest. A relevant conflict and non-disclosure is necessary. For the reasons set out in Part 8, Section 2.3 above, LGFS did have a relevant or material conflict (in the sense of a relevant conflict of duty and duty or duty and interest) and that conflict was not disclosed. The breach of fiduciary duty finding has not been set aside.

1775. However, even if that conflict is a relevant "connected" conflict (which we do not need to decide), this Appeal Ground fails at the threshold because the Endorsement did not apply to LGFS for the reasons just stated.

3.6 **Exclusion in Endorsement 16:** AHAC Appeal Grounds Matrix Row 9

1776. Alternatively, by this ground AHAC submits that the primary judge erred in finding that the claim by LGFS was not excluded by Endorsement 16 of the policy by which proprietary trading is excluded from cover: J[3677]-J[3678].

1777. Endorsement 16 provides that AHAC is not liable for any "Civil Liability" or "Defence Costs":

> Arising out of, based upon or attributable to:
>
> (iii) a proprietary trading loss, or a business loss where the **Insured Entity** is acting on its own behalf or as principal.

1778. "Civil Liability" is defined as:

> … a legally enforceable obligation to a third party to pay damages, or to make restitution in accordance with an award of a court, tribunal or a regulator under whose jurisdiction the **Insured** is bound.

1779. Her Honour held at J[3677]-J[3678]:

> … LGFS's liability to the councils is not a liability arising out of, based upon or attributable to a proprietary trading loss. LGFS's liability has nothing to do with the concept of a proprietary trading loss. LGFS's liability arises from having sold to the councils a product that failed in circumstances where LGFS breached various duties and responsibilities to StateCover and the councils. This loss is not a loss by reason of LGFS's proprietary trading or trading on its own account in any way. It is loss of a third party for which LGFS is liable within the meaning of Civil Liability as defined in the policy and outside and entirely unconnected with any notion of proprietary trading losses.
>
> AHAC's focus on the selling of the notes to the councils which LGFS purchased for that purpose as an act of proprietary trading overlooks the context of the provision as a whole. The provision is concerned with Civil Liability arising out of, based upon or attributable to proprietary trading losses. LGFS did not suffer any loss by reason of selling the notes to the councils. To the contrary, LGFS made a profit out of that activity. LGFS's loss arises by, is based upon and is attributable to the councils' claims against LGFS.

1780. AHAC submits that this reasoning ignores the structure of the policy and the wording of the exclusion for the following reasons:

1. First, the policy is a liability policy – it is not a policy which grants indemnity to an insured who sustains "a proprietary trading loss" or a business loss. It is only triggered where a third party sustains the loss in circumstances where the definition of "Civil Liability" is satisfied;

2. Second, liability under the policy is only triggered once a defined "Civil Liability" occurs. As noted above, that liability exclusively refers to "a legally enforceable obligation to a *third party*" (emphasis added);

3. Third, cover which would ordinarily be available for "Civil Liability" will nevertheless be excluded in the event Endorsement 16 applies. This endorsement excludes any liability when the "Civil Liability" arises out of or is based upon or is attributable to "a proprietary trading loss, or a business loss where the Insured Entity is acting on its own behalf or as principal". Thus, there is a need to ascertain whether the "Civil Liability" came about in those defined circumstances;

4. Fourth, the clear intention of the policy must be that "Civil Liability" as defined (that is in the sense of legal obligation to a third party) will only apply where the third party has sustained loss that has resulted from an act, error or omission. However, where the loss arises out of an insured's proprietary trading, it is excluded from cover;

5. Fifth, the correct approach to the interpretation of exclusion clauses has been settled by the High Court in *Darlington Futures* at 510 ;

6. Here, LGFS engaged in proprietary trading by buying and selling the Rembrandt notes on its own behalf. The liability arose out of that proprietary trading. The exclusion applies;

7. The use of the word “loss” in the phrase “proprietary trading loss” is awkward. A liability cannot arise out of a trading loss of the insured. The word “loss” should be disregarded to give a sensible meaning to the provision.

1781. We have assumed that this last submission is that the word “loss” where it appears twice should be ignored. Against those submissions and particularly the last of them AHAC then submits that the purchase by LGFS of the Rembrandt notes and their on-sale to the Councils was proprietary trading. It was trading, involving the purchase and sale of a product. It was proprietary because the purchase and sale was by LGFS on its own account and not on behalf of any other person, so far as the dealings with the Councils were concerned.

1782. As to the question whether the Civil Liability can be said to arise out of, be based upon or attributable to that proprietary trading AHAC submits that the liability arose out of the sale of the Rembrandt notes by LGFS to the Councils. It further submits that if the Councils had not bought the Rembrandt notes there would be no liability and that it is the purchase of the Rembrandt notes by the Councils which gives rise to any prospect of liability.

1783. AHAC’s construction of Endorsement 16 requires the word “loss” where twice appearing be read out of the endorsement for the benefit of the *proferens*. We accept the submission made by LGFS that this is to invert each part of the process of construction required by *Darlington Futures Limited* at 510:

> These decisions clearly establish that the interpretation of an exclusion clause is to be determined by construing the clause according to its natural and ordinary meaning, read in the light of the contract as a whole, thereby giving due weight to the context in which the clause appears including the nature and object of the contract, and, where appropriate, construing the clause contra proferentem in case of ambiguity.

1784. Indeed, if AHAC’s constructive process were followed the exclusion clause relevantly would read as follows:

> The Insurer shall not be liable to make payment for Civil Liability and Defence Costs [a]rising out of, based upon or attributable to … a proprietary trading or a business where the Insured Entity is acting on its own behalf or as principal.

1785. The language of the exclusion is inconsistent with AHAC’s construction. The exclusion applies only to “a proprietary trading loss, or a business loss”. LGFS’ liability to the Councils is not of that character. Its liability is for losses caused to the Councils substantially by LGFS’ misleading or negligent conduct in advising or informing the Councils about the Rembrandt notes.

1786. Deleting the word “loss”, whether where it first appears or twice would, in effect, rewrite the exclusion.

1787. The language is clear. The Endorsement has the effect of making clear that proprietary trading losses and business losses are not insured.

1788. A court should always strive to give meaning to all of the language used. There was no rectification suit at trial. This is not one of those exceptional cases where a clear mistake allows the court to rewrite a contract to avoid absurdity or inconsistency: *Fitzgerald v*

Masters (1956) 95 CLR 420 at 426-427 (Dixon CJ and Fullagar J). Nor is the intention AHAC contends for apparent. We accept the submission by LGFS that instead, read with the insuring clause and LGFS' known business of dealing in its own products, the apparent purpose is to exclude only losses on buying and selling and not a liability for negligent or misleading advice. AHAC's construction substantially changes the meaning of the contract by reducing the scope of the insurance provided, which objectively was not intended. Finally, AHAC's submission is contrary to the *contra proferentem* rule, in that it requires (asserted) ambiguity to be resolved in favour of the *proferens*, namely AHAC itself: *Darlington Futures Limited* at 510.

1789. That rule should apply with particular rigour where the relevant clause contains AHAC's standard policy wording for professional indemnity policies. Although contained in an endorsement, the effect of the Endorsement is to replace the standard cl 3.2 of the contract. The relevant sub-cl (iii) precisely reproduces the standard sub-cl (iv) of cl 3.2 of the policy wording. The effect of Endorsement 16 is only to delete from the standard wording sub-cl 3.2(ii) but to otherwise repeat and renumber the subsequent clauses.

1790. The rewriting AHAC proposes, which we set out above, produces an unsatisfactory result in the remaining language. The clause refers to "a proprietary trading loss". Without deleting the "a" as well as "loss", "a proprietary trading" makes no sense. Deleting both words changes the subject of the sentence, and if the same change is made to "a business loss" the whole sentence ceases to make sense.

1791. The construction adopted by the primary judge is consistent with the balance of Endorsement 16. In contrast, AHAC's construction gives the exclusion in para (iii) significantly broader operation than the preceding exclusions. We do not think this to have been the objective intention. Rather the exclusions are objectively intended to be of a similar character.

1792. Contrary to AHAC's submission the relevant exclusion in Endorsement 16 has utility. It makes clear, at least, that despite the width of the insuring clause (cl 1), the cover is directed to third party claims against the insured, not the insured's own proprietary trading losses. This is reinforced in circumstances where, as we have mentioned, the provision forms part of AHAC's standard wording. We agree that there are circumstances in which Endorsement 16 may have effect to exclude a claim that would otherwise be covered. An example might be where the insured was a participant in a partnership or beneficiary of a trust of which it was manager and suffered a proprietary trading loss while other partners or beneficiaries may have a claim for the insured's provision of services to the partnership or trust. So construed the redundancy asserted by AHAC does not arise. Endorsement 16 excludes liability for the insured's own losses, not LGFS' liability for the losses of a third party.

1793. The difficulty AHAC asserts in relation to the phrase "Civil Liability" is not readily apparent. A "Civil Liability" is, relevantly, a "legally enforceable obligation". A "legally enforceable obligation" can arise out of a "loss".

1794. Finally, AHAC's reliance on Endorsement 16 fails as the "proprietary trading" (if any) was not the proximate cause of LGFS' loss. We will deal with this in more detail below.

1795. Endorsement 16 has no application. This Appeal Ground fails.

3.7 **Exclusion cl 3.3:** AHAC Appeal Grounds Matrix Row 17

1796. AHAC challenges the finding that the liability of LGFS to StateCover did not fall within the scope of exclusion cl 3.3.

1797. The StateCover claim, summarised at J[2980]-J[2990], was as follows.

1798. In late 2006 LGFS, in its capacity as StateCover's funds manager, caused StateCover to subscribe for Rembrandt 2006-2 notes with a subscription price of $10 million. The Rembrandt 2006-2 notes "cashed out", resulting in an alleged loss to StateCover. StateCover suffered a loss in the order of $9.3 million: see Part 2 , Section 6 above.

1799. In the StateCover proceedings, StateCover claimed damages for that loss, together with significant interest and costs. Initially that claim was only against LGFS. After LGFS pleaded a proportionate liability defence, StateCover joined S&P and ABN Amro as respondents in those proceedings. The claims against LGFS are summarised at J[2982] and were for breach of contract, negligence and misleading or deceptive conduct. The primary judge's finding is that the claims in negligence and for misleading or deceptive conduct were independent of, and not parasitic upon, the contract claims. LGFS settled that claim by paying $2.7 million plus agreed costs of $475,000 to StateCover. StateCover's claims against each of LGFS, ABN Amro and S&P were dismissed by consent. LGFS succeeded in its claim against AHAC for the full amount of the settlement, $3.175 million, together with an indemnity for its "Defence Costs" attributable to the claim by StateCover.

1800. AHAC submits that LGFS' liability to StateCover arose in consequence of a pleading by StateCover in its statement of claim that it was an express term of the "Letter Agreement" dated 14 September 2004 that all transactions be initiated in full compliance with board approved strategy and policy. Further, the StateCover statement of claim pleaded that the investment policy and risk policy both prohibited investments in derivative instruments and that by investing in the Rembrandt 2006-2 notes on behalf of StateCover, LGFS breached that express term. AHAC submits that each cause of action pleaded against LGFS in the StateCover claim arises out of or is based upon or is attributable to a liability that LGFS had to StateCover and which was assumed or accepted by LGFS under the Letter Agreement.

1801. The primary judge found that the Rembrandt notes were a derivative instrument. AHAC submits that although her Honour made no express finding, it can be inferred from the finding that the Rembrandt notes were derivatives that LGFS breached the express term in the agreement with StateCover that all transactions be initiated in compliance with board approved strategy and policy. AHAC then submits that this breach is the proximate cause of LGFS' liability to StateCover.

1802. Her Honour's rejection of AHAC's submission depends on two points of construction.

1803. The first is whether "such liability" in cl 3.3 refers to a liability of the same type or to any liability howsoever arising. AHAC submits that the ordinary use of language is that "such" liability is a liability of the same type.

1804. The second point concerns the phrase "in the absence of such contract or agreement". AHAC submits that whatever the proper construction of "such liability", LGFS would have had no liability to StateCover in the absence of the relevant agreements because they were the only bases of the relationship.

1805. We agree with the submissions put by LGFS, which broadly reflect the conclusions of the primary judge, as follows.

1806. Clause 3.3 is an exclusion which excludes loss "[a]rising out of, based upon, or attributable to any liability to a third party assumed or accepted by [LGFS] under any contract or agreement". It is subject to an exception "to the extent such liability would have attached to [LGFS] in the absence of such contract or agreement".

1807. The words "such liability" in cl 3.3 are not a reference to the excluded contractual liability. These words are part of the exception. They mean the same liability as would have attached irrespective of the contract. The scope of the exclusion is not to be determined without regard to the exception within the exclusion clause: J[3714]. The words "such liability" in the exception mean the liability to a third party referred to in the earlier part of the exception. StateCover had only one claim, although a number of causes of action were pleaded. On the proper construction of cl 3.3, if LGFS were liable to StateCover in negligence or for misleading or deceptive conduct then the exclusion has no application. That construction accords with the words used, and the evident purpose of the exclusion. The primary judge found that LGFS was exposed to liability to StateCover in tort and under statute: J[3715]. Indeed, her Honour stated that LGFS would have had great difficulty in avoiding a duty of care to StateCover and that the Rembrandt notes were a "profoundly unsuitable" investment for a body such as StateCover: J[3717].

1808. AHAC's contrary alternative construction that once there is a liability in contract for a loss, the exclusion applies, would give the exception no work to do.

1809. The chapeau to cl 3 directs attention relevantly to a "Civil Liability", and the exclusion is of a "Civil Liability [relevantly a legally enforceable obligation] … [a]rising out of, based upon, or attributable to any liability to a third party *assumed or accepted* by [LGFS] under any contract or agreement except to the extent such liability would have attached to [LGFS] in the absence of such contract or agreement" (emphasis added). The prospective legally enforceable obligation arose because of the asserted negligence on the part of LGFS in providing services to StateCover, and arose irrespective of the Letter Agreement. It is the provision of the services, not the existence of the agreement, which constitutes the relevant assumption of responsibility. Similarly, LGFS' obligation not to engage in misleading or deceptive conduct, or to pay damages if it does, is a legislative requirement binding upon LGFS. This exists apart from any contractual obligation. Exposure to liability in tort or under statute would have arisen absent contract, for example, as LGFS submits, if LGFS was providing the service as a volunteer, under a contract which was void or in some other circumstance in which there was no contract. These causes of action, to employ the language of the primary judge at J[3715], were not parasitical to the contract claims.

1810. AHAC's contrary contention is that LGFS was liable to StateCover pursuant to a term of the agreement between LGFS and StateCover in circumstances where the liability would not have arisen in the absence of such agreement. The primary judge rejected that argument: J[3714]-J [3715]. Her Honour was correct for the following reasons.

1811. First, it is necessary to identify the relevant agreement and the duties owed by LGFS to StateCover under that agreement and at law. At the time StateCover invested in the Rembrandt 2006-2 notes the agreement between LGFS and StateCover was recorded in the Letter Agreement. The issue is whether LGFS' liability arose completely under and because of the Letter Agreement, and otherwise would not have been incurred in LGFS performing its funds management function. It did not so arise. Liability would have been incurred in the absence of such agreement. LGFS in performing a funds management function owed a duty to exercise reasonable care.

1812. The duties imposed on LGFS, by reason of the function performed, were concurrent duties in contract and tort: *Astley v Austrust Limited* at 21-23 [46]-[48]. StateCover pleaded the implied duty to exercise due care and skill in its statement of claim. The tortious liability included but also extended beyond the obligation to exercise care to comply with the StateCover investment policy. For example, arguably LGFS owed a duty to exercise reasonable care to cause StateCover to buy only suitable products.

1813. StateCover also pleaded that a term was implied into the Letter Agreement (the reference to "Outsourcing Agreement" in the pleading is clearly a typographical error) by s 12ED of the *ASIC Act* . The perceived liability to StateCover arose under the term implied by s 12ED of the *ASIC Act* as to due care and skill. This liability is not within the operation of the exclusion.

