Continuous Disclosure and Class Action Lawsuits– What Does the Future Hold for New Zealand?

Assessing the appropriate balance between issuers' and investors' interests

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<u>List of Abbreviations:</u>

FMCA: Financial Markets Conduct Act

Listing Rules: New Zealand Exchange Listing Rules

FMA: Financial Markets Authority

NZX: New Zealand Exchange

ASX: Australian Securities Exchange

ECMH: Efficient Capital Markets Hypothesis

Introduction

Continuous disclosure is a complex yet vital component of Financial Markets' regulation. There is no doubt as to the importance of the obligations in helping maintain Capital Markets' integrity.[1] *However, its value cannot overshadow the need to balance all Capital Market participants' interests in furtherance of the regime's statutory purpose.*[2] *The current framework fails to achieve this balance. It grants investors excessive protection whilst placing an unreasonable and cumbersome burden on listing issuers.*[3]

The continuous disclosure framework is multi-faceted. It encompasses a broad range of legal, economic and policy considerations.[4] This dissertation aims to determine whether the obligations framework is achieving its purpose by giving a comprehensive overview and critical analysis of its application and consequences. To help assess whether the obligations fulfil this purpose, I will be utilising a balance metaphor that weighs up investors' interests on the one side and issuers' interests on the other.

In recent years, continuous disclosure obligations have been under scrutiny in both New Zealand and Australia, where Australia's analogous provisions have led to an unprecedented opportunistic class action environment.[5] Since New Zealand's obligations model the Australian regime, I will utilise primary and secondary sources from Australia throughout this dissertation. The New Zealand and Australian reports explored in chapter 1 will set the scene for establishing that the obligations, in their current form, are failing to achieve their purpose by unduly favouring investors over issuers.

Chapter 2 will outline the purpose of the regime and explain its origination and current framework, narrowing my examination to the continuous disclosure obligations in the NZX

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[1] *Financial Markets Authority v Jackson & Gibson as voluntary administrators of CBL Corporation Limited* [2018] NZHC 2052 at [45] per Venning J. As noted in *James Hardie Industries NV v Australian Securities and Investments Commission* (2010) 81 ACSR 1, 111 at [355]

[2] Financial Markets Conduct Act 2013, s 3

[3] Capital Markets 2029 *Growing New Zealand's Capital Markets 2029 - A vision and growth agenda to promote stronger capital markets for all New Zealanders* (September 2019) at 37

[4] Michael Legg and Dr James Metzger "Submission to the Australian Law Reform Commission on the Inquiry into Class Action Proceedings and Third-Party Litigation Funders (DP 85)" at 2

[5] Australian Law Reform Commission *Integrity, Fairness and Efficiency - An inquiry into Class Action Proceedings and Third-Party Litigation Funders* (ALRC R134, 2018) at 23 and 263

Listing Rules. The chapter will also compare the no-fault nature of New Zealand and Australia's regimes with the fault approach in England and Wales to illustrate an alternative liability setting for continuous disclosure.

The application of the obligations in practice is where particular issues come to light. Although the obligations may sound good in theory, in reality, compliance is a confusing and challenging task.[6] Combining this complexity with no-fault liability and high punitive sanctions means the cost of compliance is unreasonable, deterring issuers from listing on the capital market. The effect is that an imbalance exists between investor protection and access to capital.

Chapter 3 takes a step back, examining the broader context in which continuous disclosure obligations are located. This chapter involves a critical examination of both the Australian and New Zealand environment, focusing on assessing the interplay between continuous disclosure and class actions. Various developments are currently occurring within this environment, including the impact of COVID-19, which influences how the obligations are perceived, understood and applied. In Australia, the volatility caused by COVID-19 has led to a modification of the provisions, which illustrates the regime's problematic nature and emphasises the need for review.[7] Due to the continually changing environment, my research does not account for information after September 1st, 2020.

Lastly, I will provide two recommendations for reform that will help equalise the system's current imbalance. These focus on simplifying compliance and reducing the stringency of the obligations.

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[6] Andrew Lumsden, Jessica Crawford and Chris Marshall "Indecent Disclosure - the Art and Science of Continuous Disclosure: 10 Day-to-Day Scenarios in the Resource and Energy Sector" (2017) AMPLA at 2

[7] Andrew Lumsden and Alexandra Feros "Covid-19: important changes to continuous disclosure provisions" (27 May 2020) Corrs Chambers Westgarth <https://corrs.com.au/insights/covid-19-important-changes-to-continuous-disclosure-provisions>

I Calls for review in New Zealand and Australia

The current continuous disclosure environment is tumultuous. Reports in Australia and New Zealand recommend reviewing the current continuous disclosure obligations, driven by enforcement, clarity and stringency concerns. This chapter will explore two key reports, which have been instructive in establishing my dissertation's focus. Firstly, the New Zealand Capital Markets 2029's report and secondly, the Australian Law Reform Commission's inquiry into Class Actions and Litigation Funding.

A Capital Markets 2029

Capital Markets 2029, conducted by an industry-led working group and instigated by the FMA and NZX, was established to find areas for growth and improvement in New Zealand's Capital Markets.[8] The Report outlines a vision and growth agenda to promote stronger Capital Markets for all New Zealanders.[9] Part of the Report's objectives is to ensure that Capital Markets regulation appropriately balances access to capital with investor protection.[10]

The Report recommends that NZXR and FMA conduct a review of the continuous disclosure framework and MBIE reassesses the obligations' liability settings.[11] This recommendation is flagged as highly likely to strongly improve Capital Markets within the next ten years.[12] The government welcomes the recommendations and work is already underway to assess whether the current Financial Markets Conduct regulations meet their objectives.[13]

The main driver of this recommendation is the stringency of the regime. The regime's no-fault nature coupled with high punitive action for breaches makes the cost and burden of the requirements severe, affecting issuers' desire and ability to list on the Capital Market whilst unduly favouring investor protection.[14] Several adverse flow-on effects stem from the current

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[8] Above n 3, 3
[9] At 3
[10] At 7
[11] At 36
[12] At 35
[13] Kris Faafoi "Government welcomes Capital Markets 2029 Report" (press release, 9 September 2019), The Financial Markets Conduct (FMC) Act monitoring programme is assessing the current Act, which will likely include an assessment of the continuous disclosure regime.
[14] Above n 3, at 37

regime, which market participants put forward in their submissions to Capital Markets 2029.[15] These are listed below.[16]

1. An increase in class actions, powered by litigation funders.
2. High calibre individuals deterred from taking up director roles.
3. The high cost of D&O insurance premiums.
4. Issuers' attention is on complying with their disclosure requirements to the detriment of business strategy.
5. A decline in companies wanting to list on the market.

These consequences suggest that the current regime runs counter to the objective of balancing investor protection and access to capital, raising the question of whether the current regime is appropriate.

B The Australian Law Reform Commission's Report

The Capital Markets 2029's recommendation is strengthened by the previously released Australian Law Reform Commission's (ALRC) report 'Integrity, Fairness and Efficiency – An Inquiry into Class Action Proceedings and Third-Party Litigation Funders.'[17] This Report was conducted against the backdrop of a thriving class action environment, primarily driven by litigation funders.[18] The object of the ALRC's inquiry was to consider whether the class action system and the law underpinning this system require further regulation and reform.[19]

The Report recommends that the Australian Government commission a review of its continuous disclosure framework, with regard to its legal and economic impact, noting that the liability regime appears to have been arrived at unintentionally.[20] The Report does not propose changes to the current framework beyond recommending its review. However, it advocates for a comprehensive consultation to answer the question of 'whether the current laws achieve their

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[15] Above n 3, 37
[16] Above n 3, 37
[17] Above n 5
[18] At 15
[19] At 25
[20] At 263

goals in an optimal manner.'[21] The Report reflects on several unintended and potentially adverse consequences that require further consideration to determine the current regime's appropriateness.[22] These include:

1. An examination of the proper scope of private versus public enforcement.
2. The relative efficiency of shareholder class actions and their impact on board behaviour.
3. Economic effects of class actions on both issuers and investors.
4. The impact of the regime on D & O insurance.
5. Legal and regulatory issues - market-based causation, measures of loss and defences.

The Report's brief contemplation of these issue indicate that the Australian regime's balance between investor protection and expectations on issuers is out of kilter and a substantial, balanced and unbiased review of the obligations is necessary.[23] Since New Zealand's regime is similar in both its objectives and substance, these considerations are highly relevant to this dissertation.

C Imbalance in the current system

Calls for review in Australia and New Zealand indicate that the current framework warrants review and reform. The reports suggest that the challenges facing issuers under the current regime are disproportionate to the benefits gained from imposing the obligations.[24] Additionally, the ALRC Report highlights how the relationship between class actions and continuous disclosure can lead to various adverse consequences, further explored in chapter 4 on the Winds of Change.

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[21] Above n 5, 264 citing 'M Legg, J Metzger, *Submission 12*; and to similar effect see Australian Bar Association, *Submission 69*; Law Society of NSW, *Submission 64*.
[22] Above n 5, 266
[23] Above n 5, 265
[24] Above n 3, 37; above n 5; Allens "Submission to the Australian Law Reform Commission on the Inquiry into Class Action Proceedings and Third-Party Litigation Funders" at 6; Australian Institute of Company Directors "Submission to the Australian Law Reform Commission on the Inquiry into Class Action Proceedings and Third-Party Litigation Funders" at 2

II The Continuous Disclosure Regime

A History and purpose of New Zealand's continuous disclosure framework

1 Origination and purpose

Initially, the continuous disclosure obligations were contained solely in the NZX Listing Rules. In 2002, pt 2 of the Securities Market Amendment Act inserted provisions into the Securities Market Act 1988 enforcing publicly listed issuers' continuous disclosure obligations.[25] These provisions created a broad statutory requirement for continuous disclosure, whilst the obligations' specific requirements remained in the NZX Listing Rules.[26] The Securities Market Act has since been repealed.[27]

The Financial Markets Conduct Act (FMCA) was proposed in the aftermath of the Global Financial Crisis.[28] It contains the current continuous disclosure regime, which is substantively the same as the Securities Markets Act's provisions.[29] The Act's main goal was to rebuild investor trust and create a market with informed and confident participants.[30] Parliament unilaterally agreed with its fundamental principles.[31]

The FMCA's primary purpose is to ensure Financial Markets' integrity by promoting the 'confident and informed participation of business, investors and consumers' in 'transparent, efficient and fair' markets.[32] The Act's regime intends to further this objective by providing accurate, timely and clear information to investors, creating robust governance arrangements, minimising compliance costs and supporting competition in the market.[33] The policy is underpinned by the goal of supporting business growth and furthering individuals' financial ambitions by connecting investors with business opportunities on a regulated medium.[34] The

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[25] Securities Market Act 1988, ss 19B and 19C inserted by The Securities Markets Amendment Act 2002, s 16
[26] NZX Listing Rules, r 3.1
[27] Repealed by The Financial Markets (Repeals and Amendments) Act 2013 s 4 (1)(b)
[28] (6 March 2012) 678 NZPD 872
[29] Above n 2, s 270 compare to above n 25, ss 19B and 19C
[30] Above n 28
[31] (27 August 2013) 693 NZPD 12999
[32]Above n 2, s 3
[33] Financial Markets Conduct Bill (342-2) (select committee report) at 8
[34] Shelley Griffiths "Securities Regulation, Securities Law and Financial Markets Law: From Investor Protection to Consumer Protection in New Zealand, 1985-2016" in Susan Watson (ed) *The Changing Landscape of Corporate Law in New Zealand* (The Centre for Commercial and Corporate Law Inc, Canterbury, 2017) 289 at 302

language used in the Act's purpose section and the policy considerations driving it imply that the Act's provisions should consider and balance investors' and issuers' interests equally. [35]

From these objectives I have derived a *balance* metaphor, which will be useful in establishing whether provisions of the Act are appropriately fulfilling their statutory purpose. On one side of this scale are investors' interests, represented by investor protection measures. These protections allow investors to confidently invest on the market with accurate and up-to-date information. On the other side of the scale are issuers' interests, which are characterised by the reasonableness of the expectations to which they are subject. The greater the burden of their expectations, the less accessible capital markets and subsequently, business growth, are to issuers. The continuous disclosure framework, being a component of the FMCA, should be applied in a way that strives towards an equilibrium of interests, in furtherance of the Act's purpose. Although a perfect equilibrium may not be possible, having one side of the scales too heavily emphasised obstructs the regime's purpose.

