The Leading Edge

Staying ahead of regulatory change – insights for general counsel

September 2024

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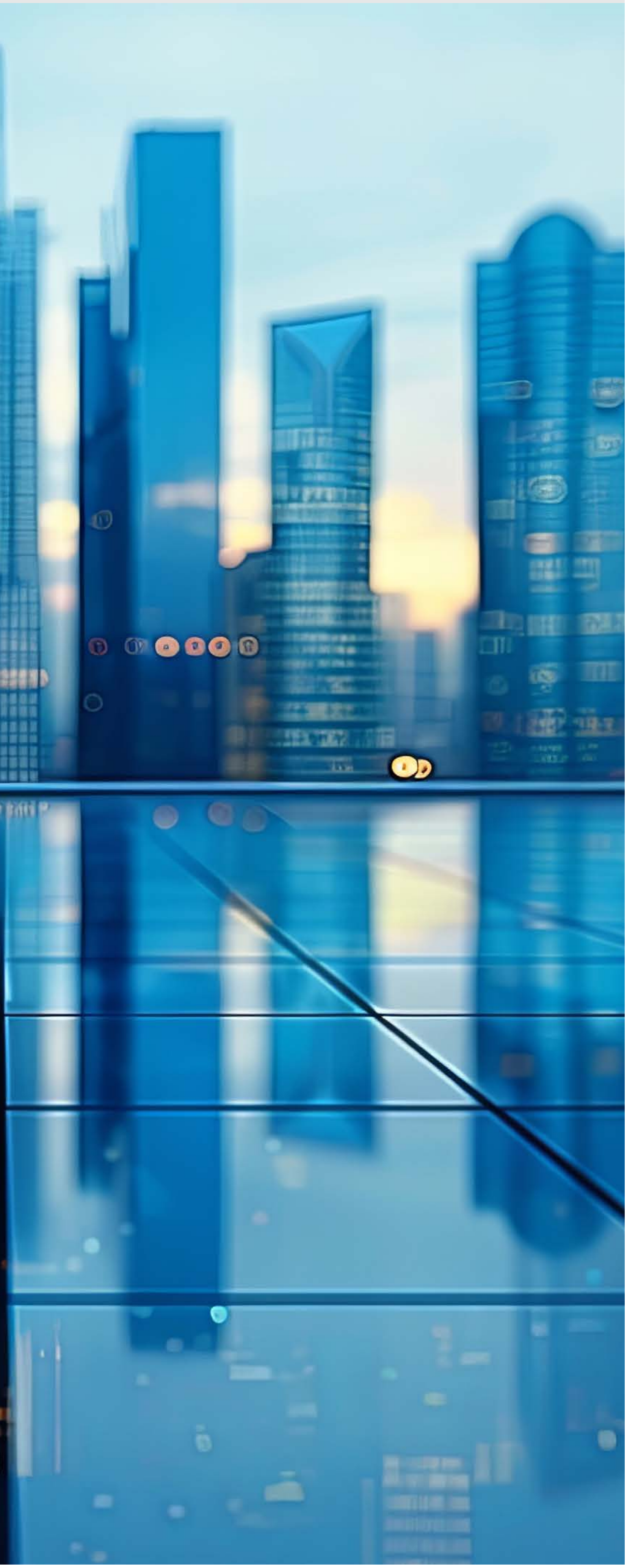


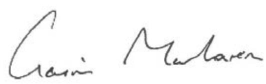
Foreword

Australian policymakers are currently facing difficult headwinds, both domestically and internationally.

At home, cost of living pressures, high energy costs and stagnant economic conditions have created a particularly challenging environment for continued energy transition efforts. Internationally, geopolitical conditions remain fraught, impacting supply chains and keeping global inflation rates stubbornly high. Against this backdrop we have witnessed increased scrutiny by regulators and stakeholders on a variety of issues, including cyber security, merger reform and environmental, social and governance (**ESG**) initiatives.

During times such as these, being alert to the nature and scope of regulatory change is especially important. This collection of articles aims to provide general counsel with relevant insights to keep across such change.

We hope you find it useful.



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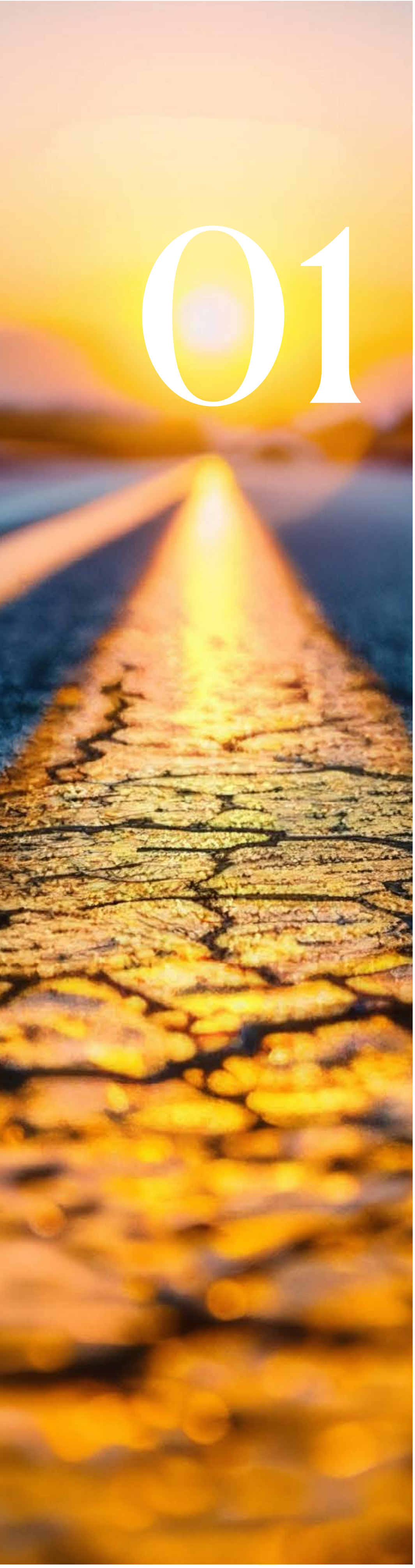
Contents



The rise of value-driven shareholder activism in Australia: a new governance playbook

By **Sandy Mak**, Head of Corporate, **Mark Wilks**, Head of Commercial Litigation, **Katrina Sleiman**, Partner and **Mary Brady**, Special Counsel

Shareholder activism is back – but with a different focus. With return-focused shareholder activism on the rise in Australia, value-based activist investing is set to grow, as it has in the United States, where it has dominated for decades.

This new wave of activism should prompt ASX-listed companies across all industries to pay greater attention to long-term value strategies and prepare to build a new best practice corporate governance playbook for positive shareholder activist engagement.

In recent times, there has been a rise in alternative asset managers that have funds dedicated to unlocking shareholder returns through activism in Australian companies. This form of activism differs from ideology-focused activism, which is primarily environmental, social and governance (**ESG**) focused, such as Grok Venture's vote against AGL's proposed demerger and the raft of climate change activist campaigns against oil and gas companies.