1814. The promise relied on by AHAC, and by StateCover as one of its claims in its pleading, appears from the words in the Letter Agreement "[i]n undertaking these functions [that is as funds manager] LGFS will comply with the policies and requirements of StateCover". AHAC's case appears to be that LGFS' prospective liability to StateCover had arisen only from the contention that the Rembrandt notes were "derivatives" and that, in causing StateCover to buy the notes, LGFS had breached its contractual promise to comply with the StateCover policy. That is not the case. In performing the function of funds manager LGFS had the power to, and assumed responsibility to cause StateCover to, acquire and dispose of investments, and owed a duty to StateCover to exercise reasonable care to comply with StateCover's policies and requirements: see *Woolcock* at 530-531 [22]-[24] . If LGFS breached the agreement with StateCover it also breached its common law and statutory duties. That is consistent with StateCover's pleading of concurrent duties, and overlapping allegation of a breach of duty of care to competently advise.

1815. AHAC's submissions characterising StateCover's case as not being a failure to advise case are incorrect. StateCover pleaded a duty to provide "investment management services with due care and skill" and pleaded a breach including a failure to advise and a failure to properly investigate. The breach relied on was a breach of that duty in tort.

1816. For these reasons, this Appeal Ground fails. Exclusion 3.3 was not engaged.

3.8 Was an excluded cause a proximate cause?: AHAC Appeal Grounds Matrix Rows 10 and 18

1817. AHAC submits that the primary judge erred in failing to find that, because one of the proximate causes of the loss of LGFS was a cause excluded by the policy, AHAC had no liability to indemnify LGFS.

1818. Where there are two proximate causes of a loss, one within the scope of the policy and the other falling within the exclusion clause, the insurer has no liability to indemnify: *Wayne Tank and Pump Co Ltd v Employers Liability Assurance Corporation Ltd* [1974] QB 57 at 69 and 74-75 ; *City Centre Cold Store Pty Ltd v Preservatrice Skandia Insurance Ltd* (1985) 3 NSWLR 739 at 744-745 .

1819. It may be accepted that if the liability arises from matters falling within the scope of Endorsement 16, then AHAC is not obliged to indemnify, even if the liability could also be attributed to a cause falling outside the exclusion and within the scope of the cover.

1820. The same principle applies if a proximate cause of the loss is a cause excluded by Endorsement 17, relating relevantly, to conflict of interest, referred to above.

1821. AHAC submits that the primary judge erred by not applying the exclusions and erred in not applying the principle that if there are two proximate causes of a loss, one within the scope of the policy and the other falling within the exclusion clause, the insurer has no liability to indemnify.

1822. Clause 3.3 is qualified by the expression "arising out of, based upon or attributable to". AHAC submits that any negligence claim or any statutory misleading or deceptive conduct claim brought by StateCover originates in or springs from the Letter Agreement between LGFS and StateCover thus constituting two proximate causes of the loss and thereby invoking the *Wayne Tank* principle.

1823. These grounds primarily fail because the exclusions relied on by AHAC are not engaged.

1824. For other reasons, AHAC's submissions on these grounds fail at the threshold. They conflate two concepts. Whether the StateCover claim is within the cl 3.3 exception does not raise a question of the interrelationship between an insured proximate cause and an excluded proximate cause. The issue, as we have explained, is one of construction of cl 3.3. Apart from the claim in contract the liability would likely also have attached absent that contract. Thus the exclusion does not apply. Questions of proximate cause do not arise. For reasons we have already identified, liability likely would have attached to LGFS in negligence and for misleading or deceptive conduct. Each of those causes of action arose irrespective of contract.

1825. However, should we be wrong about that and our conclusions concerning Endorsement 16, we are nonetheless of the opinion that "proprietary trading" was not the proximate cause of LGFS' loss.

1826. We agree that in relation to the Councils' claim against LGFS, the relevant loss was caused by what LGFS said or did not say, not by LGFS' ownership of the Rembrandt notes or "proprietary trading". The "proprietary trading" was not the effective, operative or proximate cause. Whether LGFS owned the notes or was selling an instrument owned by a third party was irrelevant to LGFS' liability to the Councils. That reasoning also applies to the breach of fiduciary duty claim as the liability in equity arises from what was said or left unsaid, and the conflict existed in either event.

1827. AHAC's alternative contention was that the primary judge erred in finding that LGFS' loss consisting of the amount of its liability to the Councils for breach of fiduciary duty was not caused by the same conduct of S&P and ABN Amro which the primary judge found was a cause of LGFS' loss consisting of its loss on the resale of the LGFS Retained Notes: AHAC Appeal Grounds Matrix Row 11. This Appeal Ground was not addressed by AHAC in its written or oral submissions. We can identify no error in the reasoning of the primary judge. This Appeal Ground fails.

3.9 Whether the settlement of the StateCover proceedings was reasonable?: AHAC Appeal Grounds Matrix Row 19

1828. AHAC challenges the finding that the settlement of the StateCover claim by LGFS was reasonable: J[3716]-J[3719].

1829. AHAC raises two arguments: whether the settlement was reasonable, and whether the settlement was in accordance with LGFS' duty of utmost good faith.

1830. AHAC submits that the evidence called by LGFS demonstrated that the settlement was not reasonable having regard to the merits of the litigation.

1831. It also submits that the evidence of Mr Peter Lambert, the Chief Executive Officer of LGFS, demonstrated that the settlement involved a breach of LGFS' duty of utmost good faith to AHAC as it showed that LGFS thought it was a good idea to settle with StateCover not because it had analysed the exposure to risk, but because of the view that AHAC would be liable to pay the sum, whatever it was, to LGFS.

1832. The primary judge determined that the good faith issue should not be permitted to be raised as it was not pleaded. However, AHAC submits that because it did not admit the reasonableness of the settlement this put the question of reasonableness, including good faith, in issue.

1833. We do not agree. It was too late to raise that case at trial. It should have been pleaded with particularity. If it had been pleaded it may well have been capable of being met with evidence and not only from Mr Lambert. A non-admission by AHAC of the reasonableness of the settlement does not mean that LGFS had to positively prove good faith.

1834. Nonetheless we will consider the submissions regarding good faith.

1835. There is no issue on appeal as to the applicable principle. If the settlement was a result of the insured not acting in good faith towards the insurer or a settlement in which the insurer's interests were sacrificed, then the settlement is not reasonable: *Broadlands Properties Limited v Guardian Assurance Company Limited* (1984) 3 ANZ Insurance Cases ¶60-552 at 78,323-78,325.

1836. AHAC submits that an objective reading of the evidence before LGFS at the time it made the decision to settle the StateCover proceedings demonstrates that it was completely indifferent to its obligations under the policy. It points in particular to the following evidence.

1837. A briefing note to the LGFS board prepared by Norton Rose, lawyers, on or about 24 May 2011, regarding the proposed StateCover settlement, included the following:

> If Chartis is willing to make a contribution to the StateCover settlement amount, LGFS would need to be prepared to pay the balance of the settlement amount without recourse to indemnity from the insurer ... Even though LGFS would still seek to recover from S&P and ABN [Amro] contribution to or indemnity for the amount it would have to pay, we would not recommend proceeding with this course (and releasing Chartis from the claim in relation to StateCover) unless Chartis is prepared to make a substantial contribution (ie around $2,500,000).

Chartis was the trading name of AHAC.

1838. Accordingly, as at May 2011, LGFS was advised not to compromise its indemnity claim for less than 80% of the total settlement sum, regardless of the fact that LGFS would still seek to recover contribution from S&P and ABN Amro.

1839. The board briefing note also refers to the possibility of approaching ABN Amro and S&P to attempt to persuade them to make a contribution to the StateCover settlement in exchange for LGFS giving up its claims against them. The briefing note states: "[i]n this regard we note that any contribution by ABN [Amro] and S&P would need to be significant in order to justify LGFS giving up its claims against these parties".

1840. A letter from Norton Rose dated 9 August 2011 advised LGFS as to the reasonableness of the StateCover offer and the implications for LGFS of accepting it. It contained Norton Rose's views as to the likelihood of LGFS being able to recover some or part of the settlement sum from ABN Amro, S&P and AHAC which included that:

> 1. There is a risk that LGFS will only be able to recover a proportion (rather than the whole) of the settlement sum from ABN Amro and/or S&P;
>
> 2. The risk of making no recovery from ABN Amro or S&P is low; and
>
> 3. LGFS' prospects of obtaining an order that AHAC indemnify it in respect of the settlement sum are strong.

1841. AHAC emphasises that the relevant evidence of Mr Lambert in cross-examination was to the effect that the advice which LGFS had before settlement was that it had a very strong case and very strong prospects of success in defeating the StateCover claim. LGFS had advice that its prospects of success with respect to the proportionate liability defence concerning S&P and ABN Amro were very strong and that if its proportionate liability defence succeeded S&P would pay 100% of the loss.

1842. AHAC submits that the most cogent documentary evidence is the letter dated 9 August 2011 from Norton Rose and the Circular Resolution from Mr Lambert dated 10 August 2011. Mr Lambert's evidence was that the contents at para 1.4(1), (2) and (3) of the Norton Rose letter comprised the totality of the reasons given by those lawyers about why the StateCover settlement should be accepted. Those paragraphs, AHAC points out, contain no analysis of the prospects of success of the StateCover claim. The summary contained in Mr Lambert's Circular Resolution is, as the primary judge described it, the essence of the reasons why the board of LGFS decided to settle. AHAC submits that the heart of that reasoning was in para 2 of the summary, which is in the following terms:

> From the perspective of a lay person involved in the case I believe that this settlement should be accepted, because it effectively decreases the 'worst case' scenario from a $10m loss to a $3mill loss without changing the expected outcome of $0 cost to LGFS. This expected outcome assumes that we may recover some or all of this payment from ABN [Amro] and/or S&P. Any balance remaining would be recoverable under the insurance policy should the court rule in our favour in that matter.

1843. The following exchange occurred in cross-examination:

> *Was your approach to settlement [of] this, Mr Lambert, 'we can pay this $3 million because we'll pick it up from the insurer, come what may'?*....Come what may, yes.

1844. We reject AHAC's submissions that LGFS failed to prove that the settlement was reasonable, judged objectively, based on the material which was available to it at the time of the settlement: *Unity Insurance Brokers Pty Limited v Rocco Pezzano Pty Limited* (1998) 192 CLR 603 at 653 (Hayne J).

1845. The primary judge correctly identified the question as being whether the settlement was objectively reasonable. There was considerable evidence to sustain her Honour's conclusions concerning the risks to which LGFS would be exposed in litigation with StateCover, not least being her Honour's views as to breach of duty by LGFS.

1846. The most compelling reason supporting the conclusion that the settlement was reasonable is the implicit and unchallenged finding by the primary judge that LGFS would likely have been liable to StateCover in negligence: J[3717]-J[3718]. Moreover, it seems that the effect of the settlement was that LGFS settled for approximately 25% of its potential liability, and retained its right to pursue S&P and ABN Amro for contribution. This alone supports the finding that the StateCover settlement was reasonable.

1847. LGFS was StateCover's funds manager and was responsible for StateCover's investment portfolio, and in practical terms determined StateCover's risk appetite. If anything, as we will explain, the StateCover duty case against LGFS was stronger than the Councils' case. StateCover is a mutual insurer. Those investments it made had to be balanced between producing returns and availability to meet claims, including spikes in claims. StateCover's breach of duty case was stronger than the Councils' case for a number of reasons. First, the term of the Rembrandt 2006-2 notes compared to StateCover's liabilities, the illiquidity of the notes, there being no promise by LGFS to buy those notes back, the potential fluctuations in the market value of those notes and the risks associated with the notes. Second, the fact that LGFS knew what StateCover's investments were and the demands on those investments. Third, that LGFS as funds manager made the decision to invest for StateCover. LGFS, consistent with the complete delegation of StateCover's investment function to it, did not warn StateCover of risks associated with subscribing for the Rembrandt 2006-2 notes. No question of reliance arose as LGFS was the decision maker.

1848. That the primary judge after a long trial found LGFS would likely have been, but for the settlement, liable to StateCover demonstrates, at least, that there was a substantial risk of a judgment adverse to LGFS in the suit brought against it by StateCover.

1849. The only real question in relation to damages was LGFS' proportionate liability defence. S&P and ABN Amro denied any liability to StateCover. On the basis of S&P and ABN Amro's defence of the Councils' claims, it is highly likely both would have continued to deny StateCover's claim. That created a risk appropriately to be taken into account in assessing the reasonableness of the settlement.

1850. At the time of the settlement StateCover's claim against LGFS was about $12 million (loss of approximately $9.3 million plus interest) plus costs. LGFS settled that claim for about a quarter of that amount, plus agreed costs. At the time of the settlement LGFS was facing the additional exposure of further interest and the further costs incurred by StateCover in prosecuting the matter to a trial lasting three months, a period which would have been lengthened by the StateCover proceedings. In the event of a total failure of its defences and cross-claims, LGFS would also have been exposed to the costs of S&P and ABN Amro and its own costs in relation to the StateCover proceedings.

1851. There is no suggestion that LGFS could have negotiated a better settlement. Inevitably such settlements require prudent judgment. The prospect of complete success needs to be balanced against the risks of failure. The latter, in this case, were substantial. Settlement of a complicated commercial case with the attendant risks to which we referred for around 25 cents in the dollar was reasonable.

1852. Finally, LGFS had legal advice from a major law firm to the effect that the offer LGFS ultimately accepted was "very attractive". This, it seems to us, was sound advice in light of all that we have explained. This included advice not only as to the possibilities of recovering the whole or part of the settlement sum from ABN Amro and S&P, to which AHAC referred in its submissions, but also the possibility that it may not be able to recover any of that amount from them. In viewing the risks it faced, as is evident from Mr Lambert's Circular Resolution, the worst case scenario of a $10 million loss was contemplated. The advice from Norton Rose to which AHAC refers must be seen in context. This was advice as to whether or not to accept a settlement offer at a significant discount.

1853. AHAC's assertion that LGFS "was completely indifferent to its obligations under the [p]olicy" in settling the StateCover proceedings is not supported by the evidence. Rather, the evidence is to the contrary. AHAC would not participate in the settlement. LGFS was required to negotiate an agreement with AHAC that the settlement sum be treated as a "Civil Liability". Further, AHAC, having not confirmed the indemnity informed LGFS that it should act as a prudent uninsured: J[3716]. These matters are inconsistent with LGFS ignoring the terms of the policy.

1854. As the primary judge correctly observed (at J[3716]) the fact that LGFS believed that it had a good claim against AHAC does not suggest that the settlement was in bad faith. Objectively that belief suggests the opposite. That LGFS settled with StateCover tends to prove that LGFS believed that the settlement was, at least, a reasonable settlement and also that LGFS recognised a risk that it may not be insured. We accept the submission that if LGFS had thought it was certainly covered there is no reason why it would have agreed to the settlement as, on that hypothesis, LGFS was not at risk on the StateCover claim. Nor would it have had reason to be out of its money while it sued AHAC. The objective facts demonstrate that LGFS wished to preserve a position where it could maintain its claim against AHAC but accept an offer which was "very attractive".

1855. In that context the options available to LGFS were identified by LGFS' solicitors. The first option was to settle with StateCover and to settle LGFS' claim against AHAC in relation to the StateCover proceedings at the same time: para 4.1(1) of Norton Rose's note. The second option was to procure AHAC's agreement to a settlement being treated as a "Civil Liability" and then to settle and pursue the claim against AHAC: para 4.1(2). The first option is explained and Norton Rose advised that they "would not recommend proceeding with this course ... unless [AHAC] is prepared to make a substantial contribution (ie around [$2.5 million])".

1856. That LGFS considered that it may be able to recover part of the settlement from ABN Amro or S&P does not advance AHAC's argument. The claim for contribution or damages potentially reduced AHAC's liability. That the 9 August 2011 advice from Norton Rose refers to that possibility does not support AHAC's allegation of bad faith; it shows LGFS was acting on good advice.

1857. Mr Lambert's evidence does not support AHAC's bad faith submissions. Mr Lambert knew that there was a risk that LGFS could be liable to StateCover. He had received advice in the form of summaries. Mr Lambert did not concede that he failed to seek advice as to the prospects of success on particular aspects of the claim. However, he did say that he had always found it very difficult to get advice from lawyers as to the exact probability of success. This hardly evidences a lack of good faith. Rather, it recognises the reality that litigation is to one degree or another uncertain. As Mr Lambert said, LGFS settled because "here was a settlement of substantially less than the amount claimed, and it was in our commercial interests to make that settlement". Objectively that was a reasonable step to take in the circumstances. It was a reasonable settlement reached in good faith.