2 Considerations underpinning the continuous disclosure framework

The continuous disclosure framework aims to further the purpose of 'fair, orderly and transparent financial product markets.'[36] The obligations stipulate the timely release of information to the market by listed issuers, to ensure investors are 'confident and informed.'[37] This timely release of information helps protect the integrity of trading on the market.[38] It enhances market efficiency and transparency, thus minimising the emergence of a false market and possibilities for insider trading.[39]

Information disclosure is vital in ensuring that Capital Markets are efficient and transparent. Market efficiency and transparency pertain to the association between share prices and information.[40] According to the Efficient Markets Hypothesis, the share price reflects all relevant and ascertainable information.[41] Thus, omissions or misrepresentations of such

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[35] Above n 2, s 3 refers to "confident and informed participation of business, investors and consumers"
[36] Above n 2, ss 3 and 229 (a)
[37] Above n 26, 3.1.1(a)
[38] Above n 1, at [45]; New Zealand Exchange Ltd *Guidance Note – Continuous Disclosure* (January 2019) at 4
[39] Above n 33, at 28; Larelle Chapple and Thu Phuong "Continuous Disclosure Compliance: Does Corporate Governance Matter?" (2015) AFAANZ 965 at 966 and 969
[40] Richard A. Brealey, Stewart C. Myers, Franklin Allen *Principles of Corporate Finance* (8th ed, McGraw-Hill/Irwin, New York) at 337
[41] Above n 40, at 338

information will lead to an artificial share price, frustrating the market's efficiency and leading to a false market.[42] Continuous disclosure supports a semi-strong version of the Efficient Markets Hypothesis by creating a framework that obliges issuers to disclose information relevant to the share price.[43] The timely disclosure of information ensures that Capital Markets participants make informed assessments of the risks and opportunities based on relevant information when trading on the market.[44] Where there are gaps in disclosure, participants on the market fail to have 'equality of knowledge.'[45] This inequality can be subject to exploitation by market insiders who are privy to exclusive information at the expense of uninformed market participants.[46] Effective continuous disclosure obligations minimise this risk of information asymmetry by ensuring disclosure of any such information to the market, thus reducing insider trading opportunities.[47]

Although these considerations are vital to ensuring the purpose of 'efficient and transparent' markets, the obligations must also account for the interests of all market participants to ensure the market is genuinely fair.[48] Excessive protection of market integrity can lead to an imbalanced approach, frustrating the purpose of the regime.

3 New Zealand and Australian harmonisation

Aligning New Zealand with Australian business law was a principal consideration in the introduction of the FMCA.[49] Introducing comparable continuous disclosure obligations helps ensure investors in Australia and New Zealand receive similar protections, furthering the single economic market objective of 'improving business through regulatory coordination.'[50] The similarities between the regimes imply that they will face similar risks and challenges. The

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[42] *Haylock v Patek* [2011] NZCA 674 at [168]
[43] Michael J. Duffy "Developments in United States Securities Class Actions: The Status of 'Fraud on the Market' Causation and Implications for Australia" (2011) 40 CLWR 345 at 349
[44] New Zealand Exchange Ltd *Guidance Note – Continuous Disclosure* (January 2019) at 4
[45] *Haylock v Patek* [2011] NZCA 674 at [114], citing *R v Staines and Morrisey* [1997] 2 Cr App R 426 (CA) at [430]
[46] Above n 45, at [114]-[115]
[47] Ministry of Business, Innovation and Commerce *Financial Markets Conduct Regulation Discussion Paper* (Wellington, December 2012) at 12; Australian Securities and Investments Commission, *in the matter of Chemeq Limited (ACN 009 135 264) v Chemeq Limited (CAN 009 135 264)* [2006] FCA 936 at [42]-[46] per French J there is an explicit link between insider trading legislation and the purpose of continuous disclosure
[48] Above n 2, s 3
[49] Above n 28; Memorandum of Understanding Between the Government of New Zealand and the Government of Australia on Coordination of Business Law (signed on 31 August 2000) at 3
[50] Ministry of Foreign Affairs and Trade *The Australian - New Zealand Closer Economic Relationship* (2005) at 3

debate as to whether New Zealand should maintain this parallelism is an important one that is explored further in the Recommendations chapter.

B The legislative regime

1 The Financial Markets Conduct Act

The continuous disclosure regime in New Zealand is a co-regulatory model.[51] The FMCA establishes the requirement for listed issuers to disclose information per the Listing Rules' continuous disclosure provisions for the relevant licensed market.[52] Section 270 holds that issuers must disclose following the Listing Rules' continuous disclosure provisions if three elements are satisfied.[53]

1. The listed issuer must have a listing agreement with a licensed market operator, such as the NZX.
2. The issuer must notify information subject to the continuous disclosure provisions.
3. The information must be ‘material information that is not generally available to the market.

‘Material Information’ is defined in the Act as being information that ‘a reasonable person would expect, if it were generally available to the market, to have a material effect on the price of quoted financial products.’[54] This information must also relate to a ‘particular financial product, a particular issuer or particular issuers.’[55] ‘Generally available to the market’ is information that people who commonly invest in relevant financial products will likely become aware of.[56] Alongside the continuous disclosure obligations outlined in the Listing Rules, the FMCA gives powers to the Minister of Commerce to alter and impose disclosure requirements and delegate authority to the FMA.[57]

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[51] Shelley Griffiths “Securities Law” in John H. Farrar, Susan Watson, Lynne Taylor (eds) *Company and Securities Law in New Zealand* (2nd ed, Thomas Reuters, Wellington) 1025 at 1169
[52] Above n 2, s 270
[53] Above n 2, s 270
[54] Above n 2, s 231
[55] Above n 2, s 231
[56] Above n 2, s 232
[57] Above n 2, ss 351(1)(b) and 350, The Minister can delegate this power to the FMA

2 *The NZX Listing Rules*

The relevant stock exchange's Listing Rules contain the primary continuous disclosure provisions which must be consistent with the FMCA's policy.[58] This dissertation will focus primarily on the NZX Listing Rules. Section 3 of the NZX Listing Rules contains the specific obligations of the continuous disclosure regime.[59] It establishes the requirement for issuers to promptly disclose 'material information' to the market rather than waiting for periodic reporting dates.[60] Under NZX rule 3.1, an issuer, once they become aware of any Material Information relating to them, must promptly and without delay release the 'Material Information' through the NZX's Market Announcement Platform (MAP).[61] They must not disclose it to any other party without disclosing it to MAP first.[62] The NZX has a Guidance Note that provides issuers with a guide for interpreting and complying with their continuous disclosure obligations.[63] It also gives issuers an idea of how the NZX will approach a potential breach of the obligations.

3 *Enforcement of the obligations*

The FMA regulates New Zealand's financial markets and the NZX operates the securities and derivatives market. Both regulators see continuous disclosure obligations as a high priority to safeguard the public market's integrity.[64] At first instance, the responsibility to enforce compliance sits with the NZXR, which has a wide range of enforcement tools.[65] Breaches of the continuous disclosure obligation can result in a range of civil sanctions. Matters may result in a referral to the NZ Markets Disciplinary Tribunal, which investigates breaches, imposes sanctions and approves settlement agreements between NZXR and the breaching issuer. [66] The benchmark penalty sought for a breach of the continuous disclosure provisions by NZXR is $30,000.[67] The NZXR has the ability to refer breaches on to the FMA, which conducts

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[58] Above n 2, s 270
[59] Above n 26, r 3.1
[60] Above n 26, r 3.1.1
[61] Above n 26, r 3.1.1(a)
[62] Above n 26, r 3.1.1.(b)
[63] Above n 44, at 8
[64] Memorandum of Understanding Between the Financial Markets Authority and NZX Limited (signed January 2015) at 2
[65] NZX Regulation *NZX Regulation Approach to Enforcement* (March 2019) at 3
[66] Above n 44, at 5; Larelle Chapple, Thu Phuong Truong and Michelle Welsh "The Penalty Quantum for Non-Compliance with Corporate Disclosure: Solace for the Market" (2018) 36 CSLJ 292 at 10
[67] *NZX Limited v Rakon Limited* NZMDT 1/14, 24 February 2014 at 81 citing *NZX Limited v Energy Mad Ltd* NZMDT 5/13, 11 October 2013 at 12

investigates and enforces penalties through application to the court.[68] The FMA may accept undertakings given by the breaching issuer to secure compensation or penalty payments.[69] Alternatively, the FMA may accept undertaking in lieu of pecuniary penalties.[70] The FMA is tough on enforcement, with pecuniary penalties, settlement agreements and compensation payments being costly to the issuer.[71] For example, Pacific Edge settled two continuous disclosure breaches with the FMA for $500,000.[72] Overlaps between the NZX and FMA's investigatory and prosecuting roles have led to some tension. Capital Markets 2029 highlighted how the current system can lead to high compliance costs and effort levels due to duplications of inquiries from both regulators. [73]

The company, directors and senior managers can all be held liable for breaches to their continuous disclosure obligations.[74] However, a director or senior manager may be exempt from liability if they take reasonable steps to ensure the company complies.[75] A breach may also give rise to civil action by injured shareholders. For example, the ongoing CBL shareholder class action includes a breach to the insurer's continuous disclosure obligations for which the plaintiffs are seeking damages.[76] The regime's no-fault nature means that issuers will not avoid the obligations by showing recklessness, negligence, or intention. After establishing that an issuer failed to disclose material information that does not fall under an exception liability will arise, regardless of the reasons for the failure. This liability setting makes the obligations much stricter than most other jurisdictions with similar listing requirements.[77]

C The Australian Continuous Disclosure framework

The NZX Listing Rules 3.1 and 3.1A are a near mirror image of the ASX Listing Rules 3.1 and 3.1A.[78] Additionally, both regimes are underpinned by the purposes of integrity and market

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[68] Above n 64; Above n 2, s 489
[69] Financial Markets Authority Act 2011, s 46
[70] Above n 69, s 46A
[71] Financial Markets Authority *Annual Report 2018/19* (30 October 2019) at 6; Financial Markets Authority *Regulatory Response Guidelines* (August 2016); Financial Markets Authority "Enforcement" (23 April 2019) <https://www.fma.govt.nz/about-us/how-we-regulate/enforcement/>
[72] Financial Markets Authority "Pacific Edge Limited - Settlement Deed" (25 May 2015) <https://www.fma.govt.nz/news-and-resources/cases/pacific-eagle/>
[73] Above n 3, at 37
[74] Above n 2, s 533
[75] Above n 2, s 272
[76] CBL Class Action "About the CBL class action" <https://www.cblclassaction.co.nz>
[77] Above n 3, at 37
[78] ASX Listing Rules, r 3.1

efficiency.[79] The obligations have statutory force under s 674 of the Corporations Act, with a breach of the ASX Listing Rules amounting to a breach of s 674 (2) of the Corporations Act 2001.[80]

As in New Zealand, the regime is no-fault, with liability attaching without requiring wrongdoing on behalf of the issuer (this has changed temporarily under the COVID-19 amendments).[81] The constructive knowledge approach to 'awareness' was also adopted from Australia, where 'aware' is interpreted as meaning 'if an officer of the entity has, or ought reasonably, to have come into possession of the information.'[82] A notable difference between the Australian and New Zealand regime is the time given for disclosure. Under the ASX Listing Rules, the disclosure must occur 'immediately.'[83] However, this has been interpreted as meaning 'promptly and without delay.'[84] Thus, the approach to timing is predominantly the same between the two jurisdictions.

D The fault approach in England and Wales

Unlike New Zealand and Australia, England and Wales liability settings require an element of fault to establish liability, requiring recklessness or dishonesty on behalf of the issuer.[85] England and Wales are subject to s 90A of the Financial Services and Markets Act 2000, which establishes a statutory civil liability regime, where issuers must pay compensation for loss arising from misleading statements, dishonest omissions and dishonest delays.[86] Schedule 10A was inserted into s 90A, expanding the regime and broadening the scope of included information.[87]

For liability to arise for a misleading statement, the 'person discharging managerial responsibilities within the issuer' must have known that the statement was 'untrue or

[79] Australian Securities Exchange Ltd *ASX Listing Rules - Guidance Note 8* (February 2020) at 6 referring to *James Hardie Industries NV v Australian Securities and Investments Commission* (2010) 81 ACSR 1, 111 at 355
[80] Corporations Act 2001 (Aus), s 674
[81] Corporations (Coronavirus Economic Response) Determination (No. 2) 2020
[82] Above n 78, r 19.12
[83] Above n 78, r 3.1
[84] Australian Securities Exchange Ltd *ASX Listing Rules - Guidance Note 8* (February 2020) at 14
[85] Above n 5, at 267
[86] Financial Services Markets Act 2000 (UK), 90A
[87] Above n 86, sch 10

misleading or was reckless as to whether it was untrue or misleading.'[88] Omissions require a similar standard for liability, where the 'person discharging managerial responsibilities within the issuer' must have known that the omission would amount to a 'concealment of material fact.'[89] Liability for a delay only arises if a 'person discharging managerial responsibilities' acted dishonestly.[90] 'Dishonesty' is defined as conduct that a person who regularly trades on the relevant securities market would regard as dishonest and the person committing the conduct is aware (or would be considered aware) of this perception. [91]

The liability settings of the disclosure regime in England and Wales's are of a far more director friendly nature compared to New Zealand and Australia. The requirement for dishonesty or recklessness demonstrates the government's intention to reduce the possibility of opportunistic litigation and limit private enforcement.[92]

E Comparing liability settings – no-fault versus fault

The liability provisions in England and Wales for delay and omissions of information share similarities with the New Zealand and Australian continuous disclosure framework. However, the diverging policy considerations behind the regimes have led to diverging fault approaches. Unlike in New Zealand and Australia, when establishing the liability settings of their regime, the UK Government sought to balance market integrity with the burden of private litigation in enforcing investors rights.[93] They deliberately shaped the regime with knowledge pertaining to the costs of class action litigation to avoid a speculative litigation environment.[94]

It is informative that, in light of an understanding and knowledge of class actions, the UK chose to adopt such an approach. The ALRC report notes that Australia, had it been aware of the consequences of class actions when amending its continuous disclosure obligations, may have opted against a no-fault approach.[95] However, this is not to say that either New Zealand or Australia should immediately change their liability settings. A fault-based approach makes

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[88] Above n 86, sch 10 pt 2 cl 2
[89] Above n 86, sch 10A cl 3 sub-cl (3)
[90] Above n 86, 10A, cl 5 sub-cl 2
[91] Above n 86, 10 A cl 6
[92] Above n 5, 269; *Companies Act 2006* (UK) [1643]
[93] HM Treasury *Extension of the statutory regime for issuer liability* (July 2008) at 5
[94] Above n 93, at 35
[95] Above n 5, at 272

enforcement of the obligations more difficult as the onus is on plaintiffs and regulators to prove fault. Although this has the benefit of restraining class actions, it also constraining and costly for regulators. Such an approach appears inappropriate for the New Zealand environment, where class actions do not play a large role in enforcing breaches. Instead, enforcement is left mainly to publicly funded regulators.