Value-focused activism is also in sharp contrast to the traditional passive investing by Australian institutional investors, who liaise with the board but do not initiate value strategies or agitate for change.

The key players

The recent pivot towards transactional activism or value-focused activism has been steered by a new generation of Australian fund managers that have followed their US counterparts and established funds dedicated to 'private equity style' or 'high conviction' investments. These investments aim to generate shareholder returns by activism, effectively establishing activist investing as an asset class.

The key players offering products in this asset class are:

- Tanarra Capital Long-Term Value Fund
- HMC Capital Partners Fund 1
- L1 Capital Catalyst Fund

There are also more experienced Australian activist funds – such as Sandon Capital and Samuel Terry Asset Management – as well as other fund managers, hedge funds and even superannuation funds that will engage in activism but do not have dedicated activist funds, such as Allan Gray and Aware Super. Investment banks are increasingly providing advice to activists and vulnerable companies alike about value creation opportunities and responses to activist action respectively.

Recent Australian campaigns

In recent years, activist investors have instigated public campaigns directed at improving shareholder returns from ASX-listed companies. Examples include:

- Tanarra Capital's campaign that culminated in the resignation of the incumbent chair and the election of the Tanarra Capital nominee to the board of Healius Limited in November last year;
- several activist investors (including HMC Capital Partners, Allan Gray, Tanarra Capital and Aware Super) advocating for board renewal and strategic change at Lendlease Group;
- L1 Capital Catalyst Fund urging Santos Ltd to split its liquefied natural gas assets;
- Sandon Capital and Samual Terry Asset Management teaming up against Karoon Energy Limited which received its first strike at its last annual general meeting;
- Allan Gray's support of ARN and Anchorage's proposal to acquire Southern Cross Media; and
- Washington H. Soul Pattison's stakebuild in Perpetual to initiate a strategy to realise value in its corporate trustee and wealth management businesses.

Key takeaways for ASX-listed companies

- Monitor your register, be aware of activist funds' strategies and understand the views of your other major shareholders
- Engage advisors early, particularly financial, legal and communications/PR advisers
- Understand your strategy for long-term value and your potential areas of attack
- Focus first on engagement, not defence, but be prepared to defend your position or litigate if necessary
- Build your communication strategy and assign one person to engage who has the expertise and bandwidth to do so
- Be conscious of and seek advice on your directors' duties and be prepared to establish independent board committees to consider the activist's demands, if necessary
- Request confidentiality arrangements wherever possible
- Monitor your continuous disclosure obligations

Activist investor strategy

The strategy of the activist fund is to build a stake initially and then typically (although not always) to approach the board with opportunities. While some approaches are confidential, this is less common where activist funds are involved, as they tend to charge higher fees than passive fund managers, and the ability to publicly demonstrate active engagement with their investee base is part of their investment thesis.

An activist may then also ramp up its campaign by publishing white papers, giving interviews to media sources and engaging with other investors to put more pressure on the board to consider its proposal.

The primary focus areas for unlocking value are:

- capital management;
- strategic and operational issues (such as M&A and disposals);
- executive remuneration (compared against overall performance); and
- board renewal.

A new governance playbook

ASX-listed companies have the opportunity to learn from recent campaigns in Australia and overseas to build a new playbook for positive shareholder activist engagement – one that is focused on understanding the company's strategy to achieve long-term value and respectful engagement (a departure from the ideology of activist defence).

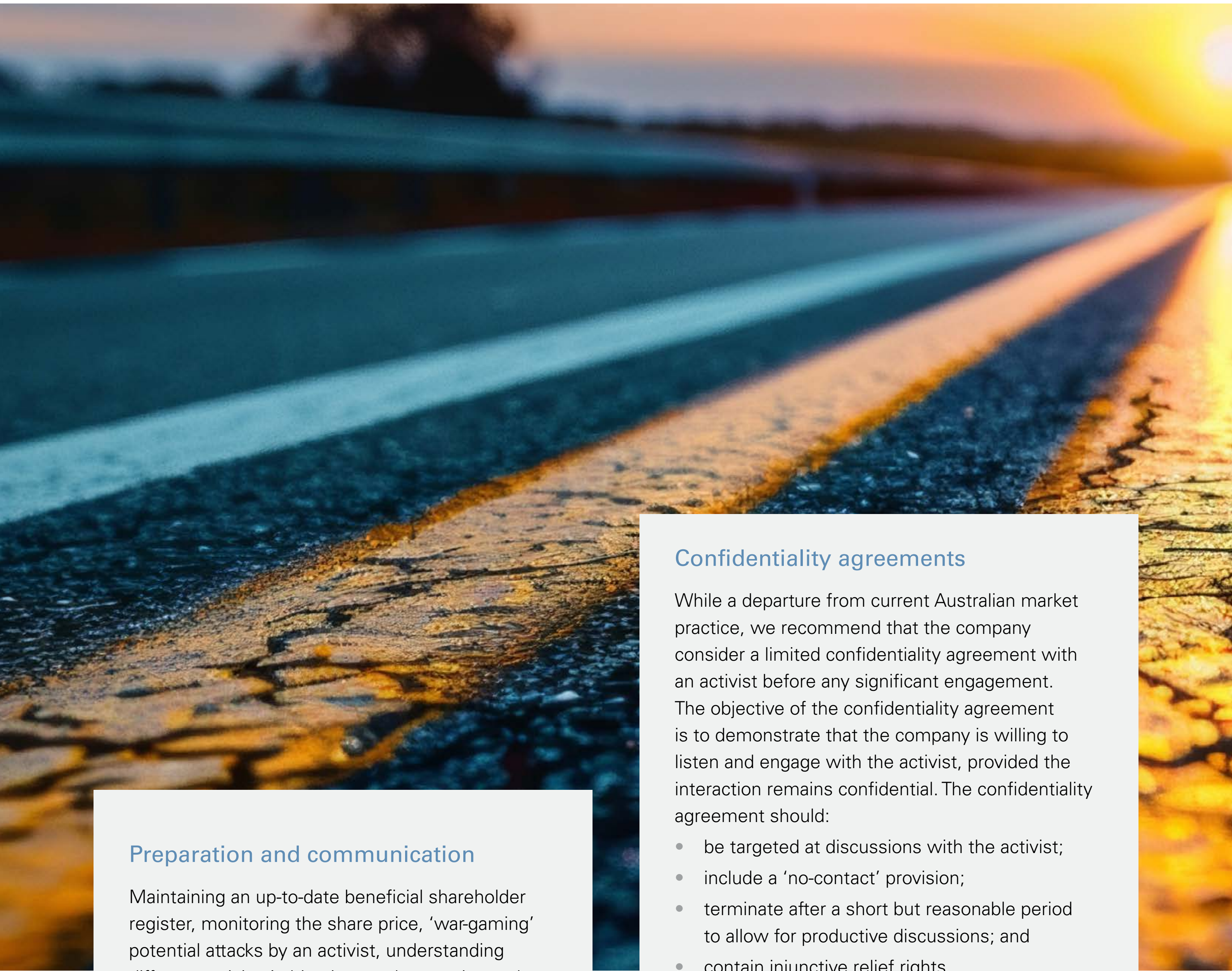
In developing this playbook, the key considerations include:

Directors' duties

Directors have a statutory obligation and fiduciary duty to act in good faith in the best interests of the corporation. While there is conjecture about the perimeter of the 'corporation' in applying this duty, undeniably, the shareholders are key listed company stakeholders and have a fundamental interest in the value of the shares.