1858. No error on the part of the primary judge has been established. This Appeal Ground fails.

PART 15: ORDERS

1859. The parties are directed to confer and bring in agreed orders to give effect to these reasons for judgment including the question of costs by 4:00pm on 13 June 2014. If the orders cannot be agreed, then the parties are to file a joint document which identifies the areas of agreement, the areas of disagreement and, for the areas of disagreement, the reason or reasons for that disagreement by 4:00pm on 13 June 2014.

I certify that the preceding one thousand eight hundred and fifty- nine (1,859) numbered paragraphs are a true copy of the Reasons for Judgment herein of the Honourable Justices Jacobson, Gilmour and Gordon.

Associate:

Dated: 6 June 2014

ATTACHMENT A - GLOSSARY OF DEFINED TERMS

-

TERM	DEFINITION
ABN Amro	ABN AMRO Bank NV, an investment bank and the creator of the Rembrandt notes.
AFSL	Australian financial services licence.
AHAC	American Home Assurance Company.
Anti-DPN	A new product developed by ABN Amro which became the CPDO.
ASIC	Australian Securities and Investments Commission.
ASIC Act	*Australian Securities and Investments Commission Act 2001* (Cth).
AUD	Australian dollars.
Bathurst	Bathurst Regional Council.
BBSW	Bank Bill Swap Rate, a reference rate based on the interest rates at which banks borrow unsecured funds.
bps	Basis points, generally used to describe percentage changes in prices. One basis point or bp is equivalent to 0.01%.
Castle	A series of ABN Amro CPDOs.

CDO	Collateralised debt obligations, another structured financial product, being a different product from the CPDO.
CDS	A credit default swap contract, or a contract relating to credit default risk. A typical CDS involves one party (the protection seller) selling to another party (the protection buyer) protection against the risk of a credit event. CDSs may be actual or notional.
CDS default payment	The sum paid by the protection seller to the protection buyer on the occurrence of a credit event (see **CDS** above).
CDS premium fee	The fee paid by the protection buyer to the protection seller for protection against the risk of a credit event (see **CDS** above).
CDX	The CDX North America Investment Grade Index, which references US credit default swaps.
Civil Liability Act	*Civil Liability Act 2002* (NSW).
Community income CPDO notes	The Rembrandt 2006-3 notes which LGFS purchased and sold to the Councils. LGFS named these notes "community income notes" and referred to them as such in its dealings with Councils.
Cooma	Cooma-Monaro Shire Council.
Corporations Act	*Corporations Act 2001* (Cth).
Corowa	Corowa Shire Council.
CPDO	Constant proportion debt obligation and was the name given to the new financial product developed by ABN Amro in 2006. CPDO notes were issued in series by special purpose vehicles under names including Castle, Chess, and, in Australia, Rembrandt.

CPDO Evaluator	A mathematical tool for modelling CPDOs and rating CPDO index transactions. The model was developed by S&P and launched on 22 March 2007.
CPDO letter	A standard form letter prepared by LGFS entitled "CPDO – The Next Generation" designed to introduce the CPDO to councils.
Councils	The PA Councils and Bathurst.
CPPI	Constant proportion principal insurance, another financial product which pre-dated the CPDO. An ABN Amro DPN is a type of CPPI.
Deniliquin	Deniliquin Shire Council.
DLG	New South Wales Department of Local Government.
DLG 2006 circular	A circular issued to all councils by the Director-General of the Department of Local Government on 27 November 2006.
DPN	Dynamic Participation Note, ABN Amro's CPPI product.
ECD Group	ABN Amro's London based Exotic Credit Derivatives Group, responsible within ABN Amro for structuring, trading and marketing structured credit products such as CDOs and CPPIs.
Eurobodalla	Eurobodalla Council.
FRNs	A floating rate note, another financial product.
FuturePlus	FuturePlus Financial Services Pty Ltd, the head of the company group of which LGSS and its subsidiary LGFS formed part after LGSS' acquisition of LGFS in October 2004.
GFC	Global Financial Crisis.

Globoxx	The Globoxx Index, which is made up of the CDX and iTraxx weighted 50% each
Grove report	A report issued by Grove Research and Advisory about the Rembrandt CPDO dated 16 November 2006.
ICA	*Insurance Contracts Act 1984* (Cth) .
iTraxx	The iTraxx Europe Index, which references European corporate default swaps.
LGFS	Local Government Financial Services Pty Ltd.
LGFS community income notes brochure	A brochure prepared by LGFS in order to market the community income notes (or the Rembrandt CPDO or Rembrandt 2006-3 notes) to councils.
LGFS Retained Notes	$26 million of the Rembrandt 2006-3 notes retained by LGFS and not sold to the Councils.
LGFS Sold Notes	$19 million of the Rembrandt 2006-3 notes sold by LGFS to the Councils.
LGSS	Local Government Superannuation Scheme owned by FuturePlus.
LIBOR	The London Interbank Offered Rate, a reference rate based on the interest rates at which banks borrow unsecured funds.
LTAS	The long-term average spread of the indices referenced by the financial product, in the case of the CPDO the Globoxx index (the combined iTraxx and CDX indices weighted 50% each).
Local Government Act	*Local Government Act 1993* (NSW) .

Mandate Letter	Contract between ABN Amro and LGFS made in October 2006 in respect of the Rembrandt 2006-3 notes.
Ministerial Order	An order made by the Minister for Local Government and amended from time to time specifying the forms of investment in which a council may invest, pursuant to s 625(2) of the *Local Government Act* .
Moody's	Moody's Investors Service Inc, a ratings agency.
Moree	Moree Plains Shire Council.
MR	Mean reversion speed, the speed with which credit spread levels are expected to return to their average level after a period where they deviated from the historically observed mean.
Murray	Murray Shire Council.
Narrandera	Narrandera Shire Council.
Narromine	Narromine Shire Council.
NAV	Net asset value.
NRB Councils	The Councils that did not enter into a Right Balance Agreement with LGFS – Bathurst, Deniliquin, Eurobodalla, Moree, Murray, Narrandera, Narromine, Oberon, Orange, Parkes and Ryde.
NSW Local Government Investments Best Practice Guide	A draft document prepared by two industry bodies, Local Government Financial Professionals and Local Government Managers' Association.
Oberon	Oberon Shire Council.
Orange	Orange City Council.

PA Councils	Twelve councils in New South Wales comprising Cooma, Corowa, Deniliquin, Eurobodalla, Moree, Murray, Narrandera, Narromine, Oberon, Orange, Parkes and Ryde.
Parkes	Parkes Shire Council.
Pre-Sale Report	Report prepared and issued by S&P about Rembrandt 2006-2 on 11 August 2006. It is called a pre-sale report because the Rembrandt 2006-2 notes were issued on 5 September 2006, after the publication of this report.
Post-Sale Report	Report prepared and issued by S&P about Rembrandt 2006-3 on 16 November 2006. It is called a post-sale report because the Rembrandt 2006-3 notes were issued on 31 October 2006, before the publication of this report.
R-2 Ratings Letter	Ratings Letter dated 5 September 2006, issued by S&P to ABN Amro confirming a public credit rating of AAA to Rembrandt 2006-2.
R-3 Ratings Letter	Ratings Letter dated 31 October 2006, issued by S&P to ABN Amro confirming a public credit rating of AAA to Rembrandt 2006-3.
RAMP	Rating analysis meeting paper, a report by a primary analyst used in S&P committee meetings to assist in determining what rating should be assigned to a product.
Ratings Letters	The R-2 Ratings Letter and the R-3 Ratings Letter.
RB Councils	The Councils that entered into a Right Balance Agreement with LGFS – Cooma and Corowa.
Rembrandt 2006-2	The first issue of the CPDO notes in Australia, relevantly, the subject of the purchase by StateCover.
Rembrandt 2006-3	

	The second issue of the CPDO notes in Australia (AUD$45 million), also referred to by LGFS and the Councils as community income notes, relevantly, the subject of the purchase by LGFS and on-sale of part of them to the Councils.
Rembrandt notes	The Australian issue of ABN Amro's CPDO, being Rembrandt 2006-2 and Rembrandt 2006-3.
Right Balance Agreement	Agreement offered by LGFS to some of the councils and into which two councils entered (Cooma and Corowa).
Right Balance brochure	A brochure describing LGFS' Right Balance service provided to some councils in or about 2005.
Right Balance letter	A standard form letter prepared by LGFS designed to accompany the Right Balance brochure sent to some councils in late 2005 and 2006 in respect of the Right Balance service.
Right Balance Service	The services provided by LGFS to the RB Councils set out in Schedule 1 to the Right Balance Agreement.
Ryde	Ryde Council.
S&P	Standard & Poors, a division of McGraw-Hill Companies Inc, and a ratings agency.
S&P Reports	The **Pre-Sale Report** or the **Post-Sale Report**, insofar as there are no material differences between the two.
SCM Group	ABN Amro's Structured Credit Marketing Group.
SOC	Statement of claim.
Surf CPDO	The generic name given by ABN Amro to its CPDO product.

Surf Presentation	A marketing presentation prepared by ABN Amro about the CPDO intended to be provided to ABN Amro clients.
StateCover	StateCover Mutual Limited.
TPA	*Trade Practices Act 1974* (Cth) .

SCHEDULE OF PARTIES

NSD 501 of 2013

MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Second Appellant

LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)
Third Appellant

AMERICAN HOME ASSURANCE COMPANY (ABN 007 483 267753)
Fourth Appellant

COOMA MONARO SHIRE COUNCIL (ABN 19 204 741 100)
Second Respondent

COROWA SHIRE COUNCIL (ABN 43 874 223 315)
Third Respondent

DENILIQUIN COUNCIL (ABN 41 992 919 200)
Fourth Respondent

EUROBODALLA SHIRE COUNCIL (ABN 47 504 455 945)
Fifth Respondent

MOREE PLAINS SHIRE COUNCIL (ABN 46 566 790 582)
Sixth Respondent

MURRAY SHIRE COUNCIL (ABN 77 334 235 304)
Seventh Respondent

NARRANDERA SHIRE COUNCIL (ABN 96 547 765 569)
Eighth Respondent

NARROMINE SHIRE COUNCIL (ABN 99 352 328 504)
Ninth Respondent

OBERON COUNCIL (ABN 13 632 416 736)
Tenth Respondent

ORANGE CITY COUNCIL (ABN 85 985 402 386)
Eleventh Respondent

PARKES SHIRE COUNCIL (ABN 96 299 629 630)
Twelfth Respondent

CITY OF RYDE (ABN 81 627 292 610)
Thirteenth Respondent

ABN AMRO BANK NV ARBN 84 079 478 612
Fourteenth Respondent

MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Fifteenth Respondent

LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)
Sixteenth Respondent

AMERICAN HOME ASSURANCE COMPANY (ABN 007 483 267753)
Seventeenth Respondent

NSD 502 of 2013

LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)
Second Respondent

ABN AMRO BANK NV (ARBN 84 079 478 612)
Third Respondent

NSD 503 of 2013

COROWA SHIRE COUNCIL (ABN 43 874 223 315)
Second Respondent

DENILIQUIN COUNCIL (ABN 41 992 919 200)
Third Respondent

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MOREE PLAINS SHIRE COUNCIL (ABN 46 566 790 582)
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MURRAY SHIRE COUNCIL (ABN 77 334 235 304)
Sixth Respondent

NARRANDERA SHIRE COUNCIL (ABN 96 547 765 569)
Seventh Respondent

NARROMINE SHIRE COUNCIL (ABN 99 352 328 504)
Eighth Respondent

OBERON COUNCIL (ABN 13 632 416 736)
Ninth Respondent

ORANGE CITY COUNCIL (ABN 85 985 402 386)
Tenth Respondent

PARKES SHIRE COUNCIL (ABN 96 299 629 630)
Eleventh Respondent

CITY OF RYDE (ABN 81 627 292 610)
Twelfth Cross Appellant

LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)
Thirteenth Respondent

MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Fourteenth Respondent

NSD 504 of 2013

COROWA SHIRE COUNCIL (ABN 43 874 223 315)
Second Respondent

DENILIQUIN COUNCIL (ABN 41 992 919 200)
Third Respondent

EUROBODALLA SHIRE COUNCIL (ABN 47 504 455 945)
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MOREE PLAINS SHIRE COUNCIL (ABN 46 566 790 582)
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MURRAY SHIRE COUNCIL (ABN 77 334 235 304)
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Seventh Respondent

NARROMINE SHIRE COUNCIL (ABN 99 352 328 504)
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OBERON COUNCIL (ABN 13 632 416 736)
Ninth Respondent

ORANGE CITY COUNCIL (ABN 85 985 402 386)
Tenth Respondent

PARKES SHIRE COUNCIL (ABN 96 299 629 630)
Eleventh Respondent

CITY OF RYDE (ABN 81 627 292 610)
Twelfth Cross Appellant

LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)
Thirteenth Respondent

ABN AMRO BANK NV (ARBN 84 079 478 612)
Fourteenth Respondent

NSD 505 of 2013

COOMA MONARO SHIRE COUNCIL (ABN 19 204 741 100)
Second Respondent

COROWA SHIRE COUNCIL (ABN 43 874 223 315)
Third Respondent

DENILIQUIN COUNCIL (ABN 41 992 919 200)
Fourth Respondent

EUROBODALLA SHIRE COUNCIL (ABN 47 504 455 945)
Fifth Respondent

MOREE PLAINS SHIRE COUNCIL (ABN 46 566 790 582)
Sixth Respondent

MURRAY SHIRE COUNCIL (ABN 77 334 235 304)
Seventh Respondent

NARRANDERA SHIRE COUNCIL (ABN 96 547 765 569)
Eighth Respondent

NARROMINE SHIRE COUNCIL (ABN 99 352 328 504)
Ninth Respondent

OBERON COUNCIL (ABN 13 632 416 736)
Tenth Respondent

ORANGE CITY COUNCIL (ABN 85 985 402 386)
Eleventh Respondent

PARKES SHIRE COUNCIL (ABN 96 299 629 630)
Twelfth Respondent

CITY OF RYDE (ABN 81 627 292 610)
Thirteenth Respondent

ABN AMRO BANK NV (ARBN 84 079 478 612)
Fourteenth Respondent

MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Fifteenth Respondent

AMERICAN HOME ASSURANCE COMPANY (ABN 67 007 483 267)
Sixteenth Respondent

NSD 522 of 2013

LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)
Second Respondent

ABN AMRO BANK NV (ARBN 84 079 478 612)
Third Respondent

MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Fourth Respondent

NSD 523 of 2013

COROWA SHIRE COUNCIL (ABN 43 874 223 315)
Second Respondent

DENILIQUIN COUNCIL (ABN 41 992 919 200)
Third Respondent

EUROBODALLA SHIRE COUNCIL (ABN 47 504 455 945)
Fourth Respondent

MOREE PLAINS SHIRE COUNCIL (ABN 46 566 790 582)
Fifth Respondent

MURRAY SHIRE COUNCIL (ABN 77 334 235 304)
Sixth Respondent

NARRANDERA SHIRE COUNCIL (ABN 96 547 765 569)
Seventh Respondent

NARROMINE SHIRE COUNCIL (ABN 99 352 328 504)
Eighth Respondent

OBERON COUNCIL (ABN 13 632 416 736)
Ninth Respondent

ORANGE CITY COUNCIL (ABN 85 985 402 386)
Tenth Respondent

PARKES SHIRE COUNCIL (ABN 96 299 629 630)
Eleventh Respondent

CITY OF RYDE (ABN 81 627 292 610)
Twelfth Respondent

LOCAL GOVERNMENT FINANCIAL SERVICES PTY LIMITED (ACN 001 681 741)
Thirteenth Respondent

ABN AMRO BANK NV (ARBN 84 079 478 612)
Fourteenth Respondent

MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Fifteenth Respondent

NSD 524 of 2013

ABN AMRO BANK NV (ARBN 84 079 478 612)
Second Respondent

MCGRAW-HILL INTERNATIONAL (UK) LIMITED
Third Respondent

Cited by:

Australian Securities and Investments Commission v Macrolend Pty Ltd (No 3) [2025] FCA 1158 -
Australian Securities and Investments Commission v Wallet Ventures Pty Ltd [2025] FCAFC 93 (24 July 2025)

24. The appellant puts its grounds of appeal as follows:

Deposit of money or loan

1. The primary judge erred in holding that the Finder Earn product was not a debentu
of moneys or a loan to the Respondent when an investor used the Finder Earn product (at J

a. on the proper construction of the Terms (as defined in the Judgment), the inv
Earn product and entering into a single arrangement to acquire TAUD and transfer

b. by s 761B of the Act and because it is reasonable to assume that the parties to
arrangement, the acquisition of TAUD and transfer of that TAUD to the Responden
purpose of determining whether the Finder Earn product was a debenture.