Establishing an appropriate continuous disclosure framework that adeptly balances all financial market participants interests is a complex task. In striking this balance, all components of the regime must be taken into account, requiring an assessment of how the obligations are applied in practice, what enforcement measures are available as well as how the framework relates to the surrounding context of class actions.[96]

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[96] Above n 4 at 2

III Compliance in practice in New Zealand

Interpretation and application of the continuous disclosure framework is key to determining whether the obligations are adequately balancing the need to protect investors whilst not being so stringent that they negatively impact access to capital. Issuers' compliance with the obligations ensures the timely disclosure of material information, thus guaranteeing that investors are 'confident and informed' and Capital Markets are 'transparent, efficient and fair.'[97] A balanced approach is necessary for the furtherance of the Act's purpose, which takes both investors and issuers interests into account.[98] The obligations may appear straightforward in practice, but they are interpreted and applied in a way that makes compliance an arduous and complicated exercise for issuers to manoeuvre, which unduly favours investors over issuers.[99]

A Combining art with science – a messy picture

Compliance is as much an art as it is a science, given the contextual nature of the obligations, lack of clarity and the demanding, time-pressured environment in which disclosures occur.[100] This combination of ambiguity and a strict timeframe can lead to personal judgment based decisions on the 'materiality' of information, which raises the chances of a breach.[101] The expectation that issuers disclose the information even if they are in doubt exacerbates this pressure and fails to account for the impact that superfluous disclosure can have on business confidence.[102] Ultimately, these issues have created an imbalance between investor protection and issuers' ability to access capital by not being unduly burdened by unreasonable expectations.

Disclosure of material information is a strict obligation, placing a heavy burden on issuers to comply. Issuers must evaluate information following the disclosure obligations as they arise, including expected and unexpected information and consider how the information may affect the market in the future. This task is difficult. It requires an understanding of the information

[97] Above n 2, s 3
[98] Above n 3, at 38
[99] Australian Securities and Investments Commission*, in the matter of Chemeq Limited (ACN 009 135 264) v Chemeq Limited (ACN 009 135 264)* [2006] FCA 936 [86] per French J
[100] Andrew Lumsden, Jessica Crawford and Chris Marshall "Indecent Disclosure - the Art and Science of Continuous Disclosure: 10 Day-to-Day Scenarios in the Resource and Energy Sector" (2017) AMPLA at 2
[101] Diane Mayorga "Managing Continuous Disclosure: Australian Evidence" (2013) 26 AAAJ 1135 at 1149
[102] Above n 44, at 23

and how it will be interpreted and used by third parties in the future. As directors are often laypersons, the obligations must be clear and unambiguous to ensure compliance is not unduly burdensome. Consequentially, it is clear from examining how the obligations operate in practice that they are challenging to apply. Thus, advice often needs to be outsourced in a very tight timeframe to determine whether a disclosure is necessary and ensure that appropriate disclosure happens promptly and without delay.

The High Court in *Financial Markets Authority v Jackson* accepted the FMA's argument that continuous disclosure obligations must be construed widely to reflect their important role in ensuring market integrity.[103] The FMA based its presumption on Australian cases outlining the purpose of the continuous disclosure regime and the Court's determination that continuous disclosure legislation is construed 'beneficially.'[104] The purpose is to ensure the efficiency and integrity of the market and ensure that investors are informed.[105] Alongside this, the obligations offer relief to harmed investors, and thus should be construed to 'give the fullest relief which the fair meaning of its language will allow.'[106] This broad application of the continuous disclosure regime must be borne in mind when examining compliance with the rules in practice. Since there is very little case law on continuous disclosure in New Zealand, substantive reference will be made to Australian case when interpreting the obligations.

B The periphery of 'information' – 'Particular' and 'generally available'

For continuous disclosure obligations to arise, information must be 'material,' particular and not 'generally available to the market.'[107] The test of whether information falls into this category is issuer-specific.[108] 'Particular information' has a broad capture, applying to information that relates to a particular issuer's securities.[109] However, the information does not need to derive

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[103] Above n 1, at 35
[104] The FMA referring to *James Hardie Industries NV v Australian Securities and Investments Commission* (2010) 81 ACSR 1, 111; *Grant Taylor v Babcock & Brown Limited (In Liquidation)* [2015] FCA 149
[105] *James Hardie Industries NV v Australian Securities and Investments Commission* (2010) 81 ACSR 1, 111, at [355]
[106] *James Hardie Industries NV v Australian Securities and Investments Commission* (2010) 81 ACSR 1, 111 at [356] citing Bull v Attorney-General (NSW) (1913) 17 CLR 370 at [384]
[107]Above n 2, s 270
[108] New Zealand Exchange Regulation *Fletcher Building Limited - Continuous Disclosure* (New Zealand's Exchange, January 2018) at 7
[109] Above n 44, at 6

from the issuer itself.[110] For example, rumours about a company's financial performance may constitute material information so long as they have sufficient degrees of 'credibility, specificity and certainty.'[111] Information originating from a third-party may also constitute ‘particular’ information. In those cases, a trading halt may need to be applied to ensure that the issuer has time to gather information and disclose it appropriately.[112]

'Generally available to the market' is defined in the Act as a two-limbed test.[113] The first limb is information that is 'made known' in a way that persons who commonly invest in securities would or would likely become aware of it and enough time has transpired for its dispersion.[114] Alternatively, it is information that is 'readily obtainable.'[115] 'Deductions, conclusions, or inferences' drawn from the first two limbs of the test will also satisfy the 'generally available' classification.[116] In Australia the courts have interpreted the two limbs of the test as being disjunctive.[117]

The category of investors within the first limb of the test is broad. Investors do not need to be professionals but should have a degree of sophistication.[118] Therefore, it would be insufficient for information to only be accessible to certain investors or needing to be substantively put together for it to make sense.[119] In the case of *Myer,* the company argued that information correcting de-facto guidance, that falsely predicted that the NPAT of FY15 would be better than that of the previous year, was 'generally available.'[120] The company relied on analyst's reports forecasting that the NPAT in FY15 would be below the previous financial year's NPAT.[121] The Court held that the reports were not 'generally available' as only a small group of paid subscribers would have access to them and 'mum and dad' investors would not be aware of the figures.[122]

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[110] Above n 44, at 9
[111] Above n 108, at 8
[112] Above n 44, at 9, above n 26, r 9.9
[113] Above n 2, s 232
[114] Financial Markets Conduct Act, s 232 (1) (a)
[115] Financial Markets Conduct Act, s 232 (2)
[116] Financial Markets Conduct Act, s 232 (3)
[117] *Grant Taylor v Babcock & Brown Limited* (In Liquidation) [2016] FCAFC 60 at [117]
[118] Above n 44, at 9
[119] Above n 44, at 9
[120] *TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Limited* [2019] FCA 1747
[121]Above n 120, at [1286]
[122] Above n 120, at [1291-2] and [1224]

'Obtainable' in the second limb of the test covers' observations, use of expertise, purchase, or any other means.'[123] In Australia, 'readily observable matters' are 'facts directly observable in the public arena.'[124] It is a question of fact that must be ascertained 'objectively and hypothetically' and does not require actual observation.[125] In *Citigroup,* the Court determined that the question was not whether the information was generally known but whether it could have been 'readily observable.'[126] This approach asks if observation of the information is straightforward.[127] The question is determined by looking at both actual and hypothetical circumstances.[128] For example, a company's financial Report is 'readily observable,' as it is easily accessible and discernible.[129]

C Predicting the unpredictable – the question of 'materiality'

If information is 'particular' and not publicly available to the market, then 'materiality' becomes the crux for establishing if an obligation to disclose the information exists.[130] Establishing 'materiality' is an ambiguous and arduous ex-ante task that essentially requires issuers to use clairvoyant powers to determine the possible future effect of information.[131] It requires a positive determination that the information might affect the market, combined with an estimation of the information's 'anticipated magnitude' on the price of listed issuers' securities.[132] This assessment is through the lens of a 'reasonable person.'[133] The assessment's objective nature makes the regime's liability settings strict, especially in comparison to other jurisdictions.[134]

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[123] Above n 44, at 9
[124] *Grant Taylor v Babcock & Brown Limited* (In Liquidation) [2016] FCAFC 60 at [119] citing *R v Firns* [2001] 51 NSWLR 548; 38 ACRSR 223; [2001] NSWCCA 191 at [56]
[125] *Grant Taylor v Babcock & Brown Limited* (In Liquidation) [2016] FCAFC 60 at [119] citing *R v Firns* [2001] NSWCCA 191 at [88] and *Australian Securities and Investments Commission v Citigroup Global Markets Australia Pty Ltd* [2007] FCA 963 at [546] and [551]
[126] *Australian Securities and Investments Commission v Citigroup Global Markets Australia Pty Ltd* [2007] FCA 963 at [551]
[127] Above n 124, at [119]
[128] *R v Firns* [2001] NSWCCA 191 at 88
[129] Above n 105, at [541]-[545]
[130] Above n 2, s 231
[131] Above n 44, at 7; Yvonne Ching Ling Lee "The elusive concept of materiality under U.S. Federal Securities Laws" (2004) 40 WULR 661 at 664
[132] Above n 124, at [96]
[133] Above n 2, s 231
[134] Above n 3, 36

The NZX has proposed a reasonable investor test coupled with a market impact test to direct issuers in this task.[135] It requires issuers to consider what a 'reasonable investor' would expect the effect of the information to be, utilising a price-movement percentage threshold as a yardstick to establish the type of effect that would likely count as ‘material.’[136] The same test for determining 'material information' is used for assessing breaches to insider trading and thus has a broad capture. Due to the similarities, resources on insider trading will help illuminate the concept of 'materiality.'[137]

1 The reasonable investor test

Since 'reasonable person' is undefined in the Act, the NZXR has created an interpretation to act as a benchmark for issuers in the Guidance Note. [138] The NZXR considers the 'reasonable person' to be someone who ‘commonly invests in securities and holds such securities for some time, based on their view of the securities' inherent value.’[139] The hypothetical investor is not a professional but should have some degree of knowledge and experience.[140] This approach is consistent with case law and overseas interpretations of 'materiality' regarding securities regulations.[141] The Australian case, *Babcock Brown*, established that 'persons who commonly invest' extends to both sophisticated and unsophisticated investors, but does not encompass irrational investors.[142] The same broad scope is likely to apply in New Zealand, creating an expectation on issuers to contemplate the perspective of a wide variety of investors. From the NZXR's perspective, this approach helps maintain the test's objectivity, as the investor is an 'independent, fair-minded bystander' whose interests are tied to neither investor nor issuers, helping ensure objective disclosures.[143]

How the reasonable investor test for assessing 'materiality' is applied originates in New Zealand from *Coleman v Myers*, which adopted the approach taken in the US securities fraud case, *TSC*

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[135] Above n 44, at 19
[136] Above n 44, at 8
[137] Michael Ziegelaar “Insider Trading Law in New Zealand” in Gordon Walker, Brent Fisse, and Ian Ramsay (eds) *Securities Regulation in Australia and New Zealand* (2nd ed, LBC Information Services, North Ryde, 1998) 556 at 606
[138] Above n 44, at 7
[139] Above n 44
[140] Above n 44, at 9
[141] Above n 137 at 609
[142] Above n 125, at [115]
[143] Above n 44, at 7

v Northway Inc.[144] In *Myers*, information is material if it would 'materially affect the mind of a vendor or purchaser.'[145] Another way of putting this illustrated in the US Supreme Court case *Basic Inc v Levinson*, where the Court held 'an omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important.'[146] Hence, the application of the reasonable investor test is as follows: issuers must look through the eyes of a 'reasonable investor,' which can encompass a wide range of possible investors[147]to predict whether they might expect the information to impact the share price.[148] The issuer must consider the effect the information may have on the reasonable investor's mind when making this prediction.[149]

The problem with this approach is that in practice, issuers will be viewing disclosure requirements from their perspectives, which are inherently tied to their own interests. Equally, when regulators are assessing if disclosure breaches have occurred, they will be focused on ensuring market integrity. [150] Thus, the interests of investors are of higher importance. Since there is no fault element, it is difficult for the issuers to defend themselves. This can have serious implications as issuers may have different conceptions of what a 'reasonable person' may consider 'material,' leading to disclosure breaches. In *Blis Technology,* the issuer considered that the increased distribution of its products from 30 to 600 Sinopharm pharmacies was not 'material information.'[151] However, the markets disciplinary Tribunal determined that since the issuer had previously announced 'major milestones' in its agreement with Sinopharm, a reasonable person would expect the increase in pharmacies to have a material effect on the price of the issuer's shares.[152] This approach was heavily investor interest focused. Interestingly, the Tribunal's approach also suggests that previous announcements will influence the 'reasonable person.' perspective, which means that issuers must consider the 'reasonable person' in light of all surrounding context as well.