In fulfilling directors' duties in the context of an activist proposal, directors should:

- acknowledge that activist funds dedicate significant time and resources to researching the relevant company, its industry and value propositions;
- consider that they have a duty to objectively and carefully evaluate an activist proposal that has the potential to create medium to long-term value;
- be cognisant of potential conflicts of interest, particularly where the stated objective of the activist is board renewal – boards should be prepared to establish an independent board committee which excludes potentially conflicted directors from considering any proposal; and
- apply the same process and perspective in assessing an activist proposal as would be the case for a control transaction.



Preparation and communication

Maintaining an up-to-date beneficial shareholder register, monitoring the share price, 'war-gaming' potential attacks by an activist, understanding different activists' objectives and strategies and being able to articulate the company's long-term value strategy are all key aspects of preparation for a board. We recommend the board pre-emptively engage legal, financial and communications advisors to assist in this preparation process if it considers that it is at risk of an activist campaign. A detailed communication and engagement strategy is also crucial when it comes to managing the relationship with activist investors. The communication strategy should outline:

- potential responses to a variety of different scenarios (taking into account the particular activist's objectives); and
- the process for response, whereby the board should respond with a single voice as much as possible and nominate an individual who is best placed to be the face of the communications.

Confidentiality agreements

While a departure from current Australian market practice, we recommend that the company consider a limited confidentiality agreement with an activist before any significant engagement. The objective of the confidentiality agreement is to demonstrate that the company is willing to listen and engage with the activist, provided the interaction remains confidential. The confidentiality agreement should:

- be targeted at discussions with the activist;
- include a 'no-contact' provision;
- terminate after a short but reasonable period to allow for productive discussions; and
- contain injunctive relief rights.

It is common practice in the US to enter into confidentiality agreements before opening discussions with activist investors. Upfront confidentiality agreements are a fresh approach to activist engagement in Australia and the activist investor may resist, particularly if promotion of its activist activity is part of its strategy. The activist will also likely not want to receive price-sensitive information and the company should not disclose price-sensitive information under this agreement. In our view, however, levelling the playing field between attack and defence by creating a confidential space for the activist investor and company to interact could be a useful tool to encourage constructive engagement. This may ultimately result in a resolution with the activist which does not become public and damage the company.

> Value-focused activism is at an all-time high in Australia and is set to increase.

Continuous disclosure

In a listed environment, continuous disclosure obligations are a major consideration. As always, the company should be aware that:

- the threshold question is whether the information would be considered to have a material impact on the price of the company's securities and a reasonable person would expect the information to be disclosed;
- confidential information and incomplete proposals have the benefit of the exception in Listing Rule 3.1A; and
- once an announcement in relation to the activist investor has been made, the company puts itself in a position of having to provide updates to shareholders, which can be burdensome and can also create share price volatility.

We recommend that the company's continuous disclosure committee stays across all communications with the activist investor and thoroughly consider whether disclosure is required. If in any doubt, the company should also consult its legal advisors given the risk of class action or regulatory action for failure to comply with continuous disclosure obligations.

If all else fails, be prepared to litigate

If engagement with an activist does not produce a constructive outcome, companies should be prepared for the engagement to wind up in the courtroom. Activist strategies which often end up in courtroom battles include board spills, attempts to alter a company's constitution through a general meeting and attempts to access shareholder details or information about the company. Companies should also be prepared to go on the offensive if an activist's strategy involves false, misleading or deceptive statements about the company.

A recent example of this in Australia (at least in a more traditional activist context) is Rural Fund Group's successful challenge to statements made by a US-based activist short seller. Where a company's interaction with an activist does turn sour, directors should also be conscious of constraints on directors' expenditure of corporate funds to defend against the campaign of an activist investor and the need to provide a balanced disclosure to investors.

Value-focused activism is at an all-time high in Australia and is set to increase. However, if the board is prepared and willing to engage, it is possible for the company and the activist to have a constructive relationship, which will also provide the board with additional time to prepare to defend itself if necessary.

A shield and a sword: the increasing importance of investment protection for technology companies

By **Nastasja Suhadolnik**, Head of Arbitration, **James North**, Head of Technology, Media and Telecommunications, **Mark McCowan**, Head of Competition, **Simon Johnson**, Partner and **Oliver Spackman**, Special Counsel

Recent years have seen a trend of increased government scrutiny of the operations of technology, media and telecommunications (**TMT**) companies globally, and a proliferation of regulations in the areas of data protection, cyber security, consumer protection and fair competition, among others.

Given domestic recourse against government regulation may be limited, investment treaties and their investor-state dispute settlement provisions are becoming increasingly relevant for TMT companies as a way to protect their investments and resist real or perceived regulatory mistreatment.

Multinational TMT companies face mounting pressures in the form of regulatory intervention that challenges their business models. Regulatory scrutiny of TMT companies, often driven by public interest imperatives, has taken the form of:

- forced data localisation requirements;
- restrictions on data processing and sharing;
- monitoring and censorship of content;
- disproportionate digital taxation measures and fines;
- compulsory transfers of proprietary information, including source code;
- increased cyber security measures;
- competition or consumer protection action; and
- outright nationalisation of TMT assets and/or operations.

Australia is no exception to this, whether by requiring TMT companies to pay local media for publishing content, investigating the algorithms used by social media platforms, or investigating the risk of foreign interference. These developments have heightened the operational risks for TMT companies operating across multiple jurisdictions.

A recent report by Chatham House and Global Partners Digital, *Towards a global approach to digital platform regulation*, identified a number of common concerns with regulatory regimes targeting TMT companies. These included an absence of independent regulatory enforcement authorities, untailored and undifferentiated regulations, vague definitions of non-compliant behaviour or content, the prevalence of large fines, restrictions and bans for non-compliance, and a risk of harsh punishments for individual employees.

In other words, the implementation of regulations in the TMT sector may be arbitrary, unfair and/or discriminatory. In these circumstances, TMT companies may be protected by rights granted to investors in international investment treaties which provide protection against unfair regulation or other mistreatment by all organs of government performing legislative, regulatory or judicial acts, be it at federal, state or municipal levels.

Investment treaty protection

Investment treaties are multilateral or bilateral agreements between States which protect qualifying investors domiciled in one contracting State when investing in another contracting State (i.e. the host State). For example, the Australia-Singapore investment treaties protect Singapore-domiciled investors in Australia.