Undertaking to repay moneys "deposited or lent" as a debt

2. The primary judge erred in holding that the Finder Earn product was not a debentu
as a debt (at J[98]-[100]) because:

a. the definition required that the money deposited or lent had to be used for th
there is no requirement that the money be so used (to the extent the Full Court in *AB*
eld that the definition of debenture in the Act imports the notion of an undertaking t
is wrongly decided); or in the alternative

b. the primary judge held that the money was not deposited or lent as part of th
capital.

Australian Securities and Investments Commission v Wallet Ventures Pty Ltd [2025] FCAFC 93 -
Silk v Silk [2025] VSC 428 -

Australian Securities and Investments Commission v M101 Nominees Pty Ltd (in liq) (No 8) [2025] FCA 741 (09

391. There is some controversy concerning whether the Full Court's reference, in *ABN AMRO* , to an "u
was intended to impose a discrete requirement that, in order to be a debenture, the loan must hav

Australian Securities and Investments Commission v M101 Nominees Pty Ltd (in liq) (No 8) [2025] FCA 741 (09

364. At the outset of its analysis of the statutory definition of debenture, the Full Court in *ABN AMRO* o
meaning and from earlier statutory definitions": at [642] (Jacobson, Gilmour and Gordon JJ) . The

Australian Securities and Investments Commission v M101 Nominees Pty Ltd (in liq) (No 8) [2025] FCA 741 (09

367. Even at this point of the analysis, it is clear that Mr Mawhinney's submission that the statutory de
cannot find a foothold in *ABN AMRO* . Rather, their Honours explicitly acknowledged that which t
law concept, at least in some respects.

Australian Securities and Investments Commission v M101 Nominees Pty Ltd (in liq) (No 8) [2025] FCA 741 (09

348. Mr Mawhinney also argued that, as the Investment Agreements did not call themselves "debentur
according to the statutory definition. This argument rested on Mr Mawhinney's reading of the thi
debentures.

Australian Securities and Investments Commission v M101 Nominees Pty Ltd (in liq) (No 8) [2025] FCA 741 (09

360. Before turning to *ABN AMRO* , the following points should be noted.

Australian Securities and Investments Commission v M101 Nominees Pty Ltd (in liq) (No 8) [2025] FCA 741 (09

404. There was an undertaking by IPO Capital to repay monies deposited by investors as a debt. Clause
under cl 9, "to repay the principal within 14 days of the Deposit Term expiring". That repayment r
performance of any separate index (cf the Rembrandt notes in *ABN AMRO*).

Australian Securities and Investments Commission v M101 Nominees Pty Ltd (in liq) (No 8) [2025] FCA 741 -
Australian Securities and Investments Commission v M101 Nominees Pty Ltd (in liq) (No 8) [2025] FCA 741 -
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Australian Securities and Investments Commission v M101 Nominees Pty Ltd (in liq) (No 8) [2025] FCA 741 -
R and N Hunter Pty Ltd ATF the Hunter Family Superannuation Fund v Count Financial Limited [2025] FCA

180. There is no generally agreed and unexceptionable definition of who is a fiduciary: ***Grimaldi v Char***
characteristics which define a fiduciary relationship cannot be exhaustively defined: ***ABN AMRO B***
and Gordon JJ) .

R and N Hunter Pty Ltd ATF the Hunter Family Superannuation Fund v Count Financial Limited [2025] FCA
R and N Hunter Pty Ltd ATF the Hunter Family Superannuation Fund v Count Financial Limited [2025] FCA
R and N Hunter Pty Ltd ATF the Hunter Family Superannuation Fund v Count Financial Limited [2025] FCA
Knowles v Interprac Financial Planning Pty Ltd [2025] QSC 78 -
Knowles v Interprac Financial Planning Pty Ltd [2025] QSC 78 -
Xie v Moshav Financial Wholesale Pty Ltd [2025] FCA 250 (26 March 2025) (Markovic J)

262. However, the proportionate liability regime in Pt 7.10 of Div 2A of Ch 7 of the Corporations Act (wl
12GP and s 12GR) , does not apply to other statutory claims including those under s 1041E of the Co

Xie v Moshav Financial Wholesale Pty Ltd [2025] FCA 250 -
Davis v Wilson [2025] FCA 108 (21 February 2025) (Shariff J)

1575. The Davis Applicants submitted that EY owed a duty of care to the Davis Applicants and to Davis
submitted that this proposition was supported by authority in *Esanda Finance* and *ABN AMRO* at [5

Davis v Wilson [2025] FCA 108 (21 February 2025) (Shariff J)

1369. True it is that, as EY submitted, in *Narain* the relevant conduct involved an ASX announcement by
against EY in this case. It is also true that *ABN AMRO* and *Bathurst Regional Council* related to the co
distinction.

Davis v Wilson [2025] FCA 108 (21 February 2025) (Shariff J)

1229. Jagot J's judgment in this respect was affirmed on appeal: *ABN AMRO Bank NV v Bathurst Regional*
also ***Chowder Bay*** *Pty Ltd v Paganin* [2018] FCAFC 25 at [31] (Besanko, Markovic and Lee JJ).

Davis v Wilson [2025] FCA 108 -
Davis v Wilson [2025] FCA 108 -
Davis v Wilson [2025] FCA 108 -
Davis v Wilson [2025] FCA 108 -
Davis v Wilson [2025] FCA 108 -
Davis v Wilson [2025] FCA 108 -
Xu v Salter Brothers Asset Management Pty Ltd [2025] FCA 89 (19 February 2025) (McElwaine J)

1085. Ms Bennett in her written opening submission put the case on the basis that the appropriate meas
time of the trial: *HTW Valuers (Central Qld) Pty Ltd v Astonland Pty Ltd* [2004] HCA 54; (2004) 217 CL
investor would have ascribed no value to them" on the basis that they were structured so as to "fur
any prospect of liquidity dependent upon an IPO for the Hotel Group and Property Opportunity F
that the units "continue to have no real value, due to the intrinsic nature of the units themselves: tl
realise value": *Bathurst* at [969] – [971] .

Xu v Salter Brothers Asset Management Pty Ltd [2025] FCA 89 -
Xu v Salter Brothers Asset Management Pty Ltd [2025] FCA 89 -
Chopsonion Pty Ltd (Controllers Appointed) v Watts Meat Machinery Pty Ltd (No 2) [2025] FCA 4 -
Wadren Pty Ltd v AIG Australia Pty Ltd [2024] VSC 807 -
J&J Richards Super Pty Ltd ATF the J&J Richards Superannuation Fund v Nielsen [2024] FCA 1472 -
J&J Richards Super Pty Ltd ATF the J&J Richards Superannuation Fund v Nielsen [2024] FCA 1472 -
Touch for Health Pty Ltd as Trustee for Knight Superannuation Fund v Property Mentors Australia Pty Ltd (N
Carter v Chubb Insurance Australia Ltd [2024] FCA 1312 (14 November 2024) (Halley J)

812. The meaning of "known to the insured" for the purposes of s 21(1) of the Insurance Contracts Act is
72] (Jacobson, Gilmour and Gordon JJ) ; *All Class Insurance Brokers Pty Ltd (in liq) v Chubb Insurance*
authoritative statements as to its construction can be distilled from those authorities:

(a) the term "known" in the phrase "every matter that is known to the insured" has its o
) 47 NSWLR 735 at 745 [37] (Davies AJA, Meagher JA agreeing);

(b) "knows" means considerably more than believes or suspects, or even strongly suspe
(2003) 214 CLR 514; [2003] HCA 25 at [30] (McHugh, Kirby and Callinan JJ); and

(c) constructive knowledge is insufficient; actual knowledge is required: *CIC Insurance L*
Byrne JJ agreeing).

In the matter of ıderful Pty Limited [2024] NSWSC 1414 -
Gerrard Toltz Pty Ltd v City Garden Australia Pty Ltd (in liq) (No 2) [2024] NSWCA 232 -
Chu v Lin, in the matter of Gold Stone Capital Pty Ltd (Trial Judgment) [2024] FCA 766 -
Absolute Tiling Solutions Pty Ltd v Certain Underwriters at Lloyds [2024] NSWSC 364 -
Tang v Yu [2024] FCA 297 -
Australian Securities and Investments Commission v Finder Wallet Pty Ltd [2024] FCA 228 (14 March 2024) (M

44. ASIC submits that, as a matter of substance, the undertaking includes repayment as a debt of the r account carried with it an obligation to repay on demand. ASIC contends that the obligation to re to be paid, relying on *Geeveekay Pty Ltd v Director of Consumer Affairs Victoria* (2008) 19 VR 512 at [72] practical and common sense fashion, relying on ***ABN Amro*** *Bank NV v Bathurst Regional Council* (20 ending with AUD that a customer chooses to invest in Finder Earn, with a notional conversion to T AUD, is not a loan to, or deposit with, Finder Wallet of money which Finder Wallet undertook to r

Troy Group Pty Ltd v Chittleborough [2023] WADC 151 (15 December 2023) (BLACK DCJ)

167. Events that do no more than 'expose what was inherent in the asset [purchased in reliance on the l 224 FCR 1 (Jacobson, Gilmour & Gordon JJ).

Troy Group Pty Ltd v Chittleborough [2023] WADC 151 -
Anderson v Canaccord Genuity Financial Ltd [2023] NSWCA 294 -
Anderson v Canaccord Genuity Financial Ltd [2023] NSWCA 294 -
City Garden Australia Pty Ltd (in administration) as trustee for the Ming Tian City Garden Unit Trust v Meng
Timeless Sunrise Pty Ltd v BigJ Enterprises Pty Ltd (No 10) [2023] VSC 524 (04 September 2023) (Delany J)

917. In *ABN AMRO Bank NV v Bathurst Regional Council* ,[135] Jacobson, Gilmour and Gordon JJ summa

1. The "critical feature is that the fiduciary undertakes or agrees to act for or on behalf

2. It is the element of undertaking (from the point of view of the fiduciary) or obligatio that the principal must act in the "interests of" or "for the benefit of" the beneficiary rather

3. Whether a fiduciary relationship exists in a particular case, and if so, the scope of th circumstances of the case.

4. The characteristics which define a fiduciary relationship cannot be exhaustively def dependent upon whether the principal and beneficiary fall into a particular status relations

5. Similarly, whether a fiduciary relationship has come into existence does not depend confidence. What matters is whether there is a relationship involving the requisite underta regard to the subjective expectations of the parties.

(citations omitted)

via

[136] Ibid 211 [1066] .

Timeless Sunrise Pty Ltd v BigJ Enterprises Pty Ltd (No 10) [2023] VSC 524 (04 September 2023) (Delany J)

TRUSTS – Fiduciary duty – Whether fiduciary relationship arose between two brothers – Accountant b matters – Fiduciary relationship established – History of joint business enterprises – Scope of fiduciary c relation to conduct establishing the unit trust – *Ying v Song* [2010] NSWSC 1500; *Hospital Products Ltd v Ui* *Ratnam* (1996) 23 ACSR 214; *Monster Tyson Pty Ltd v Harbinson* [2014] VSC 278; *Dupal v The Law Society of* 186 CLR 71; *ABN AMRO Bank NV v Bathurst Regional Council* (2014) 224 FCR 1 , applied.

Timeless Sunrise Pty Ltd v BigJ Enterprises Pty Ltd (No 10) [2023] VSC 524 -

Timeless Sunrise Pty Ltd v BigJ Enterprises Pty Ltd (No 10) [2023] VSC 524 -
Ramadan v ACN 098 408 176 Pty Ltd [2023] SASCA 91 (31 August 2023) (Livesey P; Doyle and Bleby JJ)

133. The first way in which liability for damages under s 12GF of the ASIC Act may be reduced is by a f
contributory negligence, that is a failure by the claimant "to take reasonable care". That issue was
limited to losses arising from a contravention of the prohibition on misleading and deceptive cond
reduce the payments made under the 2008 Loan which were incurred by reason of unconscionabl

via

[65] ASIC Act, s 12GF(1B)(a) ; *ABN AMRO Bank NV v Bathurst Regional Council* (2014) 309 ALR 445, [1576]-[15

Ramadan v ACN 098 408 176 Pty Ltd [2023] SASCA 91 -
Ramadan v ACN 098 408 176 Pty Ltd [2023] SASCA 91 -
Ramadan v ACN 098 408 176 Pty Ltd [2023] SASCA 91 -
H & Q Cafe Pty Ltd v Melbourne Cafe Pty Ltd [2023] VSCA 200 (25 August 2023) (Niall and Kennedy JJA; J For

117. In addition to damages for the true value of the business, a court may also award damages for cons
some supervening cause (such as ineptitude or third-party intervention)'. [92] Supervening events
on the misleading or deceptive conduct. [93] In other words, the event which causes the loss must
inaccuracies of the representations said to be misleading or deceptive. While damages will not ger
result of operating a loss-making business purchased in reliance on the misleading or deceptive cc
adduced to enable findings of fact to be made as to expenses incurred and revenue generated. [96]

The judge's rejection of the consequential loss claim

via

[93] *ABN Amro Bank NV v Bathurst Regional Council* (2014) 224 FCR 1, 190 [976] (Jacobson, Gilmour and Gordon JJ) . See also
CLR 640, 659 [40] .

Viterra Malt Pty Ltd v Cargill Australia Ltd [2023] VSCA 157 (23 June 2023) (Sifris, Walker and Whelan JJA)

606. Cargill submitted that hindsight evidence is not inherently unreliable. Rather, they submitted, suc
witnesses. [523] It was further submitted that the Viterra Parties had had ample opportunity to cros

via

[523] They referred to: *Lord Buddha Pty Ltd v Harpur* (2013) 41 VR 159, 206 (Vickery AJA, Weinberg JA
Financial Pty Ltd (2012) 38 VR 509, 542 (Nettle and Redlich JJA and Beach AJA); [2012] VSCA 262 ; *Hookey v*
Council (2014) 224 FCR 1, 331 [1733] (Jacobson, Gilmour and Gordon JJ); [2014] FCAFC 65 ; *Fabcot Pty Ltd v I*
1], Campbell JA agreeing at [2]); *Rosenberg* (2001) 205 CLR 434, 486–7 (Kirby J); [2001] HCA 18; *Chappel v H*

Viterra Malt Pty Ltd v Cargill Australia Ltd [2023] VSCA 157 -
Australian Securities and Investments Commission v Daly (Liability Hearing) [2023] FCA 290 -
Mallonland Pty Ltd v Advanta Seeds Pty Ltd [2023] QCA 24 -
Mallonland Pty Ltd v Advanta Seeds Pty Ltd [2023] QCA 24 -
Doherty v Bruce Ronald Sampey as administrator of the estate of Patricia Adele Addison (Aka Sampey) [2023
Doherty v Bruce Ronald Sampey as administrator of the estate of Patricia Adele Addison (Aka Sampey) [2023
Re DCA Enterprises Pty Ltd [2023] NSWSC 11 -
Re DCA Enterprises Pty Ltd [2023] NSWSC 11 -
Kumova v Davison (No 2) [2023] FCA 1 (09 January 2023) (Lee J)

152. It is worthwhile reiterating that each of ss 1041E and 1041H has a different focus. While the same fa
generally require further facts than a contravention of s 1041H (most notably, proof of deliberate, r
(2014) 224 FCR 1 (at 312–313 [1594] per Jacobson, Gilmour and Gordon JJ).

3Q Holdings Limited, in the matter of 3Q Holdings Limited (No 2) [2022] FCA 1359 (09 November 2022) (Chees

57. In *ABN AMRO* , the Full Court observed (at [684]):

> ...it is true that a debt is capable of including a debt that is repayable on a contingency. But the wo
> common sense fashion, consistent with its context and statutory purposes: *Hawkins v Bank of Chin*
> of a contingent debt is difficult, if not impossible. What is, or what is not, a contingent debt depen

The Full Court continued at [689]:

> As the High Court said in *Handevel* at 196, not every document creating or acknowledging a debt o
> make payment of a sum of money, dependent upon any form of contingency, constitutes a debent

3Q Holdings Limited, in the matter of 3Q Holdings Limited (No 2) [2022] FCA 1359 -
The Uniting Church in Australia Property Trust (Vic) v Ian Hartley Architects Pty Ltd [2022] VSC 233 (12 May

90. As stated in *ABN AMRO* , in a negligent advice context, known reliance (actual knowledge of relian
Church is that no material facts in support of the allegation of knowing reliance are pleaded.