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[144] *Coleman v Myers* (1977) 2 NZLR 225 at [334] citing *TSC Industries v Northway Inc* (1976) 426 US 438, 499 at [2132]
[145] Above n 144, at [334]
[146] *Basic Inc v Levinson* (1988) 485 US 224 at 231
[147] Above n 44, at 19
[148] Above n 137 at 610
[149] Financial Markets Authority *Statement of Intent 2020-2024* (16 June 2020) at 16-17
[150] Above n 105, at [355]
[151] NZ Markets Disciplinary Tribunal *Public Censure of Blis Technologies Limited by the NZ Markets Disciplinary Tribunal for a Breach of the NZX Main Board Listing Rule 10.1.1(A) and (B)* (announcement, 12 December 2014) at 7
[152] Above n 149, at 7

2 *The market impact test*

Subsequent cases and the FMCA have integrated a market impact test into the question of 'materiality,' requiring an assessment of the information's potential effect on the share price.[153] Hence, issuers must apply both a reasonable investor test (assessing how information may affect investors' minds) and a market impact test (considering what impact the information will have on the share price).

There remains uncertainty surrounding the question of what constitutes 'material effect' on the share price and how this is determined. This question is left undefined in the Listing Rules, leaving it up to the company to determine if such an effect has or is likely to take place. The difficulty is that 'material effect' is a flexible standard that may vary depending on the issuer's size and its financial product's characteristics.[154] The NZXR notes that their investigations are not based on hindsight and instead engage in a forward-looking inquiry encompassing a variety of information.[155] The NZX has established a price-movement threshold to supplement arguments that particular information is 'material.'[156] Accordingly, a price movement of 5-10% acts as a premise for investigation.[157] Although, the NZX generally considers a 10% price movement enough evidence to establish 'material effect,' they claim that price-movement by itself is not determinative for liability and is only a cross-check.[158] Instead, the NZXR will look at whether issuers carefully considered the potential market response.[159]

This additional consideration is necessary as the threshold standard is ill-equipped to assess 'material effect.' It varies depending on the issuer's size, the financial product's characteristics and the Capital Markets' environment.[160] When the market is volatile, the shortfalls of the threshold test become most apparent.[161] In light of COVID-19, the NZXR remarked that no change to an issuer's share price can constitute a 'material effect' due to the market's

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[153] Above n 137 at 610
[154] Above n 44, at 7
[155] Above n 44, at 8
[156] Above n 44, at 8
[157] Above n 44, at 8
[158] New Zealand Exchange Regulation *NZX Regulation Case Study: Continuous Disclosure - Listing Rules 10.1.1* (NZXR, November 2017) at 2
[159] Above n 44, at 8
[160] New Zealand Exchange Regulation *NZX Thematic Review 2019: Market Announcements - Material Information* (NZXR, 2019) at 16; Above n 44 at 8
[161] Australian Institute of Directors "Dealing with Continuous Disclosure in the COVID-19 Environment - AICD proposal for a temporary safe harbour" (7 April 2020) <www.aicd.companydirectors.com.au>

volatility.[162] Nonetheless, issuers have been treating the price-movement threshold with considerable importance.[163] This effect is unsurprising since a percentage threshold offers issuers a clear and endorsed scientific basis for establishing 'materiality,' rather than having to attempt the ‘art’ of establishing materiality through the viewpoint of a reasonable investor.[164] To determine whether the information will likely meet the threshold, companies can consider the effect following speculations and empirical research.[165]

3 *Reasonable investor test and market impact – an incongruous pair*

Two concerns stand out in the current approach to establishing 'materiality.' Firstly, the 'objectivity' of the test places issuers in a Catch-22.[166] Issuer liability rests on whether or not the court or regulator decides the information is material.[167] Although the issuer's deliberations provide the factual matrix for the decision and may illustrate careful consideration of market response, they are irrelevant to the ultimate determination of 'materiality’ and, consequently, liability.[168] Since the obligations are strict, if the court or regulator confirms 'materiality,' then liability for nondisclosure will arise, regardless of the reasons for why the issuer considered the information immaterial.[169] Additionally, the impact on the market is observable ex post facto.[170] Thus the court and regulators have the benefit of hindsight. They assess the information whilst knowing what effect the information had on the share price, which they use as a cross-check for liability.[171] This heavily disadvantages the issuer who does not have this benefit when making their decision.[172]

[162] Joost van Amelsfort “NZX Regulation Issuer Update: COVID-19 and approach to disclosure” (8 April 2020) New Zealand’s Exchange <www.nzx.com>
[163] Above n 160, at 2; Above n 151, at 611
[164] Above n 44
[165] Above n 151, at 611
[166] Yvonne Ching Ling Lee “The elusive concept of materiality under U.S. Federal Securities Laws” (2004) 40 WULR 661 at 680. I have phrased it as a catch-22 because issuers are expected to apply a particular test to determine materiality and thus compliance, however, the objective nature of the test means that their own deliberations are irrelevant, with the benefit of hindsight given to regulators and the court exacerbating this issue
[167] Above n 105, at [527]
[168] Above n 105, at [527]
[169] Above n 149
[170] Above n 98
[171] Above n 105, at [534] referring to Gilmour J in Fortescue Metals at [477]
[172] Sophie Cunliffe "Materiality: An Obstacle to the Enforcement of Insider Trading Law" (2008) 1 NZLSJ 449 at 477

Secondly, the application of both a reasonable investor test and a market impact test generates contradictions.[173] There are various challenges to assessing market impact through the lens of a reasonable investor. For example, behavioural finance suggests that investors tend to place sentiment above rational economic calculation.[174] This is contrary to the ECMH assumption that an efficient market will quickly incorporate new information into the price of the securities.[175] Deviations from rationality make it hard for issuers to predict how investors perceive information and its potential effect on the stock price.[176] Therefore, to determine how the information will affect the price of its securities, issuers must assess the information by utilising information, knowledge and expertise particular to them as issuers. Although this is a logical response, as share price movement is critical to liability, the use of this information is contrary to the reasonable investor perspective. The reliance on market impact suggests that the reasonable person test is an inappropriate mechanism for assessing 'materiality.'[177] Therefore, the current approach to 'materiality' is not only elusive, difficult to apply and overly stringent; it is also nonsensical.

The question of 'materiality' is an essential component of the continuous disclosure framework. How it is applied helps determine if the obligations are appropriately furthering the Act's purpose. It appears the current approach, utilising both an investor test and market impact test, is favouring the interests of investors at the expense of issuers. This imbalance runs counter to the Act's objective of equally promoting both issuers' and investors' interests.[178]

D Ignorance is not bliss – the 'constructive knowledge' test

Another contribution to the regime's stringency is that liability can arise without requiring actual knowledge of the material information. New Zealand recently adopted a constructive knowledge test as applied in Australia.[179] The question is whether a director or senior manager 'ought reasonably to have' become aware of information in the course of their duties.[180] The addition of 'ought to have known' ensures that the company has processes in place that escalate

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[173] Above n 137 at 611
[174] Above n 43, at 359
[175] Above n 151, at 607
[176] Kirsty Johnston, Christine Tether, and Ashley Tomlinson *Financial Product Disclosure: Insights from Behavioural Economics* (Ministry of Business, Innovation and Employment, OP15/01, February 2015) at 17
[177] Above n 151, at 610
[178] Above n 2, s 3 (a)
[179] NZX Listing Rules, pt A
[180] NZX Lising Rules, pt A; Above n 44, at 16

information through the company.[181] However, its introduction has received backlash. Bell Gully, in its submission to the NZX Listing Rules review, identified two potential adverse effects of the test:[182]

1. The imposition of 'unnecessary and material compliance costs on issuers;' and
2. Dissuasion of issuers from listing on the NZX as the cost of compliance and risk of liability is too great

The court and regulators will likely determine whether an issuer had constructive knowledge by utilising a factual inquiry of the available information and considering the context surrounding the issuer at the alleged time of breach.[183] This inquiry raises a substantial risk of hindsight bias in determining *what* issuers ought to have known and *when* they ought to have attained this awareness.[184] Arguably, regulators and the court will perceive information that 'ought reasonably to have been known' without comprehending the situation's actualities at the time.[185] Although hindsight is considered a non-sequitur,[186]the reality is that regulators and the market can and often do judge with hindsight.[187] Additionally, the test advances when the obligation to disclose 'promptly and without delay' is triggered, increasing pressure to disclose as soon as possible, which may lead to premature disclosure.[188]

The constructive knowledge test may dissuade issuers from listing on the NZX, curtailing their access to capital.[189] The test places a substantive burden on issuers to be continuously monitoring their escalation processes, which is costly and time-consuming.[190] Additionally, demanding compliance costs are dissuading people from becoming directors and a constructive knowledge standard will likely aggravate this.[191] A constructive knowledge standard adds to the already high levels of liability exposure that directors face. This reduces the number of

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[181] New Zealand Exchange *NZX Listing Rule Review - Consultation Paper* (consultation paper, NZXR, 11 April 2018) at 9
[182] Bell Gully "Submission to the NZX Listing Rule Review Consultation Paper" at 7
[183] Above n 122, at [155]. There is no New Zealand case law or investigations that showcase how constructive knowledge will be applied as of yet
[184] Institute of Directors "Submission to the New Zealand Exchange on the exposure draft of the NZX Listing Rules" at 4
[185] Above n 182, at 7
[186] Above n 124, at [179]
[187] Above n 98, at 6
[188] Above n 184, at 4
[189] Above n 3, at 37
[190] Above n 101, at 1150
[191] Institute of Directors and ASB *Director Sentiment Survey 2019* (November 2019)

individuals willing to take on director roles for companies listed on the public market.[192] The effect is that issuers are less able to attain high-calibre individuals as directors, reducing the incentives to list on the Exchange.

E A short timeframe for disclosure

As established above, continuous disclosure can be arduous to apply in practice, creating an imbalance between investor protection and issuer support. The rushed timeframe in which disclosures must occur exacerbates this imbalance. Issuers must carefully strike a balance between timely disclosure and premature prejudicial disclosure.[193]

Once an issuer becomes aware (or ought reasonably to be aware) of material information, they must disclose it '*promptly and without delay*.'[194] According to the NZXR, 'promptly and without delay' is a flexible criterion that depends on both the nature of the information and the circumstances at the time.[195] The NZXR will likely assess the character, complexity and quantity of the particular information, the origination of the information, whether it requires verification by a director or senior manager and the time it takes for the issuer to draft and check through an announcement.[196] Issuers are expected to have appropriate processes in place to ensure the timely disclosure of information.[197]In the investigative Report of Fletcher Buildings, the NZXR held that issuers must respond with urgency to material information, including convening board meetings at short notice and accessing advisors outside of office hours.[198] This expectation connotes the idea that issuers must drop everything for the sake of disclosure occurring 'promptly and without delay.' If this is the expectation, then despite the apparent flexibility, the words imply 'prompt and vigorous' action similar to the previous 'immediacy' standard.[199]

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[192] Above n 184, at 4
[193] Above n 101, at 1158
[194] NZX Listing Rules, r 3.1.1(a)
[195] Above n 44, at 20
[196] At 20
[197] At 22
[198] Above n 108, at 13
[199] ASX Guidance Note 8 at 14 refers to 'immediately' as meaning doing something 'as quickly as it can be done in the circumstances without delaying, postponing or deferring'

The NZXR also expects disclosures to occur outside of trading hours and wants issuers to manage their activities to make this possible.[200] Intra-day disclosure is considered disruptive to 'fair, orderly and transparent markets.'[201] If disclosure is unable to occur before the market opens, a trading halt may be needed to give the issuer enough time to respond to information.[202] However, they cannot be used to postpone disclosure deliberately.[203] Evidence suggests that trading halts can have adverse effects, such as increased volatility and price uncertainty.[204] This may prompt issuers to release information as fast as possible before the market opens to avoid a trading halt, which can lead to prejudicial disclosure.

Information released by third-parties, such as regulatory bodies, may also trigger disclosure obligations in certain circumstances.[205] Issuers should coordinate with these third-parties to ensure the release of information provides the issuer with time to comply with its regulatory obligations.[206] Of course, this is not always possible and expecting an issuer to monitor not only its own disclosures, but those of third-parties, places an arguably excessive burden on issuers.[207]

An adverse effect of this strict disclosure time-frame is the impact the obligations have on the relationship between the disclosing entity and third-parties in commercial transactions.[208] The timing of disclosure can be a challenging issue to navigate when another entity is involved. It can lead to confusion and tension in business relations with third parties, especially those in other jurisdictions.[209] Third-parties who are sensitive to public disclosure of their business activities may be averse to the information's timely disclosure by the issuer.[210] Regardless, waiting for third parties to authorise a disclosure is not a permissible ground for a delay, as was illustrated in the case of Pacific Edge.[211] The issuer sought approval from its American

[200] Above n 158, at 26, 27
[201] Above n 158, at 27
[202] Above n 44, at 22; Above n 158, at 26
[203] Above n 44, at 22
[204] Report of the Technical Committee of the International Organisation of Securities Commission [2002] Report on Trading Halts and Market Closures pg 20
[205] Above n 44, at 21
[206] New Zealand Exchange Regulation *NZX Thematic Review 2017 - Continuous Disclosure* (NZXR, 2017) at 17
[207] Above n 206, at 17
[208] Above n 101, at 1151
[209] Above n 101, at 1151
[210] Above n 101, at 1151
[211] Financial Markets Authority "FMA issues warning on continuous disclosure obligations and secures $500,000 compensation payment from Pacific Edge Limited" (press release, 25 May 2015)

contractual counterparty rather than immediately disclosing the agreement, this amounted to a likely breach of the obligations, resulting in a settlement agreement.[212] Additionally, planning business activities to ensure that disclosure occurs outside of trading hours may not be possible when conducting business with companies in different time-zones.