Investment treaties impose various legal obligations on host States with respect to the protection of investments made in the State's territory. They prohibit direct or indirect expropriation of foreign investors' assets without prompt, adequate and effective compensation. They also require host States afford 'fair and equitable treatment' to foreign investors and their investments, which typically entails the prohibition of unfair, arbitrary or discriminatory treatment. This includes the introduction of regulatory measures contrary to prior commitments made by the host State at the time of the investment with respect to the basis for, and treatment of, investments.

Additionally, investment treaties commonly prohibit discriminatory or less favourable treatment of foreign investors compared to domestic or other third State investors in like circumstances. Some require the host State to observe contractual undertakings and other obligations or commitments it has assumed towards foreign investors or their investments, which may in some circumstances effectively elevate a host State's duty to comply with contractual obligations to a foreign investor to a duty arising under the investment treaty.

When considering whether assets typically owned by TMT companies are protected investments, it is relevant to note that most investment treaties define investments broadly to include every kind of asset, including intangible assets such as contractual rights, intellectual property, shares in locally incorporated companies, debts and government permits. A TMT company's foreign investment will often involve precisely these types of assets and can therefore benefit from investment treaty protections.

Importantly, investment treaties typically allow investors to enforce their rights by commencing arbitration proceedings against the host State and claiming damages for present and future economic loss flowing from conduct that violates the protections in the treaty. In this way, treaty protections operate extra-contractually and independently of the State's domestic legal systems.

Even if there is no investment treaty between the host State and the foreign investor's ultimate home State, an investor can still obtain protection by structuring its investment through a corporate vehicle incorporated in a third State that does have an investment treaty with the host State – provided this is done at the time of making the investment, or at a later stage but before a dispute is foreseeable. Taking Australia as an example, so long as an investment into Australia came via an entity in the corporate chain which is incorporated in a jurisdiction with which Australia has concluded an investment treaty with arbitration provisions – such as Singapore – the company will benefit from investment treaty protections.

Investment treaty use by technology companies on the rise

Investment treaty planning and protection is an area of untapped potential for TMT companies as they expand their operations internationally because it can be a very efficient tool to resist unfair, discriminatory or otherwise unjust treatment. This is illustrated by a number of high-profile investment treaty claims that have been brought in response to restrictive government regulation, including:

- Uber and Colombia – In 2019, following a nationwide ban of Uber's ridesharing app in Colombia (imposed by the Colombian competition authority following a complaint brought by a local taxi company accusing Uber of failing to meet the requirements to operate in the jurisdiction), Uber issued Colombia with a Notice of Dispute under the US-Columbia Trade Promotion Agreement. An investment treaty arbitration was never formally commenced because Colombia overturned the ban shortly after Uber notified it of the dispute.
- Huawei and Sweden – In 2022, Huawei commenced arbitration under the Sweden-China Bilateral Investment Treaty claiming that Sweden breached the Treaty (and must compensate Huawei) by effectively banning Huawei's 5G network (by disallowing companies bidding to be the network operator for the State's 5G network from using Huawei equipment). Sweden defended its decision on national security concerns. The case is pending.

It is expected that TMT companies will continue to consider investment treaty protections as an opportunity to recover against instances of discriminatory or arbitrary intervention by authorities of the host States in which they operate – be it the national competition authority, telco authorities, or any other regulatory body whose conduct is attributable to the host State.

Advantages of investment treaty protection

Access to investment treaty protection provides numerous potential advantages. Because investment treaty protections operate extra-contractually and independently of the domestic law of a host State, they supplement a company's existing legal rights and the availability of relief under domestic laws in the event of unfair regulatory action.

Further, any dispute is resolved by arbitration before neutral party-appointed decision-makers who are independent of national courts and politics. Also, the ability to commence arbitration proceedings against the host State may operate as a powerful negotiating tool. The potential of an investment arbitration carries significant risks for the host State, including a perception of rising sovereign risk, what is often a very public nature of proceedings and an adverse damages award for which the host State's decision-makers will be answerable to their constituents. It is more likely that the host State will be willing to negotiate with a foreign investor when this avoids the alternative of having to defend a potentially substantial claim under the scrutiny of international and domestic media.

Investment treaties can be a useful shield and sword to protect TMT companies expanding or operating internationally. In the absence of domestic recourse, they provide important protections against abrupt and discriminatory changes to government regulation which companies can enforce by international arbitration before a neutral forum. They can also often be leveraged to reach a negotiated settlement with the host State government before progressing any claims by arbitration.

Climate-related financial disclosures: a new frontier for general counsel

By **Dr Phoebe Wynn-Pope**, Head of Responsible Business and ESG, **Andrew Lumsden**, Partner, **Jo Dodd**, Partner, **Felicity Saxon**, Partner, **Katrina Sleiman**, Partner and **Kate Gill-Herdman**, Special Counsel

Once an issue confined to environmental impacts, climate change is now understood as a systemic risk to the global economy. Decarbonisation is both an environmental and economic imperative, with implications extending far beyond high-emitting sectors and into every facet of commercial activity.

In response, Australia, like many jurisdictions, has introduced a mandatory climate-related financial disclosure regime. This represents a new frontier for general counsel and in-house legal teams, who will have a critical role to play in supporting directors and company officers to discharge their duties and obligations and, ultimately, protect the company from legal risk.

Australia's climate-related financial disclosure regime (**CRFD regime**) will commence on 1 January 2025 by extending the existing financial reporting requirements of the *Corporations Act 2001* (Cth) (**Corporations Act**) to require the preparation of a sustainability report. The CRFD regime is designed to provide investors with the information they need to understand the financial impact of climate change on the companies in which they invest.

Organisations already voluntarily reporting under the Taskforce on Climate Related Financial Disclosures will be able to leverage established processes to respond to the increased granularity and specificity of the CRFD regime's disclosure requirements. TThe CRFD regime also places a considerable burden on directors and company officers as 'gatekeepers,' who have a material obligations burden in relation to the financial management and reporting undertaken by the organisations they lead.

Key disclosure requirements

Under the CRFD regime,[1] reporting entities are required to prepare an annual sustainability report that includes the climate statement for the year, notes to the climate statement and the directors' declaration. The climate statement is required to disclose all of the following:

- any material financial risks (and/or material financial opportunities relating to climate), to be determined in accordance with the relevant sustainability standards;[2]
- any metrics and targets of the entity relating to climate, including scope 1, 2 and 3 greenhouse gas (**GHG**) emissions, and those required to be disclosed by the sustainability standards;
- any information about the entity's governance, strategy and management of risks, opportunities, metrics and targets required to be disclosed by sustainability standards; and
- any notes required by the sustainability standards (or by legislative instrument) in relation to the preparation of, and anything included in, the climate statements (together, the **climate statement disclosures**).

The CRFD regime requires reporting entities to assess and disclose climate resilience against a projected increase in global temperatures of 1.5 degrees Celsius by 2050 and a scenario that 'well exceeds' 2 degrees Celsius by 2050. Scenario analysis is the primary tool by which entities assess their resilience to climate change and identify climate-related risks and opportunities.