The Uniting Church in Australia Property Trust (Vic) v Ian Hartley Architects Pty Ltd [2022] VSC 233 (12 May

89. The Full Court went on to discuss the relationship between reliance and vulnerability; rejecting th
duty of care to avoid pure economic loss’: [98]

> 596. S&P contended at trial and on appeal that LGFS was not vulnerable because it was
> vulnerable: J[2950]. S&P submitted that finding was in error. Again it is necessary to addres
>
> 597. Legally, S&P submitted that vulnerability was a “prerequisite” for the existenc
> the plaintiff’s “inability to protect itself from the consequences of a defendant’s want c
> reason of ignorance or social, political or economic constraints. In support of this cont
> could have taken steps to protect itself from the defendant’s conduct, and was not ind
> should step in and impose a duty on the defendant to protect the plaintiff from the ris
>
> 598. S&P’s submission fails legally and factually. S&P misstates the relevant legal
>
> > In relation to the giving of advice or information, questions of reliance and actual for
> > that which a reasonable person would have), of an individual, or an ascertainable cla
> > establishing a duty of care.
>
> In the field of negligent misstatement, vulnerability is the consequence of, not an additiona
> reliance by an ascertainable class of persons.

via

[98] Ibid , [596]-[598] .

The Uniting Church in Australia Property Trust (Vic) v Ian Hartley Architects Pty Ltd [2022] VSC 233 -
The Uniting Church in Australia Property Trust (Vic) v Ian Hartley Architects Pty Ltd [2022] VSC 233 -
The Uniting Church in Australia Property Trust (Vic) v Ian Hartley Architects Pty Ltd [2022] VSC 233 -
CBRE (V) Pty Ltd v City Pacific Ltd (in liq) [2022] NSWCA 54 (11 April 2022) (Bell CJ, Leeming and Brereton JJ

68. This accords with what was said in comparable circumstances by a Full Court of the Federal Cour
reproduced by the primary judge at [334] :

> "Next, as with the claim in tort, it is necessary to consider the separate communication of the disclaimers
> the rating could not be relied on. As the facts reveal (see [72]–[93] above), LGFS read the documents it ha
> ratings letters and the pre-sale report. A reasonable person would understand that the rating was an opi
> reasonable person would not understand the disclaimer to render the rating an exercise in futility, or an

Stav Investments Pty Ltd v Taylor [2022] NSWSC 208 (09 March 2022) (Ward CJ in Eq)

346. As to damages under s 236 of the *Federal ACL* (not here applicable as I have found that it does not a
remedies" (see *Ingot* at [173] and *Henville v Walker* at [130]). The plaintiffs say that (cf the defendant
the Full Court of the Federal Court in *ABN AMRO* at [969]). In *ABN AMRO* the Full Federal Court s

> ... It is unhelpful and dangerous because inevitably the wrong question is asked: namely, is the rule in *P*
> those facts establish a compensable loss and, if so, what was its true measure? Put at its highest, *Potts v M*
> ...
>
> [Emphasis in original]

Stav Investments Pty Ltd v Taylor [2022] NSWSC 208 -
Stav Investments Pty Ltd v Taylor [2022] NSWSC 208 -
Stav Investments Pty Ltd v Taylor [2022] NSWSC 208 -
Stav Investments Pty Ltd v Taylor [2022] NSWSC 208 -
Stav Investments Pty Ltd v Taylor [2022] NSWSC 208 -
Stav Investments Pty Ltd v Taylor [2022] NSWSC 208 -
Stav Investments Pty Ltd v Taylor [2022] NSWSC 208 -
Stav Investments Pty Ltd v Taylor [2022] NSWSC 208 -
Trimat Holdings Pty Ltd v Investment Club Pty Ltd [2022] WASCA 29 (04 March 2022) (Quinlan CJ, Beech JA,

ABN AMRO Bank NV v Bathurst Regional Council [2014] FCAFC 65 ; (2014) 309 ALR 445

Trimat Holdings Pty Ltd v Investment Club Pty Ltd [2022] WASCA 29 -
In the matter of Mediation & Online Dispute Resolution Operating Network Pty Ltd [2022] NSWSC 5 (23 Febr

99. As the plaintiffs submitted, the term "statement" embraces a "representation": *ABN AMRO Bank N*
representations constituted statements for the purpose of their claim pursuant to section 1041E(1) ;
representations of fact, and matters that were known to be false by Mr Polito. The representations
the provisions of the Original Constitution and found comfort in those provisions, given they were
plaintiffs *did* have regard to the intellectual property ownership issues, as they recognised that the
statements were false.

In the matter of Mediation & Online Dispute Resolution Operating Network Pty Ltd [2022] NSWSC 5 (23 Febr

113. Ipp JA referred at [178] (citing *Smith New Court Securities Ltd v Citibank NA* [1997] AC 254 at 266 (Lor
adequate compensation for the wrong done to the plaintiff, in particular where the fraud continue
transaction induced by fraud is to lock the plaintiff into continuing to hold the asset acquired. Fur
where the misrepresentations have and continue to have operative effect. The plaintiffs submitted
between what they paid for their investments and the value of the investments following the failu

In the matter of Mediation & Online Dispute Resolution Operating Network Pty Ltd [2022] NSWSC 5 -
In the matter of Mediation & Online Dispute Resolution Operating Network Pty Ltd [2022] NSWSC 5 -

In the matter of Mediation & Online Dispute Resolution Operating Network Pty Ltd [2022] NSWSC 5 -
In the matter of Mediation & Online Dispute Resolution Operating Network Pty Ltd [2022] NSWSC 5 -
Australian Securities and Investments Commission v PE Capital Funds Management Limited (administrators
[2022] FCA 76 (09 February 2022) (Cheeseman J)

126. Section 1041H of the Act and s 12DA of the ASIC Act contain no necessary element of knowledge o
Council [2014] FCAFC 65; (2014) 224 FCR 1 at 308 [1570] (Jacobson, Gilmour and Gordon JJ) citing Be
FCA 630; (2012) 205 FCR 120 at 129 [33] and 129 [36] (***ASIC v Stone***).

Cargill Australia Ltd v Viterra Malt Pty Ltd (No 28) [2022] VSC 13 (28 January 2022) (Elliott J)

3916. However, "the 'rule' is not universal or inflexible or rigid", and is only a "rule of practice". [3241] It
establish a compensable loss and if so, what was its true measure?" [3242]

X.73.1.2.1 Determining true or real value

via

[3242] *ABN AMRO Bank NV v Bathurst Regional Council* (2014) 224 FCR 1, 188 [969] (Jacobson, Gilmour a

Cargill Australia Ltd v Viterra Malt Pty Ltd (No 28) [2022] VSC 13 (28 January 2022) (Elliott J)

3922. If, subsequent to acquisition, the plaintiff resells the asset, this will not, in itself,[3259] prevent the p
ascertained is the date of the original acquisition. Therefore, the comparison is made between the
subsequent sale. However, a resale, like a later valuation, may be relevant to the extent it illumina
occurs shortly after the original purchase, and is not affected by extrinsic factors, the amount of th

via

[3260] See, for example, *ABN AMRO Bank NV v Bathurst Regional Council* (2014) 224 FCR 1, 188 [969] , 18

Cargill Australia Ltd v Viterra Malt Pty Ltd (No 28) [2022] VSC 13 -
Cargill Australia Ltd v Viterra Malt Pty Ltd (No 28) [2022] VSC 13 -
Cargill Australia Ltd v Viterra Malt Pty Ltd (No 28) [2022] VSC 13 -
Cargill Australia Ltd v Viterra Malt Pty Ltd (No 28) [2022] VSC 13 -
Cargill Australia Ltd v Viterra Malt Pty Ltd (No 28) [2022] VSC 13 -
Cargill Australia Ltd v Viterra Malt Pty Ltd (No 28) [2022] VSC 13 -
Adams v Price [2021] WADC 130 -
Adams v Price [2021] WADC 130 -
Troiano v Voci [2021] VSC 851 -
Krejci, in the matter of Union Standard International Group Pty Limited (in liq) [2021] FCA 1483 -
Application by New South Wales Minerals Council (No 4) [2021] ACompT 5 -
Re: Porter & Anor v Mulcahy & Co Accounting Services Pty Ltd & Ors [2021] VSC 572 -
Re: Porter & Anor v Mulcahy & Co Accounting Services Pty Ltd & Ors [2021] VSC 572 -
Re: Porter & Anor v Mulcahy & Co Accounting Services Pty Ltd & Ors [2021] VSC 572 -
Re: Porter & Anor v Mulcahy & Co Accounting Services Pty Ltd & Ors [2021] VSC 572 -
McEntee v SJ Berry Pty Ltd [2021] SADC 102 -
McEntee v SJ Berry Pty Ltd [2021] SADC 102 -
McEntee v SJ Berry Pty Ltd [2021] SADC 102 -
All Class Insurance Brokers Pty Ltd (in liq) v Chubb Insurance Australia Ltd (No 2) [2021] FCA 782 (09 July 202

152. All Class also relied upon s 21(2)(d) of the IC Act , which provided a specific exclusion from the dut
insured. It referred to the Full Court's reasons in *ABN Amro* 224 FCR at 328 [1709]–[1711] where the
clear that it did not require a proposal form to be filled in by the subsidiary but required only finan

... It would be surprising if, assuming the existence of the duty, AHAC could rely on non-complia
require a proposal form to be completed. That is, beyond what was contained in, relevantly, the f

All Class Insurance Brokers Pty Ltd (in liq) v Chubb Insurance Australia Ltd (No 2) [2021] FCA 782 -
All Class Insurance Brokers Pty Ltd (in liq) v Chubb Insurance Australia Ltd (No 2) [2021] FCA 782 -
All Class Insurance Brokers Pty Ltd (in liq) v Chubb Insurance Australia Ltd (No 2) [2021] FCA 782 -
All Class Insurance Brokers Pty Ltd (in liq) v Chubb Insurance Australia Ltd (No 2) [2021] FCA 782 -
Self Care Corporation Pty Ltd v Green Forest International Pty Ltd (No 3) [2021] FCCA 1277 -
Self Care Corporation Pty Ltd v Green Forest International Pty Ltd (No 3) [2021] FCCA 1277 -
Self Care Corporation Pty Ltd v Green Forest International Pty Ltd (No 2) [2021] FCCA 1000 (12 May 2021) (Bai

31. A second category of amendment sought arises by reason of the Applicants' calculation of damage claim for damages consequent upon the alleged misrepresentation that the Freezeframe products Australia. On Mr Ross' calculations that damages claim greatly exceeds the jurisdictional limits im *an Consumer Law* (**ACL**), Schedule 2 to the *Competition and Consumer Act 2010* (Cth) (**CCAct**), for m maintained, and the nonpecuniary relief sought pursuant to that claim is important to them, the A action at common law of negligent misrepresentation: as espoused by the Full Federal Court of Au -[598], [1106], and see the High Court in *Clayton v Bant* (2020) 385 ALR 41; [2020] HCA 44, [34], [76] .

City Pacific Ltd (in liq) v CBRE (V) Pty Ltd [2021] NSWSC 456 (30 April 2021) (Walton J)

332. In *ABN Amro Bank NV v Bathurst Regional Council* (2014) 309 ALR 445; [2014] FCAFC 65 ("*ABN Amro* which created the relevant product, were liable to certain Capital Councils for misleading conduct neither the ratings agency nor the Bank dealt with the Councils. It was sufficient to ground liability investors which included the Councils: *ABN Amro* at [754]-[773], [1304]-[1308] and [1361]-[1367] .

City Pacific Ltd (in liq) v CBRE (V) Pty Ltd [2021] NSWSC 456 (30 April 2021) (Walton J)

425. Consequently, the principles identified in *ABN Amro* apply. The June Valuation was requested and CLR 1 ("*Tepko*") and applied in *ABN Amro* in the passage cited are satisfied. At common law a duty *Corporation Ltd v Peat Marwick Hungerfords* (1997) 188 CLR 241 at 252, but ultimately I have approach

City Pacific Ltd (in liq) v CBRE (V) Pty Ltd [2021] NSWSC 456 (30 April 2021) (Walton J)

336. The disclaimer does not, again as a matter of general principle, 'effectively negate' the representat *Amro* at [717] . Similarly, even though the alleged victim of misleading conduct ordinarily must pro defeat a finding of reliance which is otherwise supported by the evidence (See the discussion in Co 446 [10.20]).

City Pacific Ltd (in liq) v CBRE (V) Pty Ltd [2021] NSWSC 456 -
City Pacific Ltd (in liq) v CBRE (V) Pty Ltd [2021] NSWSC 456 -
City Pacific Ltd (in liq) v CBRE (V) Pty Ltd [2021] NSWSC 456 -
City Pacific Ltd (in liq) v CBRE (V) Pty Ltd [2021] NSWSC 456 -
Mallonland Pty Ltd v Advanta Seeds Pty Ltd [2021] QSC 74 (09 April 2021) (Jackson J)

[203] Assumption of responsibility may be negated by an express disclaimer of responsibility, as has be

via

[112] [1964] AC 465, 492, 504 and 533 ; *Esanda Finance Corp Ltd v Peat Marwick Hungerfords* (1997) 188 CLR 24

Australian Securities and Investments Commission v TAL Life Limited (No 2) [2021] FCA 193 -
The Owners - Strata Plan No 87265 v Saaib; The Owners - Strata Plan No 87265 v Alexandrova [2021] NSWSC

488. The causation inquiry on the basis of third party reliance requires a determination of whether the
"brought about by virtue of" the conduct which is in contravention of s 18 of the ACL or s 42 of the
citing *Janssen-Cilag v Pfizer* at 530–531 .

Francis v Powercor Australia Ltd and Lenehan v Powercor Australia Ltd [2020] VSC 836 (11 December 2020) (I

103. The requirement has been variously described. [48] The Full Court of the Federal Court of Austr
of the insured not acting in good faith towards the insurer or a settlement in which the insurer's in

via

[49] (2014) 224 FCR 1 (Jacobson, Gilmour and Gordon JJ) .

Francis v Powercor Australia Ltd and Lenehan v Powercor Australia Ltd [2020] VSC 836 (11 December 2020) (I

104. The question of giving *bona fide* consideration to the interests of the insurer (or the insured, for tha
is whether the settlement is objectively reasonable, having regard to the material available to the i
settlement proceeds have been obtained in that way, there is a further requirement to distribute th

via

[51] *ABN Amro Bank v Bathurst Regional Council* (2014) 224 FCR 1, 347 [1844]-[1845] citing *Unity Insuran*

Francis v Powercor Australia Ltd and Lenehan v Powercor Australia Ltd [2020] VSC 836 -
Francis v Powercor Australia Ltd and Lenehan v Powercor Australia Ltd [2020] VSC 836 -
MOS Beverages Pty Ltd v Insurance Australia Ltd trading as CGU Insurance [2020] FCA 1716 -
Mistrina Pty Ltd v Australian Consulting Engineers Pty Ltd [2020] NSWCA 223 -
Wu v Ohapif Pty Ltd (ACN 167 080 542) as trustee for the Oliver Hume Australia Income Fund [2020] VSC 552

33. Both the Defendants and the Plaintiff relied on *ABN AMRO Bank v Bathurst Council* [33] for the pur
the Federal Court (Jacobson, Gilmore and Gordon JJ) states, with reference to s 1041H of the Corpo

> 729. It is necessary to begin by noting the text of the statute. What is to be located "in th
> was S&P's communication of the rating to ABN Amro and the authorisation given to ABN A
>
> 730. It is then necessary to turn to S&P's principal submission – that s 1041H of the Corp
>
> …
>
> 733. There is no statutory warrant for interpreting the term "in this jurisdiction" in
> occurred in Australia. … [34]

via

[34] Ibid , 137 , [729] , [730] and [733] .