F When can issuers withhold market-sensitive information?

As established in The Regime chapter, issuers can withhold material information if they meet all three limbs of the exception test.[213] There is no hierarchy between these limbs.[214] From assessing how the exceptions are applied, it is clear that it is intended to have a limited scope and application.

The first limb requires that information satisfy a prescribed 'safe harbour' provision, as listed below.[215]

1. Disclosure of the information would be a breach of law
2. The information pertains to an incomplete negotiation or proposal
3. The information is insufficiently definite or a matter of supposition
4. The information is for internal management purposes
5. The information is a trade secret

Interpretations of these provisions are narrow. There is a limited range of information which is considered trade secrets or information generated for internal management purposes, due to the nature of such information generally.[216] The NZX reiterates that internal management information is only exempt insofar that a reasonable person would not expect its disclosure, re-emphasising the narrowness of the exceptions' scope.[217]

The scope of the 'breach of law' is slightly unclear. This provision was considered in *Auckland International Airport Ltd v Air New Zealand*.[218] Auckland Airport released information

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[212] Financial Markets Authority "Pacific Edge Limited" (25 May 2015)
[213] Above n 44
[214] *Auckland International Airport Ltd v Air New Zealand Ltd* HC AK CIV-2006-404-5212 at [52]
[215] NZX Listing Rules, reg 3.1.2(a)
[216] Above n 44, at 17-18
[217] Above n 44, at 18
[218] Above n 214 at [48]

concerning its price settings to Air New Zealand, who signed a confidentiality deed before receiving the information.[219] Air New Zealand considered the information 'material' and sought to disclose it, which AIAL opposed.[220] The court held that since disclosure would breach the confidentiality deed, it constituted a breach of law.[221] Conversely, the NZX Guidance note, which was released after the judgement, considers that confidentiality or non-disclosure agreements do not limit issuers' obligations under Rule 3.1.[222] Accordingly, information must breach more than contractual obligations to constitute a 'breach of law.'[223] Further, the Listing Rules make it clear that issuers must avoid, where possible, entering into obligations that inhibit the execution of Rule 3.1.[224] The court would likely interpret 'breach of law' narrowly as this is in line with other provisions of the exception.

The exception of 'incomplete negotiations or proposals' is intended to avoid disclosure prejudicially impacting ongoing negotiations, however it also has a limited application.[225] The NZ Markets Disciplinary Tribunal has made it clear that negotiations and proposals do not need to be legally binding to be held as complete under Rule 3.1.2. (a) (ii).[226] This decision aims to avoid companies structuring their affairs to circumvent their obligations.[227] In *NZX v Rakon,* the Tribunal determined that a signed but not yet legally binding agreement did not fall under the exception.[228] In that case, the fact that reopening of the negotiation was possible up until the payment of a deposit did not inhibit the agreement being considered 'complete.'[229] The Tribunal held that "the act of executing a formalised record of the terms of a potential legal relationship, with board approval on either side, reflects a high degree of certainty and commitment of the parties to those terms, at a moral and commercial level."[230] However, a signed agreement will generally be a clear indicator of disclosure, drawing a line in the sand.[231]

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[219] At [6]
[220] At [11]
[221] At [53]
[222] Above n 44, at 28
[223] Above n 44, at 17
[224] Listing Rules 3.3.1
[225] NZ Markets Disciplinary Tribunal *Public Censure of Rakon Limited by the NZ Markets Disciplinary Tribunal for a Breach of NZX Main Board Listing Rule* 10.1.1 (announcement, 5 March 2014) at [11]
[226] Above n 228, at [12-13]. The Tribunal was referring to rules under the previous Listing Rules, however these have not changed in relation to the exceptions
[227] *NZX Limited v Rakon Limited* NZMDT 1/14, 24 February 2014 at [67]
[228] Above n 225, at [18]
[229] Above n 227, at [65]
[230]Above n 227, at [66]
[231] Above n 225, at [14]

Matters of 'supposition' or 'insufficiently definite' relate to speculative or incomplete information. For example, information pertaining to analysts' forecasts may qualify as matters of supposition because they are predictions of future events.[232] Information based on 'piecemeal' or 'initial' information is considered insufficiently definite.[233] Nonetheless, issuers are under an obligation to seek additional information to determine if the information is material.[234]

The second hurdle is for information to remain confidential, as otherwise, an obligation to disclose arises.[235] Confidentiality is a strict standard, defined as 'secret.'[236] Exceptions exist for particular professional advisors and official bodies.[237] A breach of confidentiality establishes a disclosure requirement, regardless of whether information falls under a 'safe harbour' provision.[238] In *Myer,* the court held that draft internal financial forecasts were suppositions, generated for internal management purposes and insufficiently definite.[239] Thus, the issuer did not need to disclose.[240] However, the public forecast made by the CEO broke confidentiality, invalidating the exception.[241]

The last requirement is that a reasonable person would not expect disclosure of the information.[242] It covers information that would 'unreasonably prejudice the issuer' or 'provide no benefit to a person who commonly invests in financial products.'[243] However, Harrison J in *Auckland International Airport* did not consider these conditions a proscriptive limitation to the reasonable persons expectations.[244] Instead, the test requires "an objective assessment of all relevant circumstances" once the first two steps are met.[245]This objective test has a narrow scope since information satisfying the first two limbs of the exceptions will usually satisfy the reasonable person requirement.[246] There are few circumstances where the first two limbs of

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[232] Above n 120*,* at [1291]
[233] Above n 44, at 11
[234] NZX Listing Rules and Above n 44, at 11
[235] Above n 44, at 18
[236] Above n 44, at 18
[237] Above n 44, at 18
[238] Above n 120, at [1307]
[239] Above n 120, at [1299]
[240] At [1299]
[241] At [1303]
[242] NZX Listing Rules, reg 3.1.1(c); Above n 44, at 19
[243] Above n 44, at 19
[244] Above n 214, at [54] – note that he was referring to the previous guidance note 3, however there is little change
[245] At [57]
[246] Above n 44, at 19

the test are met, but the third is not.[247] Overall, the exceptions are narrow in their application and only partially useful to issuers who wish to avoid disclosing information.

G Is the current application of the regime achieving the Act's purpose?

As established, the FMCA's purpose is to ensure Capital Markets are 'transparent, efficient and fair', with 'confident and informed participation of businesses, investors and consumers,' through the protection of investors and fostering of business growth.[248] Thus, execution of the obligations must strike a balance that ensures investors are protected and issuers are subject to reasonable expectations that do not inhibit their access to capital.

The broad capture of 'information,' the convoluted 'materiality' approach, tight time-constraints and narrow exceptions, mean that the regime's current application is placing unreasonable expectations on issuers, leading to unsubstantiated, judgement-based decisions.[249] Additionally, the regime's no-fault nature makes it hard for issuers to defend themselves from the tough civil sanctions that may follow a breach. Therefore, the regime's balance is titled heavily in favour of investor protection, at the expense of issuers.

The Capital Markets 2029's Report highlights the adverse effects of this imbalance.[250] The complexity and stringency of the regime's application is causing issuers to become overly cautious and spend significant amounts of time on risk-oversight, detracting attention from business strategy.[251] Furthermore, high compliance costs dissuade people from taking director roles and deter issuers from listing.[252] D&O insurance is becoming increasingly costly because of the risk of a breach.[253] This adds an extra barrier for issuers to overcome in order to access capital and this is especially challenging for smaller and start-up companies with little spare capital. Thus, access to capital is hindered, running counter to the objective of the Act.[254]

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[247] Above n 120, at [1302]
[248] Financial Markets Conduct Act, s 3
[249] John Price, Commissioner of Australian Securities and Investments Commission "Continuous Disclosure" (Speech to Chartered Secretaries Australia Annual Conference, 3 December 2012)
[250] Above n 3, at 37
[251] Above n 3, at 37; Above n 192, at 5
[252] Above n 191, at 5
[253] Institute of Directors, MinterEllisonRuddWatts and Marsh *Directors and Officers Insurance: Trends and Issues in Turbulent Times* (June 2019) at 4
[254] Above n 3, at 7

IV Winds of Change

Now that the continuous disclosure framework's operation and the challenging nature of compliance is understood, it is necessary to view the obligations within their wider context. This chapter will focus on assessing the obligations in relation to the evolving class action environment and the recent volatility caused by COVID-19.

A The story of the two little pigs

The COVID-19 wolf came to knock on the door:

To better understand all the elements and considerations circulating in this chapter, I would ask you to tap into your childhood and remember the story of the three little pigs (in our scenario there are only two little pigs). In this story, the wolf represents COVID-19 and the houses represent the different continuous disclosure jurisdictions. New Zealand and Australia seem to have similar straw houses, but when the wolf came knocking on the doors, it blew over Australia's easily, while New Zealand's held strong. So what made the New Zealand house more stable and what lessons derive from this?

B Australia's Straw House

"He huffed and he puffed and he blew the house down…"

COVID-19 has significantly impacted the Financial Securities Markets, leading to some drastic changes in Australia.[255] The continuous disclosure obligations were deemed unfit for the COVID-19 environment, causing the Hon Josh Frydenberg, Treasurer of the Australian Commonwealth, to temporarily modify the Corporations Act 2001.[256] Regulators and plaintiffs must now show that the entity had 'knowledge of' or was 'recklessness or negligent' that information would affect the price of securities if it were generally available.[257] The

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[255] Andrew Lumsden and Alexandra Feros "Covid-19: important changes to continuous disclosure provisions" (27 May 2020) Corrs Chambers Westgarth <https://corrs.com.au/insights/covid-19-important-changes-to-continuous-disclosure-provisions>

[256] Josh Frydenberg "Temporary changes to continuous disclosure provisions for companies and officers" (press release, 25 May 2020); Corporations (Coronavirus Economic Response) Determination (No. 2)

[257]Corporations (Coronavirus Economic Response) Determination (No. 2) 2020 (explanatory note). Recklessness and Knowledge are imported from the Criminal Code 1995

"reasonable person…" in section 677 has also been omitted and replaced with "an entity knows or is reckless or negligent with respect to whether information would have a material effect on the price or value of ED securities of the entity if the entity knows or is reckless or negligent...".[258] Recklessness and knowledge import subjectivity into the liability settings of the obligations.[259] Interpretation of negligence in this context will likely be narrow as the modification intended to move away from an objective 'reasonable person' test.[260] The reasoning was that the previous disclosure requirements were unfit to cope with the market volatility and uncertainty caused by COVID-19. [261] However, this raises questions regarding whether the obligations themselves are generally unsuitable.

1 Australia's Class Action Environment:

Australia introduced its Class Action regime in 1992 through Part IVA of the Federal Court of Australia Act.[262] The Federal Court Act as well as part 9.3 of the Federal Court Rules provide the system for instigating Class Action lawsuits in the Federal Court of Australia.[263] The regime largely reflected the recommendations made by the ALRC in 1988.[264] The purpose and social utility of the regime was to increase justice by improving efficiency and vindicating just claims through a fair process.[265] It is important to note that at the time of introduction it was anticipated that the regime might be used to provide redress for shareholders if there is a breach of the ASX Listing Rules by a listed company.[266] The Minister for Justice and Consumer Affairs maintained that the regime will provide a way to enhance shareholders' access to justice and provide assistance to the formal regulators such as ASIC.[267] There was acceptance and intention for the development of shareholder class actions at the time of introduction. The regime's introduction did not garner bipartisan support as interested parties raised a range of concerns.[268] The main points of contention were that the regime would open floodgates to

[258] Above n 257, at 4
[259] Criminal Code Act 1995, ss 5.1, 5.2, 5.3, 5.4, 5.5
[260] Above n 257, at 4. 'Negligence' being a civil tort is more appropriately left to the court to decide its scope
[261] Above n 256
[262] Federal Court of Australia Act 1976, pt IVA
[263] Federal Court Rules, pt 9.3
[264] The Law Reform Commission *Grouped Proceedings in the Federal Court* (ALRC R46, 1988) at 27. The ALRC took into consideration the fact that the mass production of goods and services has made mass scale injury and loss a common reality
[265] Justice Bernard Murphy "Keynote address: Class Actions - Current Issues after 25 years of Part IVA" (University of NSW, 23 March 2017)
[266] ALRC Discussion Paper 1988 pg para 65
[267] (13 November 1991) 149 APD Senate 3018
[268] (13 November 1991) 149 APD Senate 3018. Senator Durak considered the Bill "a monstrosity"

litigation; impede upon traditional ways of exercising legal rights; create entrepreneurial, lawyer promoted proceedings; and encourage extensive out of court settlement.[269] Some of these concerns have eventuated following the regime's introduction, alongside some unanticipated complications. These arguably inhibit the execution of the regime's goals and contributed to the recent collapse of the continuous disclosure regime.[270]

2 Growth of Shareholder Class Actions and Litigation funding

The thriving state of class actions in Australia today, especially shareholder class actions, is unlikely to have been anticipated by decision makers.[271] The regime has experienced a high growth rate, mainly due to the prevalence of litigation funders. Empirical research conducted by Monash Professor, Vince Morabito, shows that 637 Class Actions have been filed between March 4th 1992 and June 30th 2019 and the number of class actions has steadily grown over the years.[272] Shareholder class actions made up 122 of all class actions, making them the most popular type of class action in Australia.[273] Albeit, accounting for competing class actions, the number of individual companies subject to shareholder class action proceedings drops down to 63.[274] Litigation funding is a significant contributor to class actions' growth, with all shareholder class actions having been funded.[275] Litigation funding was, until recently, mostly unregulated in Australia; The High Court overruled the torts of champerty and maintenance, allowing third parties to benefit from litigation.[276] This makes Australia the perfect environment for litigation funding to flourish, increasing competition to find breaches or to file competing claims.[277] Alongside this, third-parties now have a vested interest in finding continuous disclosure breaches. This has led to unintended consequences, including a rise in D&O insurance prices, difficulty in compliance and prevalence of competing class actions. [278]