There are inherent uncertainties about possible future events and the financial impacts across these timeframes. Accordingly, identifying the financial materiality of climate-related risks and opportunities to the entity's prospects requires the formulation of assumptions and exercise of judgment about what risks and opportunities are (or may become) financially material over extended timeframes based on different scenarios.

Directors' declarations as to compliance with the CRFD regime

Presently, in the context of financial reporting, the law requires directors to:

- question the information provided to them;
- have a reasonable level of financial literacy and basic accounting knowledge;
- ensure the executive team has systems, protocols and controls in place to ensure sound corporate governance; and
- individually adopt the annual financial statements and not completely delegate their review and consideration of the financial statements.

For the first three years of the CRFD regime, an entity's climate statement must include a declaration that, in the directors' opinion, the entity has taken reasonable steps to ensure the climate statement and notes of the sustainability report are in accordance with the Corporations Act (**reasonable steps declaration**).

The close relationship between directors' existing obligations to exercise care and diligence in their consideration and approval of the financial statements and the new reasonable steps obligations in relation to climate statement disclosures set out in the CRFD regime means directors should have regard to the content of their existing obligations when considering how to discharge their new responsibilities.

1 Reporting entities include (i) companies, registered schemes, registered superannuation entities and disclosing entities that meet two of the three criteria – equal to or greater than 100 employees and/or value of consolidated gross assets of that entity and the entities it controls is greater than A$25 million and/or consolidated revenue for the financial year of the entity and the entity it controls is greater than A$50 million; (ii) entities who report under the *National Greenhouse and Energy Reporting Act 2007* (Cth); and (iii) entities where the value of its assets (and the entities it controls) is equal to or greater than A$5 billion.

2 Information is material if omitting, misstating or obscuring that information could reasonably be expected to influence the decisions that primary users of general purpose financial reports make on the basis of financial statements and any climate-related financial disclosures. For example, in *Australian Securities and Investments Commission v Healey* [2011] FCA 717 (Centro), Centro's 2007 accounts, approved by the directors, failed to reveal that the shopping centre giant had approximately A$2 billion in current liabilities. Another A$1.75 billion in guarantees was not disclosed.

Three years after the commencement of the CRFD regime, directors will need to make a declaration as to whether, in the directors' opinion, the substantive provisions of the sustainability report are in accordance with the Corporations Act, including compliance with sustainability standards and climate statement disclosures (**directors' declaration of compliance**). The same liability provisions apply to both forms of declaration, including liability for false or misleading statements and misleading or deceptive conduct, as well as representations as to future matters not made on reasonable grounds.

Declarations in the absence of reasonable assurance

The requirement for external assurance (**Audit**) will be gradually phased in from the commencement of the CRFD regime through to 2030. The Australian Assurance Standards Board has proposed further consultation on the requirement for limited assurance of certain disclosures for the first three reporting years. Audit assurance is not proposed until the fourth reporting year, except for scope 1 and 2 GHG emissions which will be proposed from the second reporting year.

Should these proposals be adopted, for a period of time, directors and corporate officers will be required to make declarations outside the audit assurance process as to the most complex aspects of climate disclosures, including scenario analysis and assessment of an entity's climate resilience, transition plans and scope 3 GHG emissions.

In the absence of an audit to test the assumptions made by directors and management in the preparation of their reports, general users of financial reports will be reliant on the adequacy of a reporting entity's systems, processes, controls and resources to discharge the entity's disclosure obligations and understand the financial impact of climate risks and opportunities on the entity's prospects. They may also place greater reliance on declarations given by directors as to the entity's compliance with the disclosure requirements and underlying climate standards.

This heightened focus on the directors' declaration exposes directors and corporate officers to greater reputational and legal risks.

Elevated risks despite transitional relief

Climate statement disclosures will ultimately be subject to the same liability provisions that apply to reporting entities and their directors for the preparation of annual reports. However, the CRFD regime will provide some limited transitional relief from liability, including a three-year period of immunity from private litigants for higher risk statements made in the sustainability report such as disclosures about scope 3 GHG emissions, scenario analysis or transition plans.

However, this relief is limited in both scope and duration. There is no immunity from Australian Securities and Investments Commission (**ASIC**) enforcement action. Immunity for forward-looking statements expires after one year unless those statements are about scope 3 GHG emissions, scenario analysis or an entity's transition plan made in the sustainability report. All immunity expires after three years.

Importantly, the limited relief provisions are confined to the sustainability report and **do not** apply to:

- the directors' obligations to ensure that the reasonable steps declaration is not misleading;
- accounting for the financial impact of climate risks and opportunities in the financial statements e.g. adjustments to asset values or contingent liabilities in relation to environmental remediation obligations;
- the requirement in s295 of the Corporations Act for directors to give a declaration as to the financial position of the entity; or
- the requirement in s295A of the Corporations Act for a listed entity's chief executive officer and chief financial officer to give a declaration about the listed entity's financial statements.

> “In-house legal teams should plan for the CRFD regime's natural extension to nature-related financial risks.

'Reasonable steps' in the face of uncertainty

In the absence of a statutory definition of 'reasonable steps' and case law considering 'reasonable steps' in the context of climate disclosures, reporting entities will need to be guided by the courts' treatment of 'reasonable steps' more generally. What might constitute 'reasonable steps' is largely an objective test which is highly fact-dependent and will differ depending on the entity, complexity of the entity's business and the internal reporting procedures within the business.

In *Centro*, 'reasonable steps' was defined as a standard determined by reference to the particular circumstances that oblige the directors to take a sufficient interest in the material available to them (or that they might appropriately demand from executives or agents). This case also highlighted the close relationship between a director's more general duties to the corporation and the specific statutory requirements associated with the adoption of financial statements.

Directors and the executive team that supports them need to carefully consider the level of climate literacy needed to discharge their obligations having regard to:

- the complexity of the entity's business model and corporate structure;
- its operating environment; and
- the nature of the information directors require to enable them to provide those declarations.

To enable them to test the assumptions and judgments underpinning the entity's disclosures, directors and executive teams also need to understand the sources of physical and transition risks of climate change and how those risks are likely to affect the entity. They need to use that knowledge to be satisfied that the entity's policies, processes and procedures for assessing the financial materiality of climate risks and opportunities and making sure the climate statement disclosures are robust and defensible. 'Reasonable steps' may also include underlying data collection, retention and management processes and the engagement of external expertise to supplement internal capabilities.

The role of general counsel

General counsel have long been considered officers of the company with a duty to protect it from legal risk. In the context of climate disclosures, this includes:

- promoting corporate compliance with the CRFD regime's requirements (both substantive and administrative);
- promoting compliance with prohibitions on misleading conduct and ensuring the board of directors is properly informed of matters that create or increase a risk that would put them in breach of their legal obligations; and
- protecting against litigation risk.