Wu v Ohapif Pty Ltd (ACN 167 080 542) as trustee for the Oliver Hume Australia Income Fund [2020] VSC 552
Wu v Ohapif Pty Ltd (ACN 167 080 542) as trustee for the Oliver Hume Australia Income Fund [2020] VSC 552

HAP2 Pty Ltd v Bankier [2020] QCA 152 (21 July 2020) (Sofronoff P and Morrison and Philippides JJA)

63. As the appellant acknowledged at trial, it has also been established that in the case of a financial ad or of which the adviser should have been aware, [20] but of which the client is unaware. A materia significance if warned of it.[21]

via

[20] *NMFM Property Pty Ltd v Citibank Ltd* (2000) 107 FCR 270 at [427]-[428] ; *ABN AMRO Bank NV v B*

HAP2 Pty Ltd v Bankier [2020] QCA 152 -
Lloyd v Belconnen Lakeview Pty Ltd [2019] FCA 2177 (20 December 2019) (Lee J)

335. As the Full Court noted in *ABN AMRO Bank NV v Bathurst Regional Council* [2014] FCAFC 65; (2014) because it obscures the fundamental inquiry: what are the facts, do those facts establish a compens

TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Limited [2019] FCA 1747 -
TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Limited [2019] FCA 1747 -
TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Limited [2019] FCA 1747 -
TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Limited [2019] FCA 1747 -
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TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Limited [2019] FCA 1747 -
TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Limited [2019] FCA 1747 -
Masters v Lombe (Liquidator); In the Matter of Babcock & Brown Limited (In Liq) [2019] FCA 1720 (18 October

377. Before addressing the liquidator's argument in submissions that *Re HIH* does not apply to relief so continuous disclosure, I will consider Federal Court consideration of market-based causation follo often arisen before the Federal Court in the context of securities class actions. Recently, Lee J sum at 15–16 [31] :

> ... *Secondly*, it involves risk as at least one issue, commonly described as 'market based causation', in obiter, in *Grant-Taylor v Babcock and Brown Ltd (in liq)* [2015] FCA 149; (2015) 322 ALR 723 at 765-7 *v Cao* [2015] FCAFC 94; (2015) 236 FCR 322 at 333 [68] per Gilmour and Foster JJ; the decision of Bre recent observations of two Full Courts as to indirect causation in *ABN AMRO Bank NV v Bathurst R* Gordon JJ and *Chowder Bay Pty Ltd v Paganin* [2018] FCAFC 25 at [61] per Besanko, Markovic and I

Masters v Lombe (Liquidator); In the Matter of Babcock & Brown Limited (In Liq) [2019] FCA 1720 (18 October

365. In *Grant-Taylor First Instance*, Perram J considered whether BBL failed to disclose important inforr Perram found that the plaintiffs failed on the question of liability for breach of the Act and, therefo with those issues "relatively briefly", concluding that, had it been necessary to reach a view on the reasons outlined at 765–766 [219], being:

> (i) the relevant statutory questions appear in ss 1317HA (the damage resulted from the c
>
> (ii) provisions of this kind import a notion of causation;
>
> (iii) while reliance is a sufficient condition for establishing causation it is not a necessar misleading conduct are one obvious example of this: *Janssen-Cilag Pty Ltd v Pfizer Pty Ltd* (19
>
> (iv) it is relevant to take into account the underlying context of the alleged infringemen to affect price (and where the listing rules also require disclosure). The provision assumes t

(v) a plaintiff may not recover where it knows of the misleading nature of the alleged c
NSWLR 653; 252 ALR 659; 68 ACSR 595; [2008] NSWCA 206 at [19]–[22] and [612]–[619] (CA)
observations by the Court of Appeal do not preclude a case brought by a council against a r
of a council association about particular financial instruments and the council had then rel
maintained: *ABN AMRO Bank AV v Bathurst Regional Council* (2014) 224 FCR 1; 309 ALR 445; 9
NSWSC 1763 at [264]–[265] per McDougall J; *McBride v Christie's Australia Pty Ltd* [2014] NSV
at [87]–[92] per Farrell J.

(vi) *ABN AMRO* establishes that, at least in principle, where A misleads B and B in cons

(vii) the facts on this case are different to those in ABN AMRO to this extent: here it is al
loss to C. This is not the same factual situation as arose in *ABN AMRO* but I do not think it r

(viii) while I accept that generally a plaintiff must show in a misleading conduct case tha
Investments Pty Ltd v Collins Marrickville Pty Ltd (No 1) (1988) 39 FCR 546 at 559; 79 ALR 83 at 9
(CA)) it is artificial to speak of reliance in non-disclosure cases such as the present: *Campbel*
143] .

Masters v Lombe (Liquidator); In the Matter of Babcock & Brown Limited (In Liq) [2019] FCA 1720 (18 Octobe

365. In *Grant-Taylor First Instance*, Perram J considered whether BBL failed to disclose important infor
Perram found that the plaintiffs failed on the question of liability for breach of the Act and, theref
with those issues "relatively briefly", concluding that, had it been necessary to reach a view on the
reasons outlined at 765–766 [219], being:

(i) the relevant statutory questions appear in ss 1317HA (the damage resulted from the c

(ii) provisions of this kind import a notion of causation;

(iii) while reliance is a sufficient condition for establishing causation it is not a necessar
misleading conduct are one obvious example of this: *Janssen-Cilag Pty Ltd v Pfizer Pty Ltd* (19

(iv) it is relevant to take into account the underlying context of the alleged infringemen
to affect price (and where the listing rules also require disclosure). The provision assumes t

(v) a plaintiff may not recover where it knows of the misleading nature of the alleged c
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Masters v Lombe (Liquidator); In the Matter of Babcock & Brown Limited (In Liq) [2019] FCA 1720 -
Masters v Lombe (Liquidator); In the Matter of Babcock & Brown Limited (In Liq) [2019] FCA 1720 -
Masters v Lombe (Liquidator); In the Matter of Babcock & Brown Limited (In Liq) [2019] FCA 1720 -
Wyzenbeek v Australasian Marine Imports Pty Ltd (in Liq) [2019] FCAFC 167 -
Eckford v Six Mile Creek Pty Ltd (No 2) [2019] FCA 1307 (20 August 2019) (Rares J)

333. Mr Eckford claimed that he and Mrs Eckford would never have entered into the contract to purch
would have been the case, but argued that even if this were so, Mr and Mrs Eckford would have ke
similar expenditures in acquiring such a property and built a dwelling of similar standard. They c
compensation or damages, for the benefits he and his late wife had had from living at lot 10 since t
living on lot 10 since the construction of the dwelling on it was completed and therefore, an allowa
had not been able to identify any precedent for such an allowance, but noted that the Full Court h
approach to an award of damages had to be flexible and best adapted to give the injured claimant
injustice.

Luo v Windy Hills Australian Game Meats Pty Ltd (No 3) [2019] NSWSC 862 -
Roo Roofing Pty Ltd v Commonwealth [2019] VSC 331 (31 May 2019) (John Dixon J)

654. By contrast with liability in negligence, 'the concept of indeterminacy has no, or no separate, role i
additional criterion of, knowledge (actual or which a reasonable person would have) of reasonable

via

[159] Ibid 116 [598] .

Roo Roofing Pty Ltd v Commonwealth [2019] VSC 331 -
Roo Roofing Pty Ltd v Commonwealth [2019] VSC 331 -
DIF III - Global Co-Investment Fund LP v Babcock & Brown International Pty Limited [2019] NSWSC 527 (13 I

268. However, as the defendants recognise, the rule in *Potts v Miller* is not an inflexible one. In assessing
which shed light on the true value as at that date: *HTW Valuers (Central Qld) Pty Ltd v Astonland Pty*
appropriate to assess damages at the date of trial, such as where the asset is not readily saleable: se
beek v Australasian Marine Imports Pty Ltd (No 2) [2018] FCA 1517 at [224] ff per Derrington J.

Demetrios v Lehmann [2019] VSC 301 (10 May 2019)

55. In *ABN Amro* , the relevant question was the same as that obtaining in *Selig* : whether the proportio
relevant respondents or whether it was limited to claims based on contravention of s 1041H . The F
the states and territories' and referred specifically to Part 4 of the *Civil Liability Act* and Part IVAA
Federal Court then stated that s 1041L(1) contains significant differences to the two state Acts and g
must be considered bearing these differences in mind. [34] Further, when discussing *Wealthsure* a
stated: [35]

> The cases involving State legislation such as *Reinhold* and *Godfrey Spowers* take a different approac
> contextual differences in the apportionment provisions of that legislation from that found in the C

via

[34] *ABN Amro* (n 31) [1552].

Demetrios v Lehmann [2019] VSC 301 (10 May 2019)

PRACTICE AND PROCEDURE – Application to dismiss or strike out defendant's proportionate liability
action for the claim to be apportionable – Unsettled point of law – Inappropriate to summarily dismiss o
Act 1958 (Vic) , Part IVAA – *Corporations Act 2001* (Cth), s 1041L – *Selig v Wealthsure Pty Ltd* (2015) 255 CLR 6
Group Pty Ltd (No 2) [2013] NSWCA 58 – *Reinhold v New South Wales Lotteries Corp (No 2)* (2008) 82 NSWL

Demetrios v Lehmann [2019] VSC 301 (10 May 2019)

62. In circumstances where the High Court in *Selig* did not refer to *Reinhold* , *Dartberg* or any other like
and in light of discussions in appellate cases such as *ABN Amro* , I do not consider the question pos
that *Selig* does not foreclose an argument that the Factual Construction of cases where Part IVAA

Demetrios v Lehmann [2019] VSC 301 (10 May 2019)

61. In other words, his Honour favoured the Legal Construction. Mossop J did not refer to or rely on S

Demetrios v Lehmann [2019] VSC 301 (10 May 2019)

56. The Full Federal Court in *ABN Amro* went on to say that (citations omitted): [36]

Nothing stated by Middleton J in *Dartberg* is contrary to the views we have expressed as to th
7] Indeed, when referring to these in passing at [18]-[19] his Honour appears to have accepted
the words 'claim for damages made' found in s 1041L(1) . This is to be distinguished from his
observed by Middleton J at [29]-[31]:

> [29] As the respondents observed, in drafting the provisions of Pt VIAA of the *Wrongs Act* , t
> action for damages arising from a failure to take reasonable care. The provisions do not rec
> requires that the claim arise from a failure to take reasonable care. The expressions "arising
>
> [30] In my view, Pt IVAA could apply in the circumstances of this proceeding according to i
> necessary elements any allegation of failing to take reasonable care, an additional enquiry i
> determine the application of Pt IVAA. Even though the claims in this proceeding themselv
> strict sense, a failure to take reasonable care may form part of the allegations or the evidenc
> evidence, it may be found that Pt IVAA applies.
>
> [31] In these circumstances, where a respondent desires to rely upon Pt IVAA of the *Wrongs*
> failure to take reasonable care. In a proceeding where the applicant does not rely upon any
> particularly important for the proper case management of the proceedings. It would be des
> which it relies in support of the allocation of responsibility it contends should be ordered.
> IVAA of the *Wrongs Act* , then the respondent has the onus of pleading and proving the req
> as a matter of fact, whether the relevant claim brought by the applicant is a claim arising fr

These observations concerning the *Wrongs Act* have no application to the relevant provisions of th

via

[36] *ABN Amro* (n 31) [1584]-[1585].

Demetrios v Lehmann [2019] VSC 301 -
Demetrios v Lehmann [2019] VSC 301 -
Demetrios v Lehmann [2019] VSC 301 -
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Demetrios v Lehmann [2019] VSC 301 -
Demetrios v Lehmann [2019] VSC 301 -
Bankier v HAP2 Pty Ltd [2019] QSC 101 -
Bankier v HAP2 Pty Ltd [2019] QSC 101 -
Bankier v HAP2 Pty Ltd [2019] QSC 101 -
Babscay Pty Ltd v Pitcher Partners (a Firm) [2019] FCA 480 (15 March 2019) (Middleton J)

74. The parties referred me to a number of authorities relevant to causation. These included *Digi-Tec*
224 FCR 1 ('***ABN AMRO Bank***'). Neither authority is directly on point having regard to their facts.
significantly the application of the law to the facts is not appropriate. Even on the approach unde
to whether their representations were material to the decisions made by the Applicants: see, e.g. th

Babscay Pty Ltd v Pitcher Partners (a Firm) [2019] FCA 480 -
Babscay Pty Ltd v Pitcher Partners (a Firm) [2019] FCA 480 -
Williams v Vpac (Vic) Pty Ltd (Civil Claims) [2019] VCAT 332 -
Flash Lighting Company Ltd v Australia Kunqian International Energy Co Pty Ltd (No 3) [2018] VSC 711 -
Wyzenbeek v Australasian Marine Imports Pty Ltd (No 2) [2018] FCA 1517 (10 October 2018) (Derrington J)

221. The objective of the rule in *Potts v Miller*, as is the case with the *Astonland* measure, is to calculate
the present, the adoption of the appropriate measure is determined, to some extent, by the nature
conduct in question is referrable to some enduring characteristic of the asset acquired which has t
misleading nature, the rule in *Potts v Miller* may well be inapposite. A comparison between the sal
caused by the conduct. In *ABN AMRO Bank v Bathurst Regional Council* (2014) 224 FCR 1 at 186 [963]
causes of the diminution in the value of the assets acquired in that case, which were investment no
said at 189 [971]:

> Here, the questions posed by *Potts v Miller* are inapposite because, as we have explained when ass
> inability of the notes, inconsistent with a AAA rating, to survive relatively rapid credit spread wid
> characteristics of the notes themselves (and the characteristic of the notes to which the negligent a
> event: at J[3417], [3427] and [3455]– [3456]. The primary judge was correct to conclude that in those
> amount it received on the notes being sold to LGSS: at J[3462].

Wyzenbeek v Australasian Marine Imports Pty Ltd (No 2) [2018] FCA 1517 (10 October 2018) (Derrington J)

227. The authorities demonstrate that in many cases the loss or damage suffered on the acquisition of p
paid and the true value of the asset at the time of purchase: *ABN AMRO*. That is particularly so wh
claimant is induced to acquire an investment which will mature in a number of years and the indu
loss at the expiry of the investment is necessarily a more apposite consideration as any decline in t
representation. Similarly, where the misleading conduct continues to have an operative effect or t
limit the assessment of damages to the "true value" at the date of sale: *ABN AMRO* at 188-9 [971]–[9

Wyzenbeek v Australasian Marine Imports Pty Ltd (No 2) [2018] FCA 1517 -
Wyzenbeek v Australasian Marine Imports Pty Ltd (No 2) [2018] FCA 1517 -
Finadri v Westpac Life Insurance Services Ltd [2018] VCC 1636 -
Investa Properties Pty Ltd v Nankervis (No 9) [2018] FCA 793 -
Investa Properties Pty Ltd v Nankervis (No 9) [2018] FCA 793 -
Perera v GetSwift Ltd [2018] FCA 732 -
Minerva (Aust) Pty Ltd v Suburban Land Agency [2018] ACTSC 103 -
Modakboard Australia Pty Ltd v Matthew Howard Brady [2018] NSWSC 399 -
Downer EDI Rail PL v John Holland PL [2018] NSWSC 326 -
Downer EDI Rail PL v John Holland PL [2018] NSWSC 326 -
Vanguard Financial Planners Pty Ltd v Ale [2018] NSWSC 314 -
Allianz Australia Ltd v Taylor [2018] VSC 78 (26 February 2018) (Mukhtar AsJ)

40. The Full Court of the Federal Court in *ABN Amro Bank NV v Bathurst Regional Council*, [15] adopted
person's claim' in s 48(2)(a) were not referable to the precontractual obligations of the insured und
referred to in s 48(2) concerned obligations after the contract was made and arising out of the mak

via

[15] [2014] 224 FCR 1.

Lockyer v Bermingham [No 3] [2018] WASC 61 (26 February 2018) (Tottle J)

328. For present purposes it is sufficient to refer to the summary of the applicable principles referred t

[The] applicable principles *may* be summarised as follows. First, for there to be a duty to exercise reasonable

(1) The speaker must realise, or the circumstances must be such that the speaker ought to have re connexion with some matter of business or serious consequence; and

(2) The circumstances must be such that it is reasonable in all the circumstances for the recipient

In respect of the second limb, the nature of the subject matter, the occasion of the interchange, and the identi exercise judgment will all be *included* in the factors which will determine the reasonableness of the acceptanc is not exhaustive.