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[269] Above n 268
[270] Moira Saville and Peta Stevenson *Ripe for Reform - Improving the Australian Class Action Regime* (Institute for Legal Reform, report. March 2014) at 1
[271] Above n 5 at 23
[272] Vince Morabito *An Evidence-based Approach to Class Action Reform in Australia: Shareholder Class Actions in Australia - Myths v Facts* (Monash University, November 2019) at 12
[273] Above n 272, at 16
[274] Above n 272, at 16
[275] Above n 5, at 69
[276] *Campbells Cash and Carry Pty Limited v Fostif Pty Limited* [2006] HCA 41
[277] XL Catlin and Wotton + Kearney *How did we get here? The history and development of securities class action in Australia* (whitepaper, May 2017) at 13
[278] Above n 5, 263

Class actions for breaches of continuous disclosure typically develop from an ASIC inquiry into a company that has experienced a marked change in the share price.[279] If ASIC investigates a price movement, litigation funders will often pursue the claim even if ASIC does not. It is hard to determine whether these claims pursued by the class actions are, in fact, meritorious. Hardly any class action suits have advanced to judgment, with the majority being settled out of court.[280] Companies are more willing to make a settlement payment than go to court, since this is a costly process and often results in a market confidence decline.[281] The high standard of the obligations makes the chance of a large pay-out too risky even if the company has a good defence.[282] Over 50 percent of shareholder class actions have been settled as of 2019, with the majority of other claims either being stayed, discontinued or transferred to another jurisdiction.[283] This gives litigation funders an advantage as even if there was no breach, the company is likely to settle. This appears counterintuitive to the obligations' goals, which are to ensure market integrity and investor protection.[284] Unmeritorious claims do not protect investors as they have not been harmed; instead, they merely serve the interests of the funders, which is contrary to the regime's objectives.

Additionally, meritorious claims that do reach settlement can also adversely affect the integrity of the market. In a submission to the ALRC, Professor Legg and Dr Metzger suggest that settlements accompanied by non-admission of guilt allow corporations to hide their wrongdoing.[285] Thus, the current shareholder model for enforcing continuous disclosure breaches appears counter to the objective of 'transparent' and 'efficient' markets.

A driver of this unanticipated and averse class action environment is that the operation and enforcement of the substantial law underpinning shareholder class action proceedings is unfit for purpose. ASX and ASIC accept that the continuous disclosure obligations are inherently difficult to comply with, especially regarding the test of materiality.[286] By looking at share

[279] Above n 277, at 20
[280] Australian Law Reform Commission *Inquiry into Class Action Proceedings and Third-Party Litigation Funders* (ALRC DP85, 2018) at 28
[281]Australian Institute of Company Directors "Submission to the Australian Law Reform Commission on the Inquiry into Class Action Proceedings and Third-Party Litigation Funders" at 4
[282] Larelle Chapple, Thu Phuong Truong and Michelle Welsh "The Penalty Quantum for Non-Compliance with Corporate Disclosure: Solace for the Market" (2018) 36 CSLJ 292 at 3
[283] Above n 272, at 20
[284] Above n 79
[285] Above n 4, at 3
[286] Above n 84, at 11

price movement on the market, ASIC, and consequentially litigation funders, will always have the benefit of hindsight. To emphasise this point, ASIC's commissioner accepted that the benefit of hindsight makes it easier to see when a decision was wrong as they can look at how the information affected the market in reality.[287] If there was no price movement, ASIC is unlikely to bring an action. [288] To help cope with this, the commissioner recommends issuers follow the questions posed by the ASX Guidance note 8. The issuers are to ask themselves the following questions: "Would this information influence my decision to buy and sell securities in the entity at their current market price?" and "Would I feel exposed to an action for insider trading if I were to buy or sell securities at their current market price, knowing this information had not been disclosed to the market?"[289] These questions bring an element of subjectivism and culpability into determining 'materiality,' which is contrary to the obligations' objective nature and illustrates the gaps in the current approach.

Overall, issuers are left in a disadvantageous position. They face the impossible task of predicting the future and the advice they receive on how to comply is, at best, a useful tip and, at worst, a misleading precedent. It is also noteworthy that although ASIC and ASX may acknowledge the difficult task faced by issuers and may show some leniency, class action litigators will not be so kind. They are motivated by their own interests rather than public utility. This plays into the issue of the tense relationship between public and private enforcement.

3 Private versus public enforcement

There is a tension surrounding the scope of public versus private enforcement, which influences the wider question of whether the current regime is appropriate.[290] Whether continuous disclosure obligations are enforced by public or private entities has bearing on how meritorious enforcement claims are, as well as how they deter and compensate necessary parties. A reliance on private enforcement in Australia's case has led to failure on both of these grounds.

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[287] John Price, Commissioner of Australian Securities and Investments Commission "Continuous Disclosure" (Speech to Chartered Secretaries Australia Annual Conference, 3 December 2012) at 5
[288] Above n 287
[289] Above n 83, at 11
[290] Above n 5 at 266

ASIC plays a central role in the enforcement framework. As already addressed, investigations conducted by ASIC will often spurn class action lawsuits. Despite ASIC's ability to bring actions for continuous disclosure breaches, in the past it has tended to shy away from enforcement, instead leaving it to private litigation.[291] ASIC has a wide array of enforcement powers at its disposal, being able to bring both criminal and civil actions, which include infringement notices.[292] When deciding whether or not to pursue misconduct, ASIC looks to the regulatory benefits. It assesses whether the misconduct is part of a trend and whether taking action will send a message.[293] They also consider whether another method may be appropriate in light of the cost and time of proceedings.[294] On this basis, they encourage private action to be taken to allow them to reallocate their resources elsewhere.[295] ASIC argues that since the Corporations Act provides ways for shareholders to take private action, regulators should not have to carry the full burden of enforcement, especially as private class actions are an efficient way of ensuring justice.[296] This is also reinforced by the fact that ASIC has a tendency to avoid imposing significant breaches on issuers, instead opting for negotiated outcomes.[297] On the other hand, since bringing a claim as an individual is costly and difficult, shareholders are forced to participate in class actions to get compensation.

This highlights the tension between private and public enforcement and raises questions over who should be responsible for holding companies that breach their obligations to account. The Hayne report noted that ASIC's starting response of "how can this be resolved through agreement," is an inappropriate approach for a conduct regulator as compliance cannot be achieved purely through negotiation.[298] Commissioner Hayne recommends that ASIC's enforcement culture change, with the key focus being on ensuring that the law is obeyed and

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[291] Jeremy Cooper, Deputy Chairman Australian Securities and Investments Commission "Corporate Wrongdoing: ASIC's Enforcement Role" (Keynote address to International Class Actions Conference, Park Hyatt Melbourne, 2 December 2005)
[292] Elisabeth Boros "Public and Private Enforcement of Disclosure Breaches in Australia" (2009) 9 JCLS 409 at 417
[293] Australian Securities and Investment Commission *ASIC's approach to enforcement* (Information Sheet 151, September 2013) at 4
[294] Above n 291, at 4
[295] Australian Securities and Investments Commission "Submission to the Australian Law Reform Commission on the Inquiry into Class Action Proceedings and Third-Party Litigation Funders" at 11
[296] Above n 293, at 11
[297] Kenneth M. Hayne *Final Report: Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* (Royal commission, final report vol 1, 1 February 2019) at 425
[298] Kenneth M. Hayne *Interim Report: Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* (Royal commission, interim report vol 1, 28 September 2018) at 277

enforced.'[299] Enforcement should not be left to private actions as the considerations and incentives involved are markedly different from those involved in public enforcement.[300] ASIC has accepted that its enforcement approach must change and has started to implement a 'Why not litigate?' approach.[301] This means that, once satisfied that a breach is more likely than not to have occurred and that there seems to be a public interest involved, ASIC will actively ask itself: 'Why not litigate?'[302] When taking action ASIC intends to pursue, if appropriate, both private individuals and the corporate entity to ensure corporate and individual accountability.[303]

This growing scope of public enforcement in Australia is likely to result in a drastic change in the enforcement landscape. What effects this will have on private litigation is yet to be seen. Running parallel to the changing public enforcement approach are the new rules facing litigation funders. From August 22nd, litigation funders will need to hold Australian Financial Services Licences and operate as Managed Investment Schemes.[304] The changes are in conjunction with an inquiry by the Parliamentary Joint Committee on Corporations and Financial Services on Litigation Funding and the Regulation of the Class Action Industry.[305] This is likely to result in a deceleration of litigation funding as the funders adjust to the new requirements.[306] This may create the space for public regulation to flourish. There are conflicting views on the appropriateness of a purely publicly regulated sphere.[307] The scope of that debate is too extensive for this dissertation, however it is noteworthy that this is taking place. The Report by the Parliamentary Joint Committee may shed some light on the future of private versus public enforcement.

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[299] Kenneth M. Hayne *Final Report: Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* (Royal commission, final report vol 1, 1 February 2019) at 432
[300] Above n 290, at 432
[301] Sean Hughes "ASIC's approach to enforcement after the Royal Commission" (Speech at the annual Conference of the Banking and Financial Services Law Association, Gold Coast, 30 August 2019)
[302] Above n 301
[303] Above n 301
[304] Josh Frydenberg "Litigation funders to be regulated under the Corporations Act" (press release, 22 May 2020)
[305] Parliament of Australia "Litigation funding and the regulation of the class action industry" < https://www.aph.gov.au/Parliamentary_Business/Committees/Joint/Corporations_and_Financial_Services/Litigationfunding>
[306] Ronald Mizen "New rules could see funded class actions grind to a halt" (27 July 2020) Australian Financial Review <www.afr.com/politics/federal/new-rules-could-see-funded-class-actions-grind-to-halt>
[307] Australian Institute of Directors "Dealing with Continuous Disclosure in COVID-19 Environment - AICD proposal for a temporary safe harbour" (7 April 2020) <www.aicd.companydirectors.com.au>; Tony Boyd "Beware ASIC Replacing Class Actions" (17 June 2020) Australian Financial Review <https://www.afr.com/chanticleer/beware-asic-replacing-class-actions-20200616-p5535d>

4 Circularity issues

The circularity issue is another consideration that raises questions over the legitimacy of shareholder class actions. The circularity issue suggests that security class action lawsuits do not serve their purpose of deterrence and compensation as those who end up paying for the action are the shareholders themselves.[308] This leads to pocket shifting between shareholders and money being lost in between to lawyers and litigation funders. The settlement and litigation expenses are both borne by the defending company's shareholders, albeit by differing shareholders. The ALRC also made note of the circularity issue in its Report. The Report acknowledged that, according to Miller, there are three classes of shareholders: Victims, who have lost out because of the companies breach; winners, who sold their shares and made a profit from the breach; and the targets, who are shareholders during the time the company has the class action brought against it.[309] The company often loses profitability and its assets value diminishes through the class action, penalising the 'target' shareholders.[310] Therefore, those shareholders bear the cost of litigation and the effect that litigation has on the company. This unfair and disproportionate effect of shareholder class action raises questions as to the legitimacy of the actions themselves. Professor John Coffee holds that rather than questioning whether securities class actions are frivolous, we should instead be looking at who should bear the penalties. He suggests shifting the damages onto the culpable parties and away from the innocent shareholders.[311]

Ultimately, when enforcing obligations, public entities' motives and actions are inherently aligned with the market integrity purposes of the regime. On the other hand, private enforcers, swayed by their own interests, excessively pursue potential breaches for the purposes of making a profit. Given the incentive for shareholders to litigate and issuers to settle, reliance on private enforcement has contributed to the excessive number of class actions and a potentially significant number of unmeritorious enforcement claims. Additionally, circularity issues in class action lawsuits leads to the costs and benefits of litigation being distributed in ways that contradict the deterrence and compensation purposes of continuous disclosure enforcement.

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[308] John Coffee "Reforming the Securities Class Action: On Deterrence and its Implementation" (2006) 106 Colum L Rev 1534 at 1534
[309] Above n 5, at 276
[310] Above n 5, at 277
[311] Above n 308, at 1538

What implications does Australia's environment have for New Zealand?

From observing the context within which Australia's continuous disclosure have operated, it is understandable why the regime crumbled when faced with the COVID-19 wolf. As illustrated above, the foundations upon which the obligations operated were unsound. Perhaps it was less a result of the COVID-19 wolf's huffing and puffing and more due to the shaky enforcement foundations upon which the house was built that led the treasurer to announce that the obligations would be temporarily modified.

C New Zealand – A house of sticks on solid foundations?