Accordingly, in-house legal teams have an important role to play in ensuring management and the board understand the entity's disclosure obligations and whether the entity's compliance framework is sufficient to meet those obligations so as to enable corporate officeholders to discharge their duties and responsibilities.

In-house legal teams will also play a crucial role in helping to ensure corporate officeholders understand the legal risks (including those arising from harm to the entity's reputation) arising from compliant climate disclosures that reveal potential inadequacies in the governance, strategy or management of climate risks and opportunities.

With the Federal Government and ASIC expanding their focus to nature-related financial risks, in-house legal teams should plan for the CRFD regime's natural extension to nature-related financial risks.

As ASIC Chair Joe Longo told audience members earlier this year, entities should "ensure that any systems and processes they adopt for the purpose of climate-related financial disclosures be sufficiently agile to incorporate additional sustainability topics in future years."

Digital resilience and the CrowdStrike outage: key considerations for business

By **James North**, Head of Technology, Media and Telecommunications, **Mark Wilks**, Head of Commercial Litigation, **Chris Pagent**, Head of Class Actions and **Angelina Yurlova**, Senior Associate

On 19 July 2024, a bug in a software update deployed by endpoint protection and cyber-attack detection company CrowdStrike triggered a global IT outage, the scale of which was unprecedented. In Australia, the outage hit during a workday, with business leaders suggesting the financial impact topped A$1 billion.

While recovering financial losses was front of mind for many businesses in the immediate aftermath of the incident, it is the longer-term, ongoing implications of the outage that now beg closer attention from boards and executives, including the likelihood of increased scrutiny and oversight from both governments and regulators.

Currently, there is no one specific regulator of the IT industry in Australia as there is for other industries. IT vendors such as CrowdStrike must comply with generally applicable legislation, including the Australian Consumer Law (**ACL**) and the *Privacy Act 1988* (Cth) (**Privacy Act**), but do not have sector-specific regulatory oversight.

For the Australian Government, cyber security has been a major priority, with the release of the 2023-2030 Australian Cyber Security Strategy late last year. The Government's Security of Critical Infrastructure Act aims to protect businesses in outages caused by cyber incidents but it does not apply to general IT outages, despite the impact the CrowdStrike outage had on Australia's critical infrastructure.

Boards and executives should be keenly aware of any third-party systems that have the potential to impact on their business operations. Some industries are required to assess the risks posed by third-party technology vendors, including from a business continuity perspective. For example, the Australian Prudential Regulation Authority's (APRA) CPS 230, which applies to APRA-regulated entities such as banks and insurers, requires that such entities:

- establish and maintain robust risk management frameworks;
- enhance board governance, accountability and oversight;
- assess and mitigate operational risks;
- develop effective business continuity management strategies; and
- strengthen arrangements with service providers.

CPS 230 will come into effect on 1 July 2025 and will replace five current APRA standards on outsourcing and business continuity management. In the wake of the CrowdStrike outage, ensuring that APRA-regulated entities address vulnerabilities in their management of operational risk such as the increasing reliance on service providers, ineffective software development controls and low disruption tolerance will no doubt be a key priority for regulators such as APRA.

Now that we've seen the impact that such vulnerabilities can have on the global economy, governments and regulators are likely to step up – with additional scrutiny on digital resilience being the logical next step. There have already been calls at the Federal Government level to ensure the resilience of digital technologies in Australia, with Shadow Digital Economy Minister Paul Fletcher calling for stronger and more confident regulation of the technology sector. Following the recent Optus mobile network outage, Minister for Communications The Hon Michelle Rowland MP has directed the Australian Communications and Media Authority to make enforceable industry standards to improve how telecommunications companies communicate with customers during major outages. While the directive is limited to telecommunications companies, this step demonstrates the Federal Government's commitment to improving the digital resilience of the Australian economy.

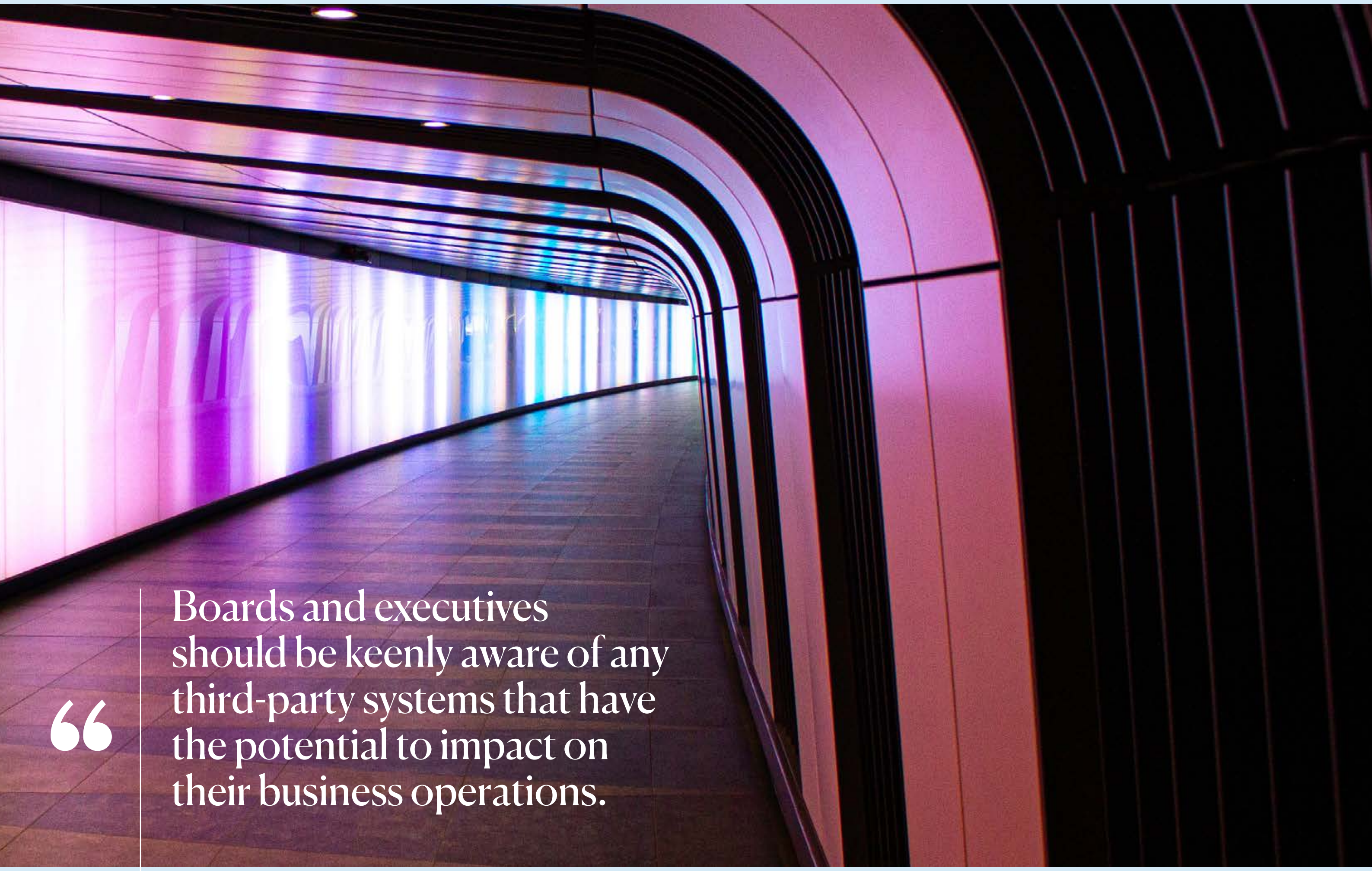
Outside of Australia, however, there is no precedent for regulating digital resilience beyond the financial sector. Similarly to CPS 230, the European Union's Digital Operational Resilience Act will aim to ensure the 'operational resilience' of banks and insurance companies and their information and communications technology service providers from January 2025.