Second, proof of the criteria at [573] and [574] above establishes an assumption of responsibility or known reli

Ms Richardson and Bepad owed Mr Lockyer a duty of care

Lockyer v Bermingham [No 3] [2018] WASC 61 (26 February 2018) (Tottle J)

ABN Amro Bank NV v Bathurst Regional Council [2014] FCAFC 65 ; (2014) 224 FCR 1

Allianz Australia Ltd v Taylor [2018] VSC 78 (26 February 2018) (Mukhtar AsJ)

40. The Full Court of the Federal Court in *ABN Amro Bank NV v Bathurst Regional Council* , [15] adopted person's claim' in s 48(2)(a) were not referable to the precontractual obligations of the insured und referred to in s 48(2) concerned obligations after the contract was made and arising out of the mak

Lockyer v Bermingham [No 3] [2018] WASC 61 -
Semantic Software Asia Pacific Ltd v Ebbsfleet Pty Ltd [2018] NSWCA 12 (14 February 2018) (Macfarlan and W

136. This evidence indicates that Mr Vinson relied upon the representations contained in the Investor representations. The fact that Mrs Vinson relied upon her husband's recommendation does not m misleading and deceptive conduct (*ABN Amro Bank NV & Others v Bathurst Regional Council & Ors* (

Equititrust Limited (In Liq) (Receiver Appointed) (Receivers and Managers Appointed) (Responsible Entity) v
11 -
Equititrust Limited (In Liq) (Receiver Appointed) (Receivers and Managers Appointed) (Responsible Entity) v
11 -
Equititrust Limited (In Liq) (Receiver Appointed) (Receivers and Managers Appointed) (Responsible Entity) v
11 -
Tarangau Game Fishing Charters Pty Ltd v Eagle Yachts Pty Ltd [2017] QSC 306 (14 December 2017) (Atkinson

395. In *ABN AMRO Bank NV (ARBN 84 079 478 612) v Bathurst Regional Council* [259] the Federal Court of

"[1508] The question of apportionment of loss is a matter of judgment and discretio

[1509] In *Podrebersek v Australian Iron and Steel Pty Ltd* (1985) 59 ALR 529 at 532; 59 AL

A finding on a question of apportionment is a finding upon a 'question, not of p relative emphasis, and of weighing different considerations. It involves an indi by different minds': *British Fame (Owners) v Macgregor (Owners)* [1943] AC 197 at reviewed.

[1510] Here, the primary judge assessed the correct questions, principally:

(1) the relative culpability of the conduct of each of LGFS, S&P and A seriousness relative to that of the others; and

(2) the relative importance of the conduct of each of those parties in c

Tarangau Game Fishing Charters Pty Ltd v Eagle Yachts Pty Ltd [2017] QSC 306 -
Innes v AAL Aviation Limited [2017] FCAFC 202 -
Clurname Pty Limited v McGraw-Hill Financial, Inc [2017] FCA 1319 (10 November 2017) (Wigney J)

159. The fifth and sixth contentions can also be dealt with shortly. As for the fifth contention, a fair rea fraudulent claims. It pleads those claims separately and in the alternative. As for the sixth conten representations by the Commonwealth Bank. That contention is rejected for the reasons already g the SCDOs. Standard & Poor's submissions concerning inducement appeared to be based on the s case in relation to inducement are a matter for trial. It should also be noted that similar argumer circumstances in *ABN AMRO* at [744] .

Clurname Pty Limited v McGraw-Hill Financial, Inc [2017] FCA 1319 -
Clurname Pty Limited v McGraw-Hill Financial, Inc [2017] FCA 1319 -
Smith v Australian Executor Trustees Ltd [2017] NSWSC 1406 -
Mobis Parts Australia Pty Ltd v XL Insurance Company SE (No 7) [2017] NSWSC 1321 -
Mobis Parts Australia Pty Ltd v XL Insurance Company SE (No 7) [2017] NSWSC 1321 -
Oliver Hume South East Queensland Pty Ltd v Investa Residential Group Pty Ltd [2017] FCAFC 141 (01 Septen

209. In these reasons, I have adopted the use of the following terms in relation to participants, articles a

- Investa Properties Pty Ltd ("Investa Properties");
- Investa Residential Pty Ltd ("Investa Residential");
- Investa Properties and Investa Residential (the "appellants");
- Investa Property Group Holdings Pty Ltd ("Holdings");
- Investa Residential's former corporate name, Clarendon Residential Group Pty Ltd ("
- Brittains Road Pty Ltd, the prior purchaser of Lot 170 ("Brittains Road");
- The group of companies owned by Holdings (the "Investa Property Group");
- Mr Ashley Colin Nankervis ("Mr Nankervis");
- Mr Adam Kimberley Barclay ("Mr Barclay");
- Oliver Hume South East Queensland Pty Ltd ("Oliver Hume");
- Two Eight Two Nine Pty Ltd ("TETN");
- Mr David Tonuri ("Mr Tonuri");
- Queensland Property Centre Pty Ltd ("QPC");
- Spencer Projects Pty Ltd ("Spencer Projects");
- Mr Barclay's wife ("Ms Barclay");

- Ms Barclay's daughter, Jaide Spencer Crosbie ("Ms Crosbie");
- The development site at Cardena Drive, Augustine Heights, Ipswich, Queensland (th
- *Fiduciary Obligations*, the Hon Dr P.D. Finn ("Dr Finn"), Law Book Company Limited,
- *The Fiduciary Principle,* the Hon Dr P.D. Finn, an article contained within *Equity, Fidu* *Principle* 1989");
- *Contract and The Fiduciary Principle*, the Hon Dr P.D. Finn, UNSW Law Journal, 1989,
- *Fiduciaries: Who Are They?* the late the Hon Justice B.H. McPherson CBE ("McPherso Commonwealth Law Conference ("CLC Papers"), Vol 5, complete presentation at 5.4 of the C
- *When Do Fiduciary Duties Arise?* the Hon Justice Edelman, (2010) 126 LQR 302 (the *"20*
- *Bristol and West Building Society v Mothew* [1998] Ch. 1 (Court of Appeal); (*"Bristol v Mo*
- *Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41 ("*Hospital Pr*
- *John Alexander's Clubs v White City* (2010) 241 CLR 1 ("*John Alexander's Clubs*");
- *Electricity Generation Corporation (t/as Verve Energy) v Woodside Energy Ltd* (2014) 306 A
- *Codelfa Construction Pty Ltd v State Rail Authority (NSW)* (1982) 149 CLR 337 ("*Codelfa*");
- *Manildra Laboratories Pty Limited v Campbell* [2009] NSWSC 987 ("*Manildra Laboratori*
- *Tate v Williamson* (1866) 2 Ch. App. 55 (L.C.);
- *ABN AMRO Bank NV v Bathurst Regional Council* (2014) 309 ALR 445 (" *ABN AMRO Ban*
- *News Limited v Australian Rugby Football League Limited* (1996) 64 FCR 410 ("*News Limi*
- *Australian Securities Commission v AS Nominees Limited* (1995) 62 FCR 504 ("*ASC v AS N*
- *Grimaldi v Chameleon Mining NL (No 2)* (2012) 200 FCR 296 ("*Grimaldi*")
- *Investa Properties Pty Ltd v Nankervis (No 7)* [2015] FCA 1004 (the "primary judgment");
- *Property Agents and Motor Dealers Act 2000* (Qld) (the " PAMD Act ").

Oliver Hume South East Queensland Pty Ltd v Investa Residential Group Pty Ltd [2017] FCAFC 141 -
Oliver Hume South East Queensland Pty Ltd v Investa Residential Group Pty Ltd [2017] FCAFC 141 -
Addenbrooke Pty Ltd v Duncan (No 2) [2017] FCAFC 76 (16 May 2017) (Dowsett, Gilmour and White JJ)

274. I should say that for present purposes, I find no assistance in the decision of this Court in *ABN AM*

Addenbrooke Pty Ltd v Duncan (No 2) [2017] FCAFC 76 (16 May 2017) (Dowsett, Gilmour and White JJ)

664. Secondly, s 12GM of the ASIC Act (like its counterpart, s 237 of the Australian Consumer Law (*Con* concerning causation of loss and recovery of damages. It vests the Court with flexible powers to cr

> 963. A number of matters are worth stating. ... subject to the loss being proved, the app amount which will most fairly compensate for the wrong suffered" provided that it works n *TW Valuers* at [65] . ... causation and damages are closely linked: *Ingot Capital Investments* at

misrepresentations, there will be many cases where the losses are *not* represented by the di
t [35]-[40] ; *Ingot Capital Investments* at [176]-[180] and [190] ; and *Smith New Court Securities L*
might arise are not closed.

Addenbrooke Pty Ltd v Duncan (No 2) [2017] FCAFC 76 -
Addenbrooke Pty Ltd v Duncan (No 2) [2017] FCAFC 76 -
Addenbrooke Pty Ltd v Duncan (No 2) [2017] FCAFC 76 -
Muswellbrook Shire Council v The Royal Bank of Scotland NV [2017] FCA 414 -
Chowder Bay Pty Ltd v Paganin [2017] FCA 332 -
Chowder Bay Pty Ltd v Paganin [2017] FCA 332 -
Ceccon Transport Pty Ltd v Tomazos Group Pty Ltd [2017] NTSC 25 -
Ceccon Transport Pty Ltd v Tomazos Group Pty Ltd [2017] NTSC 25 -
Ceccon Transport Pty Ltd v Tomazos Group Pty Ltd [2017] NTSC 25 -
Ceccon Transport Pty Ltd v Tomazos Group Pty Ltd [2017] NTSC 25 -
RCR Energy Pty Ltd v WTE Co-Generation Pty Ltd [2017] VSCA 50 -
Gloucester Shire Council v Fitch Ratings, Inc (No 2) [2017] FCA 248 -
Riva NSW Pty Limited v Official Trustee in Bankruptcy [2017] FCA 188 -
McGraw-Hill Financial, Inc (now known as S&P Global, Inc) v Mitsub Pty Ltd (Trustee) [2017] FCAFC 11 (02 F

35. On 6 June 2014, the Full Court delivered judgment in the appeal from the judgment of Jagot J (*ABl*

McGraw-Hill Financial, Inc (now known as S&P Global, Inc) v Mitsub Pty Ltd (Trustee) [2017] FCAFC 11 -
McGraw-Hill Financial, Inc (now known as S&P Global, Inc) v Mitsub Pty Ltd (Trustee) [2017] FCAFC 11 -
McGraw-Hill Financial, Inc (now known as S&P Global, Inc) v Mitsub Pty Ltd (Trustee) [2017] FCAFC 11 -
McGraw-Hill Financial, Inc (now known as S&P Global, Inc) v Mitsub Pty Ltd (Trustee) [2017] FCAFC 11 -
John Montclare v Metlife Insurance Ltd (formerly Citicorp Life Insurance Ltd) (ACN 004 274 882) [2016] VSCA

140. As the judge recorded, the amendments came about because of a review of the ICA which was pul
make clear that a third party beneficiary could sue an insurer without the intervention of the Polic
to rely on the conduct of the insured, where relevant, in defence to a claim from a third party bene
following:

> 10.1 Third party beneficiaries should have access to the following provisions of the IC A
>
> - the same rights and obligations as an insured for the purposes of subrogation
> - the duty of utmost good faith (but not pre-contractually); and
> - where the IC Act allows the insured to give notice, for example, pursuant to s
>
> ...
>
> 10.2 Subsection 48(3) of the IC Act should be clarified so that it is clear that a third party
> able to raise the conduct of the insured (whether pre or post contract) in defence to a claim
>
> ...
>
> 10.3 Section 48A of the IC Act should be amended so that:
>
> - it is clear that a third party can bring an action against an insurer without the
> - the life insured can be nominated as a third party beneficiary; and
> - a third party beneficiary can provide a valid discharge to the insurer. [63]

via

[62] Alan Cameron and Nancy Milne, 'Review of the *Insurance Contracts Act 1984* (Cth) — Final Repo
the judge also observed, the Full Federal Court in *ABN AMRO Bank NV v Bathurst Regional Council* (2014)
party to the insurance contract was not under the obligation of disclosure under s 21 or a duty not to mak
because of a fraudulent misrepresentation the third party beneficiary had made: *ABN AMRO* (2014) 224 F
'Section 48(2) confines the person's obligations to those which are "in relation to the person's claim". We
[1641]). The Court agreed with what Clarke JA (with whom Meagher JA agreed) had said in *C E Heath Cas*
contractual disclosure under s 21 is imposed only upon a party to the contract.

John Montclare v Metlife Insurance Ltd (formerly Citicorp Life Insurance Ltd) (ACN 004 274 882) [2016] VSCA
John Montclare v Metlife Insurance Ltd (formerly Citicorp Life Insurance Ltd) (ACN 004 274 882) [2016] VSCA
William Derek McNee v P-Value Pty Ltd [2016] VSCA 223 -
Choo v Zhang [2016] NSWCA 193 -
Choo v Zhang [2016] NSWCA 193 -
Choo v Zhang [2016] NSWCA 193 -
Muswellbrook Shire Council v Royal Bank of Scotland NV [2016] FCA 819 -
Mitsub Pty Limited v McGraw-Hill Financial Inc [2016] FCA 559 -
Mitsub Pty Limited v McGraw-Hill Financial Inc [2016] FCA 559 -
Mitsub Pty Limited v McGraw-Hill Financial Inc [2016] FCA 559 -
HFPS Pty Limited (Trustee) v Tamaya Resources Limited (In Liq) (No 2) [2016] FCA 446 -
HFPS Pty Limited (Trustee) v Tamaya Resources Limited (In Liq) (No 2) [2016] FCA 446 -
In the matter of HIH Insurance Limited (In Liquidation) (ACN 008 636 575) and others; Smith v Anthony Greg
Anthony... [2016] NSWSC 482 (20 April 2016) (Brereton J)

62. (2014) 309 ALR 445 at 726-727 [1375]-[1376] , referring to Janssen-Cilag Pty Ltd v Pfizer Pty Ltd (1992) 37 F
NSWCA 455 .

In the matter of HIH Insurance Limited (In Liquidation) (ACN 008 636 575) and others; Smith v Anthony Greg
Anthony... [2016] NSWSC 482 (20 April 2016) (Brereton J)

67. In *Grant-Taylor v Babcock and Brown Ltd (in liq)* , [64] Perram J accepted, *obiter,* that a party who acq
failure to disclose material required to be disclosed, so long as they were not themselves aware of t
Tech and *Ingot* , a plaintiff may not recover where it knows of the misleading nature of the alleged
where A misled B, and B in consequence misled C (as *ABN AMRO* established), and a case in which
was not relevantly different.

In the matter of HIH Insurance Limited (In Liquidation) (ACN 008 636 575) and others; Smith v Anthony Greg
Anthony... [2016] NSWSC 482 (20 April 2016) (Brereton J)

61. (2014) 309 ALR 445 at 726-727 [1374]-[1377] .

In the matter of HIH Insurance Limited (In Liquidation) (ACN 008 636 575) and others; Smith v Anthony Greg
Anthony... [2016] NSWSC 482 -
In the matter of HIH Insurance Limited (In Liquidation) (ACN 008 636 575) and others; Smith v Anthony Greg
Anthony... [2016] NSWSC 482 -
In the matter of HIH Insurance Limited (In Liquidation) (ACN 008 636 575) and others; Smith v Anthony Greg
Anthony... [2016] NSWSC 482 -
City of Swan v McGraw-Hill Companies, Inc [2016] FCA 343 -
QNI Resources Pty Ltd v Sino Iron Pty Ltd [2016] QSC 62 (23 March 2016) (Jackson J)

82. The plaintiffs also relied upon *ABN AMRO Bank NV v Bathurst Regional Council* . [52] The relevant statutory provisions were contained in the *Corporations Act 2001 (Cth)* and the *Australian Securities a* judgment are long. However, one of the arguments advanced by the appellants was that the respo respondents had not relied on the misleading or deceptive representations in buying the securities

via

[52] (2014) 224 FCR 1 .