"He huffed and he puffed but it did not blow down"

As already illustrated, New Zealand's continuous disclosure obligations are nearly identical to Australia's and face similar levels of market volatility and uncertainty due to COVID-19. Yet, New Zealand has chosen not to modify its obligations.[312] This is because the FMA does not see a risk of opportunistic class actions as it exists in Australia. The FMA also considers that the current legislation is appropriate despite acknowledging the recommendation for a review by the Capital Markets 2029 report.[313] They highlight the need to avoid using hindsight when assessing if there was a disclosure breach. The NZXR also made it clear that the continuous disclosure rules and continuous disclosure guidance note continue to apply.[314] The NZXR did acknowledge that the new COVID environment is exceptionally volatile, resulting in a growth of share price movements. The main concern is how to assess 'materiality' under these conditions.[315] The NZXR gave some general directions to approach materiality in its Guidance Note Update. They noted that the percentage threshold is not determinative and is only used by the NZX as a reference point.[316] Information may be material even if it results in the share

[312] Financial Markets Authority "FMA Statement on Director Liability and Continuous Disclosure" (press release, 17 June 2020)
[313] Above n 312
[314] Joost van Amelsfort "NZX"s Regulation Issuer Update: Covid-19 approach to disclosure" (NZX Regulation update, 8 April 2020) at 1
[315] Australian Institute of Directors "Dealing with Continuous Disclosure in the COVID-19 Environment - AICD proposal for a temporary safe harbour" (7 April 2020)
[316] Above n 314 at 2

price remaining unchanged.[317] Decisions that will have a significant impact on operating or capital expenditure must be assessed to determine what effect they will have on the share price in the COVID-19 environment, thus requiring disclosure.[318] The NZXR recommends that companies be cautious when identifying 'material' information and may need to make a number of consecutive announcements as the implications of COVID-19 become clearer. In relation to financial projections, the NZXR holds that forecasts that have not been withdrawn will be held as valid. Issuers should not assume that the market will account for and integrate the impact of COVID-19 into their own interpretations of pre-COVID projections.[319] Instead, issuers should be reviewing their disclosures and updating them as soon as there is a material risk of the financial products actual results differing from the forecasts. Although the COVID environment makes it difficult for issuers to be sure what the impact will be on their financial products, they are expected to disclose as soon as information is 'material.'[320] Even if issuers consider their information incomplete, the obligation still exists to seek out further information and disclose the information if it is 'material.'[321] The fact that COVID-19 has made the possibility of gaining clear information more difficult does not exempt issuers from their obligation to seek out information and disclose it once sufficient information is available to form a view.[322] The NZXR makes it clear that information that the NZX is likely to deem 'material' includes actual or prospective covenant breaches and cancellations or deferrals of dividends.[323] The reason the NZXR highlights these as being 'material' is that, due to the impact of COVID-19, some issuers are facing more covenant breaches and dividend cancellations or deferrals than usual. This also applies to any decisions relating to the deferral or cancellation of interest payments. The NZXR also reminds companies of their capital raising obligations, noting that relevant administrative announcements may need to be made. [324] Despite these recommendations, there were no actual changes to the rules. So why are the New Zealand obligations better at withstanding COVID-19 than Australia's?

1 Class actions in New Zealand - a gathering storm?

[317] At 2
[318] At 2
[319] At 3
[320] NZX Listing Rules 3.1
[321] At 3
[322] At 4
[323] At 4
[324] At 4

Auckland University Lecturer Nikki Chamberlain has conducted New Zealand's first and to date, only empirical research on class actions in New Zealand. It demonstrates that class actions are on the rise, despite New Zealand not having a formal regulatory regime.[325] The only governing law is rule 4.24 of the High Court Rules, which allows plaintiffs to sue on behalf of other persons.[326] Although this rule was not created in anticipation of the modern class action environment, the courts have applied it liberally to allow plaintiffs to create class actions.[327] For example, in a recent landmark decision, the Court of Appeal accepted an 'opt-out' approach to class actions, which automatically makes people with a relevant claim a member of the class action making it easier for plaintiffs and funders to create claimant groups.[328] However, there is little clarity surrounding how far the court will take the High Court rules, which creates uncertainty and makes regulation a necessity for curing the defects in the current un-legislated model. While it is undeniable that class actions are becoming more frequent, a range of factors are stemming this growth. Chamberlain expounds these factors in her report and they are as follows: [329]

1. The lack of a statutory framework
2. The Accident Compensation Scheme inhibits claims being brought for personal injury, which is a large proportion of class actions in other jurisdictions.
3. The courts are averse to giving out large damages awards, which limits the attractiveness of bringing a claim.
4. The relative size of New Zealand means that less claims exist and are brought.
5. Litigation funding has been slow to grow in New Zealand due to the torts of Champerty and Maintenance barring third-party funding of litigation.[330]

Although the torts of Champerty and Maintenance are still recognised in New Zealand, the courts tend to minimise them due to the strong public policy reasons for allowing litigation funding.[331] The appropriateness of the tort is heavily debated and may be abolished due to

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[325] Nikki Chamberlain "Class Actions in New Zealand: An Empirical Study" (2018) 24 NZBLQ 132 at 154
[326] High Court Rules 2016, r 4.24
[327] Above n 325, at 137
[328] *Ross v Southern Response Earthquake Services Limited* [2019] NZCA 431
[329] Above n 320, at 151
[330] Sir Douglas White "Setting the Scene: The law reform project and current review of class actions and litigation funding" (Speech at the Future of Class Actions Symposium, The University of Auckland Business School, 15 March 2018) at 9
331 *PricewaterhouseCoopers v Walker* [2017] NZSC 151, [2018] 1 NZLR 735 at [100]. Citing *Trendtex Trading Corporation v Credit Suisse* [1982] AC 679 NZHL at 703 per Lord Roskill

strong opposition.[332] Chamberlain expects to see a growth of litigation funding in New Zealand for a range of reasons. These include the reduction of the Maintenance and Champerty torts, the need for third-party funding of financially pressured plaintiffs and the economic viability of third-party funding.[333]

If litigation funding flourishes we would likely see a jump in the number of class actions being brought. Although New Zealand's class action environment is still relatively small, there appears to be a storm brewing on the horizon. There are clear indications that the courts see class actions as a legitimate form of litigation and are open to developing this area of law. There have also been some key Australian cases, which are likely to guide New Zealand's legal approach in meaningful ways. For example, the Federal Court in the *Myer* shareholder class action case accepted the 'market-based causation' theory, meaning shareholders do not need to prove loss from the breach, rather, it is presumed.[334]

The future of class actions and litigation funding in New Zealand is uncertain. The New Zealand Law Commission has reopened its review of Class Actions and Litigation Funding.[335] The review is in its early stages, therefore, this dissertation can only speculate as to what the Report will recommend. So far the Law Commission has recognised that New Zealand's regime is underdeveloped in comparison to other jurisdictions.[336] Accordingly, the Commission's task is to design a regime which realises the benefits of class actions and litigation funding whilst avoiding potential costs and harms. The commission is in the unusual and lucky position of effectively having a 'blank canvas' to work with as there is no regime in place as of yet. This means that they can learn from other jurisdictions and find a regime that is a good fit for New Zealand. The commission has already mentioned that they intend to benefit from other jurisdictions and overseas reviews.[337] Hopefully the Law Commission will take into consideration the relationship between continuous disclosure obligations and shareholder class actions when making their recommendations.

[332] Law Commission *Subsidising Litigation* (NZLC R72, 2001) at 10
[333] New Zealand Law Society "Litigation funding and class actions" (7 June 2019) NZLS <https://www.lawsociety.org.nz/news/lawtalk/issue-929/litigation-funding-and-class-actions/>
[334] Above n 120, at 1671
[335] Law Commission "Competing class actions as a 'beauty parade'" (17 August 2020) <https://www.lawcom.govt.nz/news/class-actions-news>
[336] Above n 330, at 11
[337] Above n 330, at 11

Since shareholder class actions are not currently a large component of New Zealand's enforcement regime, enforcement is left primarily to public regulation. This has fostered a robust public enforcement regime, which is governed by the Financial Markets Authority and NZXR. Under the FMCA, the FMA has a wide range of enforcement powers at its disposal, which it intends to use on a fit-for-purpose basis. [338] There seems to be an overall perception that the FMA is highly effective in its regulatory capacity.[339] It can be inferred from the FMA's public statement that its main focus is on conduct and promoting trust and confidence in the markets.[340] It has the strategic priority of achieving "credible deterrence of misconduct" through active enforcement.[341] Because the regulator sees continuous disclosure as a high priority, the monitoring and enforcement of the obligations are consistently reviewed. This review process includes putting pressure on the NZX to be rigorous in their and investigations and enforcement. In the 2020 review of NZX, the FMA found that there was still scope for the NZX to increase the depth and scope of its continuous disclosure inquiries.[342]

In any case, what is clear is that New Zealand's regulatory approach differs from Australia's in that the regulators do not shy away from taking active steps beyond investigations. They are involved in enforcement and are not afraid to issue large penalties.[343] Whether this would still be the case if shareholder class actions had a more significant role in litigating disclosure breaches is debatable. The recent 4 million dollar increase to the FMA's litigation fund will likely see regulators involvement in enforcement of continuous disclosure breaches remain the same or increase.[344] Thus, I suggest that New Zealand's public enforcement scope would not decrease even with an increase in shareholder class actions. If this is the case, it may be implied that many of the issues faced by Australia in relation to the private versus public enforcement scope would not eventuate.

[338] Financial Markets Authority *Regulatory Response Guidelines* (August 2016) at 8
[339] PricewaterhouseCoopers *Financial Markets Authority - Efficiency, Effectiveness, and Baseline Review* (Ministry of Business, December 2019) at 5
[340] Rob Everett *Annual Corporate Plan 2019/20* (Financial Markets Authority, Corporate Plan, 2020) at 18.
[341] Financial Markets Authority *Strategic Risk Outlook 2019* (9 August 2019) at 9
[342] Financial Markets Authority *Market Operator Obligations Review - NZX* (June 2020) at 6
[343] Financial Markets Authority "Pacific Edge Limited - Settlement Deed" (25 May 2015) <https://www.fma.govt.nz/news-and-resources/cases/pacific-eagle/>
[344] Kris Faafoi "$4 million increase in FMA litigation fund to strengthen enforcement capability" (press release, 29 October 2019)

D A house is only as strong as its foundations

New Zealand and Australia's continuous disclosure regimes teach us that whether the house collapses depends more on the strength of its foundation, than the make-up of the house itself. While New Zealand's continuous disclosure obligations essentially mirror Australia's, the environments in which they operate are fundamentally different for two main reasons. Firstly, Australia has a booming class action environment and New Zealand does not. Secondly, Australia relies significantly on private enforcement of obligations, whereas New Zealand relies significantly on public enforcement. Private enforcement and class actions may, to an extent, grow in prevalence in New Zealand. However, it is still unlikely these will reach the same problematic levels seen in Australia. The public regulatory scope has already been established in New Zealand and is unlikely to be diminished. At the same time, the Law Commission's review of class actions will hopefully take into consideration the lessons learned from Australia and ensure New Zealand does not face the same issues.

V Recommendations

A How to rebalance the continuous disclosure regime

1 The key issues that are facing the current regime:

Currently, the 'no-fault' regime is weighted heavily towards investor protection, placing excessive and unreasonable expectations on issuers. This runs counter to the purpose of the FMCA, which places equal emphasis on the interests of investors and issuers. It is imperative that the regime be reviewed and rebalanced to ensure that the Act's purpose is fostered.

The below diagrams illustrate the balance metaphor alluded to in earlier chapters. They demonstrate the current balance and projected balance under the new recommendations. On the left of each diagram is the level of investor protection, on the right is the stringency of expectations placed on issuers. Note that I consider a perfect equilibrium unfeasible considering the conflicting interests of investors and issuers.

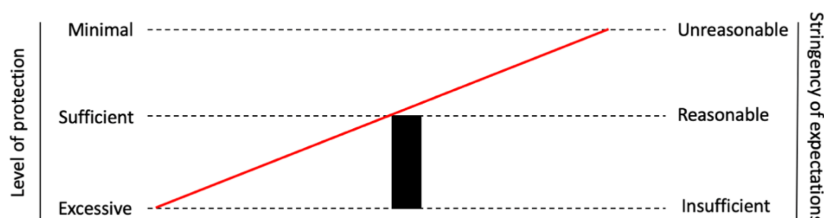

Diagram 1: The current regime balance

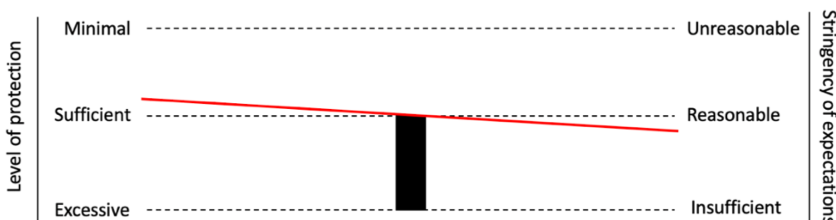

Diagram 2: The aimed for regime balance under the recommendations

The matters I consider most pressing within the existing continuous disclosure regime are as follows:

1. **Clarity** – The task for determining 'material information' is ambiguous and complex, making it difficult for issuers to comply in practice.
2. **Timing** – Currently, the NZXR appears to be interpreting 'promptly and without delay' as near immediacy, requiring issuers to place their disclosure obligations above all else. This approach is causing personal-judgement-based decisions, which increase the chances of a breach and seem contradictory to the regime's spirit.
3. **Stringency** – The regime being no-fault makes it especially investor-friendly for class actions and regulators, tilting the balance unduly towards market integrity and investor protection over issuer support.