Broader regulation of digital resilience therefore seems unlikely at this stage and, in our view, digital resilience is a subject matter that is best dealt with through prudent technology governance by appropriately skilled and well-advised boards and executives.

Ongoing digital resilience considerations for businesses

To ensure digital resilience and mitigate the risks posed by future IT outages in the longer term, businesses should carefully consider the following:

1. **Agreements with technology vendors.** For businesses reconsidering their contract terms going forward, it is unlikely that IT vendors will change their standard form liability positions. All businesses need to strike a reasonable balance between risk and reward for any given customer relationship. An IT vendor is unlikely to underwrite unlimited trading losses in return for



> Boards and executives should be keenly aware of any third-party systems that have the potential to impact on their business operations.

a relatively modest subscription fee from a small customer. However, large government and corporate users may have the bargaining power to negotiate more favourable risk positions in contracts. Customers with a more modest spend may have the benefit of the statutory consumer guarantees under the ACL, which apply regardless of an IT vendor's standard terms and can benefit businesses as well as individual consumers. Smaller customers may also have the benefit of the unfair contract terms regime, which applies under the ACL to standard form contracts where small businesses meet certain thresholds.

2. **Technology governance.** The CrowdStrike outage was caused by a coding update that went wrong, and highlights the dangers of poor IT and cyber security practices. Businesses are becoming focused on pushing out updates faster, particularly to address dynamic cyber threats, and reducing IT costs. It is also becoming increasingly common to use artificial intelligence to write software code. If businesses do not adopt safe coding practices, including proper software testing and phased rollouts, we may see more CrowdStrike-type outages in the future. Businesses should invest in sound technology governance that includes data redundancy measures and manual workarounds to ensure that the operational impacts of IT outages are mitigated.
3. **Insurance arrangements.** Businesses should also consider their insurance position, looking at whether their policies could cover loss arising from IT systems outages more generally – either through cyber insurance or business interruption insurance.
4. **Class actions.** CrowdStrike customers are required to agree to New York governing law and arbitration in Singapore. This largely foregoes access to Australian courts in the pursuit of legal remedies. By virtue of these arbitration clauses being embedded in the standard customer terms, a class action is likely to be challenging. Should CrowdStrike seek to enforce those agreements, any proceedings brought in Australia will be the subject of an application for a stay and for the parties to be referred to arbitration on an individual basis.

Regardless of their size, all businesses should undertake a holistic risk assessment of their technology environment. This includes:

- identifying which systems are likely to have a significant impact if affected by an outage;
- negotiating contract terms where possible to improve liability positions; and
- building redundancy into operations, processes and systems.

05

The ongoing merger reform debate: where is it likely to land?

By **Mark McCowan**, Head of Competition, **Ian Reynolds**, Partner and **Lara Hall**, Partner

Earlier this year, the Federal Government announced sweeping reforms to Australia's merger rules.

The proposed reforms will introduce a mandatory and suspensory merger control regime in Australia. In an apparent attempt to give the business community clarity and confidence about filing requirements and timelines, the proposed law is highly detailed and prescriptive.

The Australian Competition and Consumer Commission (**ACCC**) has also been at pains to emphasise that it envisages clearing the vast majority of deals on a proposed expedited timeline. However, too much discretion to extend review timelines is given to the ACCC and the new regime seems likely to capture many more deals, involve generally longer reviews on average for all but the simplest deals, and substantially increase the upfront process complexity of seeking ACCC clearance.

More substantially, there remain real concerns about the extent to which the ACCC's decision-making under the new process will be insulated from thorough and effective judicial review. Finally, administering the new regime effectively will require a substantial increase in ACCC resources and, perhaps just as importantly, cultural change.

Overview of proposed changes

Treasury released exposure draft materials on 24 July 2024, which are likely to be further revised before implementation. In brief, the exposure drafts propose that:

- On 1 January 2026, a new mandatory and suspensory merger control regime will commence.
- Acquisitions of shares or assets that meet prescribed monetary or market concentration thresholds will require notification.
- The combined effect of all acquisitions within the previous three years by all parties will be aggregated to determine if notification thresholds are met and can be considered as part of a review.
- Significant penalties will apply for failure to comply with the requirements to notify and suspend completion, and for providing false or misleading information.
- Indicative timeframes of 30 working days and 90 working days for 'Phase I' and 'Phase II' reviews respectively, and fast-track determinations after 15 working days will be introduced. If the ACCC does not make a determination in those time periods, a transaction is cleared.
- The ACCC may permit an acquisition that would be likely to substantially lessen competition if it would be likely to result in a net public benefit that would substantially outweigh that lessening of competition after a 'Phase III' review (50 working days).
- Review by the Australian Competition Tribunal will be available, based only on the information before the ACCC – 90 calendar days (extendable by 90 calendar days). 'Fast-track' review (60 calendar days) may be sought.

Legislative proposals are unclear and incomplete

A number of features of the drafts would undermine the main benefit of a mandatory regime – increased certainty – and the regime as drafted would be problematic in practice.

Monetary thresholds

It is proposed that transactions will require notification if they meet either of the following monetary thresholds (and there is a 'material connection' to Australia):

- If the combined Australian turnover of the merger parties (including the acquirer group) is greater than A$200 million, and either the Australian turnover of at least two merger parties is greater than A$40 million **or** the global transaction value is greater than A$200 million.
- If the acquirer group's Australian turnover is greater than A$500 million, and either the Australian turnover of at least two merger parties is greater than A$10 million **or** the global transaction value is greater than A$50 million.

The circumstances in which a target business or asset has a material connection to Australia would include where it is registered or located in Australia, supplies goods or services to Australian customers, or generates revenue in Australia.

All acquisitions by an acquirer and its corporate group within the previous three years in relation to the same product or service market/s (irrespective of geographic location) would be aggregated for the purposes of assessing whether an acquisition meets the turnover threshold, regardless of whether those acquisitions themselves would have individually required notification.

Market concentration thresholds

It is also proposed that transactions will require notification if they meet either of the following market concentration thresholds:

- A share of 25% of any 'affected' or 'adjacent' market, where Australian turnover of at least two of the merger parties (including the acquirer group) is greater than A$20 million.
- A share of 50% of any 'affected' or 'adjacent' market, with a lower turnover requirement of greater than A$10 million.