QNI Resources Pty Ltd v Sino Iron Pty Ltd [2016] QSC 62 -
QNI Resources Pty Ltd v Sino Iron Pty Ltd [2016] QSC 62 -
QNI Resources Pty Ltd v Sino Iron Pty Ltd [2016] QSC 62 -
QNI Resources Pty Ltd v Sino Iron Pty Ltd [2016] QSC 62 -
Westpac Banking Corporation v Wittenberg [2016] FCAFC 33 -
Woodlawn Capital Pty Ltd v Motor Vehicles Insurance Ltd [2016] NSWCA 28 (09 March 2016) (Macfarlan, Wa

110. That being so, there is, as Woodlawn submits, no starting date from which a "reasonable period" n possible to be satisfied whether any of the letters from MVIL in the period 17 November 2011 to 13 F

Woodlawn Capital Pty Ltd v Motor Vehicles Insurance Ltd [2016] NSWCA 28 (09 March 2016) (Macfarlan, Wa

75. Sub-section 925A(2) (which has been extracted earlier at [46] above) refers to awareness by the clie requisite awareness does not include awareness of the existence of the statutory right to rescind. T *Regional Council* [2014] FCAFC 65; (2014) 224 FCR 1 . There, the Full Court (Jacobson, Gilmour and G

> ... The conditioning facts before a notice may be given pursuant to the provision [s 925A] are twofold. Fir about awareness of any right to rescind, that is an awareness of the meaning and effect of ss 924A and 92 "the facts" giving rise to such an entitlement which is required. *The facts are those, proof of which, in combi* be given within a "reasonable period" after the client became relevantly aware. (my emphasis)

Woodlawn Capital Pty Ltd v Motor Vehicles Insurance Ltd [2016] NSWCA 28 -
Woodlawn Capital Pty Ltd v Motor Vehicles Insurance Ltd [2016] NSWCA 28 -
Woodlawn Capital Pty Ltd v Motor Vehicles Insurance Ltd [2016] NSWCA 28 -
Woodlawn Capital Pty Ltd v Motor Vehicles Insurance Ltd [2016] NSWCA 28 -
Woodlawn Capital Pty Ltd v Motor Vehicles Insurance Ltd [2016] NSWCA 28 -
Siegwerk Australia Pty Ltd (In liq) v Nuplex Industries (Aust) Pty Ltd [2016] FCA 158 (29 February 2016) (Beach

ABN AMRO Bank NV v Bathurst Regional Council (2014) 224 FCR 1
Alexander v Cambridge Credit Corporation Ltd

Siegwerk Australia Pty Ltd (In liq) v Nuplex Industries (Aust) Pty Ltd [2016] FCA 158 (29 February 2016) (Beach

79. As I say, I accept that while a plaintiff has the onus of showing loss caused by the breach, if the loss contract-breaker. But such an evidentiary onus does not rise to the level of disproof as such (cf the 254 ALR 273 at [27] (8) and [46] per Jagot J; *Bathurst Regional Council v Local Government Financial Ser* *Bathurst Regional Council* (2014) 224 FCR 1)). The evidentiary onus may be discharged by showing fa

Trilogy Funds Management Ltd v Sullivan (No 2) [2015] FCA 1452 (18 December 2015) (Wigney J)

ABN AMRO Bank NV v Bathurst Regional Council (2014) 224 FCR 1; [2014] FCAFC 65
Ackers v Austcorp International Ltd

Trilogy Funds Management Ltd v Sullivan (No 2) [2015] FCA 1452 -
Tamaya Resources Limited (in liq) v Deloitte Touche Tohmatsu (A Firm), in the matter of Tamaya Resources

Tamaya Resources Limited (in liq) v Deloitte Touche Tohmatsu (A Firm), in the matter of Tamaya Resources
Melbourne City Investments Pty Ltd v UGL Limited [2015] VSC 540 -
Melbourne City Investments Pty Ltd v UGL Limited [2015] VSC 540 -
Rogers v Roche [2015] QSC 272 -
Rogers v Roche [2015] QSC 272 -
Investa Properties Pty Ltd v Nankervis (No 7) [2015] FCA 1004 -
Investa Properties Pty Ltd v Nankervis (No 7) [2015] FCA 1004 -
Investa Properties Pty Ltd v Nankervis (No 7) [2015] FCA 1004 -
Caason Investments Pty Ltd v Cao [2015] FCAFC 94 -
Caason Investments Pty Ltd v Cao [2015] FCAFC 94 -
Williams v Pisano [2015] NSWCA 177 -
Montclare v Metlife Insurance Ltd [2015] VSC 306 -
Montclare v Metlife Insurance Ltd [2015] VSC 306 -
Postorino v Encryption Technologies Corporation Pty Ltd [2015] FCCA 1634 (19 June 2015) (Lloyd-Jones J)

151. Postorino argues that Pritchard also represented that ETC was worth $30 million and that he gave
of the company, as Coombs did. Coombs communicated with Postorino for the benefit of Pritchar
communication was designed to induce Postorino to buy the shares from Pritchard or his compan
Bathurst Regional Council (supra) at [1355] there is an analogy (ambient not identical) to this matter a

Postorino v Encryption Technologies Corporation Pty Ltd [2015] FCCA 1634 (19 June 2015) (Lloyd-Jones J)

145. The second representation simply stated is that ETC was worth $30 million or more. This was cor
that ETC was worth $30 million and he attributed the increase in value, at least in part, to the "*Rus*
reference to the "*Russian deal*" was one of Coombs additions. It was a response to Postorino's previ
email was not in terms that suggested Coombs was merely passing on information for what it was
explanation. None of the three types of passing on identified by McHugh J in *Butcher v Lachlan Ele*

> *...[g]enerally, when a speaker deploys and highlights an opinion, while marketing a financial produc*
> *belief in the reliability of the opinion, the speaker is reasonably to be understood to assert that the opi*

That this present case involves shares to be sold for $125,000 makes no difference to that analysis.

Postorino v Encryption Technologies Corporation Pty Ltd [2015] FCCA 1634 -
Lambert Leasing Inc. v QBE Insurance Ltd [2015] NSWSC 750 -
Selig v Wealthsure Pty Ltd [2015] HCA 18 -
Selig v Wealthsure Pty Ltd [2015] HCA 18 -
Selig v Wealthsure Pty Ltd [2015] HCA 18 -
Grant-Taylor v Babcock & Brown Ltd (in liq) [2015] FCA 149 -
Grant-Taylor v Babcock & Brown Ltd (in liq) [2015] FCA 149 -
Caason Investments Pty Ltd v Cao [2014] FCA 1410 -
Caason Investments Pty Ltd v Cao [2014] FCA 1410 -
Latteria Holdings Pty Ltd v Corcoran Parker Pty Ltd (No 2) [2014] FCA 1378 (19 December 2014) (Mortimer J)
ABN AMRO Bank NV v Bathurst Regional Council (2014) 309 ALR 445; [2014] FCAFC 65
Australian Energy Regulator v Snowy Hydro Ltd

Latteria Holdings Pty Ltd v Corcoran Parker Pty Ltd (No 2) [2014] FCA 1378 -
Latteria Holdings Pty Ltd v Corcoran Parker Pty Ltd (No 2) [2014] FCA 1378 -
Latteria Holdings Pty Ltd v Corcoran Parker Pty Ltd (No 2) [2014] FCA 1378 -
J and a Vaughan Super Pty Ltd (Trustee) v Becton Property Group Pty Ltd (No 3) [2014] FCA 1380 (17 Decembe

7. The elements necessary to establish a cause of action under s 1041H were considered recently by th
the court said at [767] in upholding the decision of the trial judge:

At trial, LGFS established that (a) by communicating the rating S&P made the representations as t
S&P did not have reasonable grounds nor did it exercise reasonable care and skill, and (c) in those
subject to its reliance on the disclaimers does not challenge (a). Point (c) follows from (a) and (b), s

The loss or damage claimed as compensation under s 1041I by Vaughan Super in this case is plead
[15] to [24]. The foundation of the cause of action claimed by Vaughan Super in this connection are
annexed to the proposed pleading as Schedule B. Paragraph [18] of the proposed pleading sets out
by those statements to the ASX which are pleaded in paragraph [15]. It is the representations said t
Super to its detriment and to be the cause of loss and damage.

GREAT SOUTHERN LTD (in LIQ) (RECEIVERS & MANAGERS APPOINTED) -v- YOUNG [2014] WASC 48

ABN Amro Bank NV v Bathurst Regional Council [2014] FCAFC 65

GREAT SOUTHERN LTD (in LIQ) (RECEIVERS & MANAGERS APPOINTED) -v- YOUNG [2014] WASC 48
Cahill v Kenna [2014] NSWSC 1763 (10 December 2014) (McDougall J)

265. In view of the conclusions to which I have come, it is not necessary to delve into this debate. Howe

(1) where damages are claimed for misleading or deceptive conduct, in contravention of an applicable sta

(2) the inquiry must be whether the loss claimed occurred by reason of, or as a result of, that conduct - se

(3) thus, what the plaintiff must show is that the conduct in question was an effective or direct cause of th

(4) that conduct may be a direct or effective cause of the loss if it was an essential part of the chain of caus
ALR 445 at [1377] ; and

(5) focussing on reliance may divert attention from the statutory requirement: that the loss claimed be ca
inappropriate as a tool for examining the question of causation: *Campbell v Backoffice Investments Pty Ltd*

Cahill v Kenna [2014] NSWSC 1763 -
McBride v Christie's Australia Pty Ltd [2014] NSWSC 1729 (04 December 2014) (Bergin CJ in Eq)

ABN AMRO Bank NV v Bathurst Regional Council [2014] FCAFC 65; (2014) 309 ALR 445 , considered

McBride v Christie's Australia Pty Ltd [2014] NSWSC 1729 (04 December 2014) (Bergin CJ in Eq)

262. In *ABN AMRO* , an investment bank ABN AMRO created structured financial products known as C
AMRO's request. Local Government Financial Services Pty Ltd (LGFS) purchased Notes from ABN
(the highest possible rating) and this was widely publicised by both ABN AMRO in the course of m
conceded by S&P that the rating was flawed. It knew that the only purpose of its rating was to facil

McBride v Christie's Australia Pty Ltd [2014] NSWSC 1729 -
McBride v Christie's Australia Pty Ltd [2014] NSWSC 1729 -
McBride v Christie's Australia Pty Ltd [2014] NSWSC 1729 -
Highup Pty Ltd (in Liquidation) v Gubas [2014] FCA 1170 (05 November 2014) (Buchanan J)
ABN AMRO Bank NV v Bathurst Regional Council [2014] FCAFC 65; (2014) 309 ALR 445
Blatch v Archer

Highup Pty Ltd (in Liquidation) v Gubas [2014] FCA 1170 (05 November 2014) (Buchanan J)

70. Much depends on the statutory context (*Hawkins* at 572D ; *ABN AMRO Bank NV v Bathurst Regiona*

Permanent Custodians Limited v Geagea (No 3) [2014] NSWSC 1489 -
Motor Vehicles Insurance Ltd v Woodlawn Capital Pty Ltd [2014] NSWSC 1503 -
Lew Footwear Holdings Pty Ltd v Madden International Ltd [2014] VSC 320 -
Financial Services Council Ltd v Industry Super Australia Pty Limited [2014] FCAFC 92 (25 July 2014) (Gilmou
ABN Amro Bank NV v Bathurst Regional Council [2014] FCAFC 65 cited

Community Corporation 21561 v Pier Apartment Hotel Pty Ltd (No 2) [2014] SADC 130 (25 July 2014) (Slattery J
Mulvaney (as liquidator of the Hellenic Athletic & Soccer Club of SA Inc) v The Commissioner of Taxation (Cth)
United Football Club Pty Ltd [2012] SADC 179; *Parletta Constructions Pty Ltd v Prince (No 2)* [2000] SADC 101
CA); *Thompson v ACTV* (1996) 141 ALR 1; *Glenmont Investments Pty ltd v O'Loughlin* (1999) 79 SASR 185; *Godf*
Cosco Oceania Chartering Pty Ltd (no 2) [2008] FCA 1656; *Wealthsure Pty Ltd v Selig* [2014] FCAFC 64; *ABN A*
P Fire and General Insurance Company Ltd v Dixon (1982) VR 833; *JN Taylor Holdings Ltd v Bond* (1993) 59 SA
Romford Ice and Cold Storage Co Ltd [1957] AC 555, considered.

Community Corporation 21561 v Pier Apartment Hotel Pty Ltd (No 2) [2014] SADC 130 (25 July 2014) (Slattery J

57. There is a specific exclusion within s 4(2)(c) of application to liability subject to apportionment un

via

[41] There is now a considerable body of authority in Australia about what claims are apportionable: viz
Ltd v Cosco Oceania Chartering Pty Ltd (No 2) [2008] FCA 1656 and there are also demonstrable differences
Council [2014] FCAFC 65 .

Financial Services Council Ltd v Industry Super Australia Pty Limited [2014] FCAFC 92 (25 July 2014) (Gilmou

34. In those circumstances, the Court sees no reason not to give effect to its conclusion that s 622(3) mu
applicant submitted that the two provisions were directly inconsistent and that the Court should g
Authority (1998) 194 CLR 355) the Court does not share that view. Although in practical terms the re
directly inconsistent and that what is involved is rather the process of construing them in an harm
President to appoint a fresh member to fill a casual vacancy in a way which is inconsistent with s 6
accordance with the dictionary definition in s 12 (i.e., all members of the Commission regardless of
definitions which it contains apply unless the context otherwise requires that is, in fact, how s 12 is
Commission v Treloar [1992] 1 VR 447 at 449-450 (FC); *Kelly v The Queen* (2004) 218 CLR 216 at 245 [84
-[91] and most recently *ABN Amro Bank NV v Bathurst Regional Council* [2014] FCAFC 65 at [649] .

Community Corporation 21561 v Pier Apartment Hotel Pty Ltd (No 2) [2014] SADC 130 -
Rivercity Motorway Finance Pty Limited (Administrators Appointed) (Receivers and Managers Appointed) v

71. In *ABN AMRO* the Full Court drew attention at [1575] to significant differences between relevant pr
between s 1041L(1) of the Corporations Act and s 34(1) of the NSW Act . There are also significant d
differences provide any sound basis for distinguishing *Reinhold* when it comes to determining the
TPA .

Rivercity Motorway Finance Pty Limited (Administrators Appointed) (Receivers and Managers Appointed) v

36. The crux of Mr Smith's argument was that s 87CB(2) can pick up both apportionable and non-app
relation to s 1041L(2) of the Corporations Act in *ABN AMRO* and *Wealthsure* . It was accepted by th

Rivercity Motorway Finance Pty Limited (Administrators Appointed) (Receivers and Managers Appointed) v

41. Be that as it may, the Full Court in *ABN AMRO* has clearly approved Finkelstein J's reasoning in *BI*
relevant provisions of the TPA were not necessary to the decision in that case, I consider that I mu
re correct. This necessarily entails rejecting the submission put by Mr Smith SC and other counsel
against AECOM for damages under s 87 are apportionable claims.

Rivercity Motorway Finance Pty Limited (Administrators Appointed) (Receivers and Managers Appointed) v

36. The crux of Mr Smith's argument was that s 87CB(2) can pick up both apportionable and non-app
relation to s 1041L(2) of the Corporations Act in *ABN AMRO* and *Wealthsure* . It was accepted by th

Rivercity Motorway Finance Pty Limited (Administrators Appointed) (Receivers and Managers Appointed) v

40. It does seem odd that a claim for damages for conduct in contravention of s 52 brought under s 82
of s 52 , and giving rise to precisely the same loss and damage, would not also be an apportionable
VIA was intended to avoid as discussed in *BHPB Freight, Bennett* and *ABN AMRO* , will not be avoid
87 is exercised in accordance with the same considerations that inform the assessment of damages

Rivercity Motorway Finance Pty Limited (Administrators Appointed) (Receivers and Managers Appointed) v
ABN AMRO Bank NV v Bathurst Regional Council [2014] FCAFC 65
Akron Securities Ltd v Iliffe

Rivercity Motorway Finance Pty Limited (Administrators Appointed) (Receivers and Managers Appointed) v
Rivercity Motorway Finance Pty Limited (Administrators Appointed) (Receivers and Managers Appointed) v
Rivercity Motorway Finance Pty Limited (Administrators Appointed) (Receivers and Managers Appointed) v
Rivercity Motorway Finance Pty Limited (Administrators Appointed) (Receivers and Managers Appointed) v
Rivercity Motorway Finance Pty Limited (Administrators Appointed) (Receivers and Managers Appointed) v
McGraw-Hill Financial Inc v City of Swan [2014] FCA 665 (24 June 2014) (Jacobson J)
ABN Amro Bank NV v Bathurst Regional Council [2014] FCAFC 65
Astro Exito Navegacion SA v W.T. Hsu (The "Messiniaki Tolmi")

McGraw-Hill Financial Inc v City of Swan [2014] FCA 665 -