There needs to be a refinement of the obligations across these factors to ensure a more appropriate balance between investor protection and the reasonableness of expectations placed on issuers.[345] These recommendations will help ensure New Zealand avoids the Australian regime's consequences, which were arrived at unintentionally.[346]

B Recommendation 1 – the reasonable issuer test

Insert the following section into the Act:

Meaning of a reasonable person

(1) In this part, when assessing material information for the purpose of establishing a continuous disclosure obligation under s 270, a **reasonable person** means –

  a) A listed issuer party to a listing agreement with the New Zealand Exchange; and
  b) Is of a similar size and liquidity of the issuer that the pertinent information applies to; and
  c) Has adequate processes in place to assess the information; and

[345] Above n 2, at 37
[346] Above n 5, at 263

d) Has considered the potential impact on the market from disclosing the information based on the knowledge and information the issuer had available to it at the time

Firstly, it is imperative to note that this recommendation applies specifically to continuous disclosure obligations under the Listing Rules, as stated in (1), to avoid altering insider trading requirements.[347]

Under the FMCA, 'material information' is determined by looking at whether a 'reasonable person' would expect the information to have a material effect on the price of securities.[348] The interpretation of a 'reasonable person' is currently a 'reasonable investor,' which can be a confusing and challenging test to apply, as outlined in chapter 3.[349] This interpretation has led to an imbalanced environment where investors are excessively protected and issuers must navigate ambiguous and unreasonable expectations.[350]

I recommend that 'reasonable person' be defined as an objective issuer possessing pertinent features. The objective issuer must be of the same liquidity to the relevant issuer since this can influence the share price movement.[351] The current 'reasonable person test' assesses information from a hypothetical investor's viewpoint, who has a vastly different knowledge base and interests to the issuer. My recommended approach effectively amounts to a question of whether the issuer acted as a 'reasonable issuer' would. By changing the viewpoint to a reasonable issuer, the issuer's obligations become more aligned with their own knowledge and interests, reducing the amount of clairvoyance required when complying with the test. This change resolves the conflict between the current market impact test and investor test. This creates a framework which is still objective, but more explicitly outlines the scope for what a reasonable issuer should consider when making continuous disclosure decisions.

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[347] Financial Markets Conduct Act 2013 s 231. This section also applies to insider trading laws.[347]
[348] Financial Markets Conduct Act, s 231
[349] Above n 44
[350] This was explored in chapter 3
[351] Above n 206, at 6

1 A scientific basis for disclosure – The Framework

I recommend the NZX establish a guideline that outlines how issuers should apply the 'reasonable issuer' test. The test includes a consideration of any information that may affect the share price and has potential material implications for the company's performance, projections, company structure and outlook. A reasonable issuer must understand and identify these elements, which will act as an effective proxy for determining whether there is an expectation for information to have a material effect on the price of the issuer's quoted financial product.[352] I propose that if issuers complied in disclosing information affecting these elements, investors would have the necessary information to make informed investment decisions; the ECMH supports this approach.[353]

The NZX should endeavour to make the scope and application of this framework clear and straightforward. The NZX may consider delineating and detailing the different kinds of information that commonly have significant implications for a company's performance, projections, company structure and outlook. While there can still be no definitive list of the type of information that is material – as is the case within the current regime – this new framework enables the NZX to provide more scientific guidelines. Whether information will have material implications for a company's performance, projections, company structure and outlook is much easier to define and answer than assessing how an investor would perceive the information. The former can be answered, at least in part, by modern economic theory, other empirical literature and common sense – skills and knowledge that one can expect a "reasonable issuer" to have. The latter is overly complicated and unfit for purpose, for reasons I have already explained in depth.

This dissertation will not attempt to pronounce which specific factors should be outlined in the guidance note, as this is well outside the ambit of my research. However, the point remains, that in principle, it is possible to provide such guidance. Successful guidance of this sort reduces the reliance on personal judgement in disclosure decisions and provides the foundation for a more consistent and transparent assessment of issuer decision making. Continuous disclosure will be less of an art and more of a science.

[352] Above n 167, at 706
[353] Above n 40, at 338

2 *Potential criticisms of the recommendation:*

A key concern is that changing the 'reasonable person,' from a reasonable investor to a reasonable issuer, subverts the independent fair-minded bystander perspective. Instead, the perspective of someone whose interests align with the issuer is supported.[354] Since the reasonable issuer possesses similar characteristics and information to the issuer, there is an inherent risk that the issuer's subjective interests are taken into account. Although I concede that this risk exists, a correct application of this test should mitigate it. When issuers are considering 'materiality,' they are looking through an objective and reasonable issuer lens, which has a broad scope. This approach considers all factors that a typical issuer would consider relevant to the information's market impact, including investors' interests. Regulators will also take this approach when assessing if there was a breach.

Another concern may be that the proposed framework's capture is too narrow, increasing information asymmetry and undermining the market's integrity. This concern is unwarranted. I conducted a stress test of the proposed framework, assessing whether the list of potentially material information under the Guidance Note fell within the criteria of information relating to the issuer's performance, projections, company structure and outlook. All of the information listed was straightforwardly captured by the framework, demonstrating the appropriateness of its scope.

A third anticipated criticism is that the recommendation fails to account for the vulnerability of investors. Issuers are at an unfair advantage because they are privy to important information, which they may or may not disclose.[355] Obligations and regulations are the only safeguards for ensuring that information reaches investors.[356] Therefore, they must be effectively applied to balance out information asymmetry. Indeed, my recommended "reasonable issuer" test tips the balance back toward issuers and reduces the level of investor protection. However, this is only to the extent that investors are inordinately protected in the first place. The benefits gained from a more transparent and straightforward obligation test greatly outweigh the nominal costs of reduced investor protection, particularly given the regime's no-fault nature and significant punitive action following a breach. Furthermore, I posit that part of being an investor does and

[354] Above n 44, at 7
[355] Above n 47, at 12
[356] Above n 136, at 66

should entail managing risks to pursue rewards. Thus, the disclosure obligations should only aim to mitigate risks, which would otherwise lead to asymmetric information.

If necessary, to mitigate these criticisms, an overt requirement may be included for the reasonable issuer to consider a reasonable investor's interests. To avoid this requirement effectively amounting to the current approach of viewing the information through a reasonable investor's lens, consultation with industry professionals and regulators is required. Adopting this requirement in addition to the recommendation would help equalise the balance between investor protection and expectations on issuers.

C Recommendation 2 – Extending 'promptly and without delay'

My second recommendation is to extend 'promptly and without delay' to encompass up to a 24-hour time period, easing some of the regime's cost and burden. This approach will allow issuers more time to gather third-party advice and make thoughtful inquiries and assessments concerning their disclosure obligations, reducing judgment-based decisions. Additionally, it will help issuers disclose information outside of trading hours without implementing a trading halt.

Arguably, this recommendation poses a risk to the market's integrity as there is a longer time-span in which information asymmetry and insider trading may occur. However, there are safeguards in place under the Act protecting investors from insider trading, which the recommendation does not affect.[357] Moreover, I recommend establishing a stringent confidentiality requirement in the Guidance Note, which ensures that all investors are trading on the same informational basis, reducing information asymmetry. A breach of this requirement, irrespective of who caused the breach, means the original 'promptly and without delay' approach is reinstated.

Additionally, it may be argued that the recommendation will reduce investor confidence because it seemingly diverges from the principles of efficient and transparent markets. Since information is not being released to the market as quickly, the market is less transparent and the share price is not an accurate reflection of all available information. The effect is that

[357] Financial Markets Conduct Act 2013, s 234

investment decisions are misinformed within the 24-hour timeframe, which may lead to poor investment choices. However, there is doubt surrounding the accuracy of the Efficient Markets Hypothesis.[358] It is suggested that information may not be immediately understood and utilised by investors in a way anticipated by efficient market theory.[359] Therefore a temporary delay of its release is unlikely to have a significant impact on the market. In any case, if information remains confidential within the 24-hour timeframe, investors are still not disadvantaged relative to each other – 'equality of knowledge' is maintained.[360]

D Do not throw out the baby with the bathwater

I have decided not to recommend replacing the objective test with a fault-based approach such as the recklessness, negligence, or knowledge approach as temporarily adopted in Australia.[361] Although it would be significantly less stringent by requiring a level of blameworthiness, as issuers are only liable when they are reckless, negligent, or knowingly in breach of their obligations, the costs outweigh any potential benefits and are contrary to the purpose of the regime.

When determining a breach, the issuer's subjective awareness of their liability or risk of liability would need to be assessed, shifting the onus from issuers demonstrating compliance to regulators proving fault.[362] Although negligence may create some level of objectivity, it is likely to be coloured by recklessness and knowledge and hence interpreted narrowly. This approach imposes an arduous and time-consuming task on regulators and plaintiffs who have to gather evidence and justifications to prove non-compliance.[363] Since the New Zealand class action environment is undeveloped, the FMA and NZX would be most affected, constraining the Capital Market's public regulatory oversight. The result would be a less transparent and efficient market, as the compulsion on issuers to disclose is significantly diminished. Another danger is that issuers may attempt to delay or restrict the amount of information they disclose.

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[358] Kirsty Johnston, Christine Tether, and Ashley Tomlinson *Financial Product Disclosure: Insights from Behavioural Economics* (Ministry of Business, Innovation and Employment, OP15/01, February 2015) at 3
[359] Richard A. Brealey, Stewart C. Myers, Franklin Allen Principles of Corporate Finance (8th ed, McGraw-Hill/Irwin, New York) at 343; Aswarth Damodaran *Investment valuation: tools and techniques for determining the value of any asset* (3rd ed, Wiley, Hoboken, 2012) at 130-140
[360] Above n 45 at [114] citing *Staines v Morrisey* [1997] 2 Cr App R 426 (CA) at 430
[361] Corporations (Coronavirus Economic Response) Determination (No. 2) 2020
[362] Above n 261, at 4
[363] AP Simester and WJ Brookbanks, *The Principles of Criminal Law* (4th Ed, Thomson Reuters, Wellington, 2012)

Since the constructive knowledge test is inoperable under a fault-based regime, there is scope for issuers to circumvent their obligations by claiming a lack of knowledge or understanding.

In the UK and now Australia, the implementation of a fault-based regime was based on a deliberate policy choice to control the risk of opportunistic class actions.[364] New Zealand does not have this risk, making it gratuitous to change the regime's foundational approach. Instead, modifications to the current no-fault regime are an apt way of dealing with any concerns in the current scheme. However, if New Zealand's class actions environment were to develop significantly, the risk of overlitigation will increase the already heavy burden of continuous disclosure and may lead to unanticipated consequences as witnessed in Australia.[365] Thus, I recommend that the Law Commission bear in mind the relationship between shareholder class actions and continuous disclosure obligations when establishing their recommendations for the upcoming inquiry into Class Actions and Third-Party Litigation Funding.[366]

1 Implications on Australian harmonisation:

If New Zealand maintains a no-fault regime and Australia decides to keep its current fault-based approach, this will create some level of discord in the Trans-Tasman harmonisation policy. Variance in regulations between the two countries may have implications for the business environment created by the Trans-Tasman bubble, currently being discussed in light of COVID-19.[367] If the bubble eventuates, this may warrant placing an increased level of priority on achieving business and regulatory alignment with Australia. Of course, continuous disclosure obligations are one part of that environment and therefore changes to them may be involved in such an agenda. Although this is notable, it is mere speculation, and further research is needed to determine how diverging continuous disclosure obligations will impact upon New Zealand and Australian business relations under a Trans-Tasman bubble and otherwise.

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[364] HM Treasury *Extension of the statutory regime for issuer liability* (July 2008) at 29
[365] Above n 5
[366] I anticipate that this will be a relevant concern in the Law Commission's inquiry into class actions and litigation funding
[367] Katharine Murphy "Morrison and Ardern agree on travel 'bubble' between New Zealand and Australia" (5 May 2020) The Guardian <https://www.theguardian.com/world/2020/may/05/trans-tasman-travel-bubble-to-allow-flights-as-soon-as-lockdowns-ease-morrison-and-ardern-agree>

Conclusion

The continuous disclosure framework has been subjected to scrutiny and recommendations for reform in recent years. Although this is in part centred around their interplay with the unprecedented development of class actions in Australia, the obligations themselves require reform.

The balance of the environment at present is weighted too heavily in favour of investors. An undue focus on market integrity has led to burdensome, ambiguous and ultimately unreasonable expectations being placed on issuers, whilst investors are overprotected. Australia has shown how these obligations can fall apart when located within an overly opportunistic class action environment and exposed to high market volatility. Substantial review and reform of the obligations is required to rebalance the current system and ensure that the interests of issuers and investors are accounted for equally.

Striking this balance is, of course, easier said than done. The myriad of factors incorporated within the continuous disclosure framework makes it difficult to determine what needs to be changed and what is best left. Parliament and regulators should be wary of reactive, ad-hoc changes that are ill-suited to New Zealand's Capital Markets environment and enforcement mechanisms. Equally, they should avoid imitating changes Australia has made based on false conflations between Australia's system and New Zealand's. Although both houses are made from straw, the stability of the enforcement foundations differ and are highly important. New Zealand does not currently face the same threat of overly opportunistic class actions. However, given the seriousness of the threat, the upcoming Law Commission report into class actions should bear it in mind and investigate further the association between continuous disclosure and class actions.

Viewed independently of its enforcement foundations, New Zealand's regime is still in need of reform. I have proposed two recommendations that will help to realign the obligations with its purpose. Firstly, the 'reasonable person' should be defined as a 'reasonable issuer' when establishing 'materiality.' Secondly, "promptly and without delay" should be interpreted as extending to a 24-hour time frame. These changes will ensure that expectations placed on

issuers are reasonable, whilst maintaining sufficient investor protection. Ultimately, the regime will be rebalanced and market integrity will be preserved.

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