Treasury's proposal appears to be that the **bare acquisition** of a greater than 25% or 50% market position would require notification and that no **increment to** an existing market position would be required. That seems to be designed to capture both horizontal overlaps in merger parties' products or services (i.e. overlaps at the same level of the supply chain), and vertical or conglomerate acquisitions where merger parties have moderate to large positions in 'adjacent' markets.

Treasury's objective is "to ensure the ACCC is informed of mergers most likely to be anti-competitive, while minimising the overall compliance burden on businesses". However, our initial view is that the monetary thresholds are likely to over-capture transactions for review and the market concentration thresholds will be challenging to apply in practice, leading to conservative over-reporting from merger parties.

Treasury estimates that between 300-500 acquisitions would be caught each year. 500 reviewable mergers annually is substantially more than previously estimated, but in our view is likely still understated. It would represent a 52% increase in the ten-year average, and the extra administrative burden on the ACCC and parties will likely result in substantial delays. It will be critical for the ACCC to provide greater detail about how the jurisdictional nexus test would apply, including the amounts of goods or services supplied to Australian customers or revenues generated in Australia that will indicate a 'material connection' to Australia.

While there are a small number of regimes that use market concentration thresholds, they are challenging to apply if they are based on 'share of supply' rather than principled and conventional market definition principles. 'Share of supply' is a substantially broader and more fluid concept that in the United Kingdom can include the numbers of workers employed or even intellectual property rights held. If market share is to be used, it will be critical to develop a significant bank of ACCC precedent on market definitions in a variety of industries, which will take time.

Treasury has proposed that the ACCC would be able to grant parties a 'notification waiver' within 30 business days if there is uncertainty as to whether the notification thresholds are met. However, the notification waiver regime is unwieldy and uncertain – it will take almost as long as a first-phase decision on notification to obtain a waiver and there is no clarity as to how the ACCC will exercise its discretion to grant a waiver.

Further, proposed 'high-risk' acquisitions would require notification based on separate, sector-specific notification requirements. This raises the prospect of multiple layers of thresholds for parties to consider and further uncertainty.

Control test

Only acquisitions of 'control' will require notification. There will be a rebuttable presumption that acquisitions of more than 20% of the voting power of a target will confer control, but control may be inferred from "any practice or pattern of behaviour affecting the policies" of a target. This is concerningly broad and is inconsistent with comparable control tests in overseas jurisdictions and the *Corporations Act 2001* (Cth), which refers to practical control over financial or operating policies and not broader 'patterns' or 'behaviours'.

> Due to the mandatory nature of the regime, the breadth of the control test, and the substantial penalties for getting it wrong, it is inevitable that parties will take cautious positions.

Too much procedural discretion to the ACCC

Statutory timelines provide some procedural certainty and discipline. However, significant uncertainties remain:

- The ACCC will have a 'reasonable period' to confirm that a notification, with stringent information requirements, is complete before starting a review. That is out-of-step with other jurisdictions' tight timeframes to determine application validity. While the ACCC reasonably needs to be satisfied that an application is in an acceptable form before commencing a review, a broad discretion as to when a review is able to commence will simply allow the ACCC to extend pre-notification consultation periods to alleviate pressure created by statutory review timelines. The ACCC will consult on the notification form and procedure further in 2025. Until then, we cannot gauge how difficult, involved or lengthy pre-notification discussions with the ACCC as to complete notifications will be. Overseas experience suggests multi-month processes with multiple drafts.
- The ACCC has significant discretion to control the timing of reviews. There are multiple options for the ACCC to extend reviews, including by issuing requests for information, if 'material' (rather than substantial or competitively significant) changes in facts occur, or if the ACCC delays providing certain analytical material to parties. The flexibility in the process is heavily and disproportionately weighted in favour of the ACCC.

- The ACCC's current practice is to deal with between 80-90% of transactions in a confidential pre-assessment period (of around 3-6 weeks). It is likely that the significant majority of notifications under the new regime will be similarly unproblematic and could be 'fast-tracked', but there is no clarity as to how the ACCC will exercise its discretion to make a decision within the 15-working day fast-track determination process. Any transaction that does not result in a material market share increment should be 'fast-tracked' and subject to much more limited information requirements (which is the position in the European Union). That would focus and shorten pre-notification discussions.

Review rights

On an application for review, the Australian Competition Tribunal can only consider information before the ACCC and new information not in existence during the ACCC's review. This limitation substantially constrains the scope of appeal rights under the new regime, particularly in circumstances where the parties may not have full access to all information that is before the ACCC during the review. Parties should be permitted to file new evidence if its importance only becomes apparent on review of the ACCC's determination and there should be effective 'access to file' provisions to permit parties to comprehensively review all information before the ACCC (as there is in the European Union).

Without explanation, the threshold for obtaining a clearance based on net public benefits has been increased. 'Phase III' approval can only be obtained if a net public benefit **substantially** outweighs any public detriment. The current test requires public benefits to simply **outweigh** public detriments. This change would appear to jettison a broad range of merger and non-merger authorisation precedent, increasing uncertainty and permitting the ACCC yet more discretion.

Changes in substantive assessment

The current 'substantial lessening of competition' test is proposed to be expanded via the addition of the words 'creates, strengthens, or entrenches substantial market power'. That expansion of a long-established and well-understood definition is also intended to apply to other provisions of the *Competition and Consumer Act 2010* that utilise the same test, including the prohibitions on misuse of market power and anticompetitive agreements. It is unclear how that change will apply in practice. This proposed change would call into question whether businesses in leading market positions can engage in competitive conduct (including conduct in which their smaller rivals engage) that may enhance their market position, even to a degree that is not necessarily substantial or meaningful to the competitive process. This needs further thought before adoption and should be fully consulted on.

Transitional arrangements

The new regime commences on 1 January 2026. Provision is made for parties to voluntarily notify under the new rules from 1 December 2025. No provision appears to have been made for transactions notified under the current informal regime where the ACCC has not made a decision by 31 December 2025. Requiring parties to re-apply or engage in parallel processes would be impractical as different tests would apply, and this should be urgently clarified.

What next?

Due to the mandatory nature of the regime, the breadth of the control test, and the substantial penalties for getting it wrong (including multi-million-dollar penalties), it is inevitable that parties will take cautious positions. As a result, more acquisitions will be subject to notification, suspension and ACCC conditions even if they raise no or limited competition concerns.

In the interim, it will be important for the business community to continue to advocate for sensibly set notification thresholds, clearer definitions of what types of transactions are required to be notified, transparency as to timing, and effective and practical due process and review.

Unravelling complexity: navigating Australia's sanctions landscape

By **Nastasja Suhadolnik**, Head of Arbitration, **Joshua Aird**, Senior Associate and **Eleanor Clifford**, Associate

Australian businesses have been navigating sanctions laws for many years, often as part of broader compliance programs to address anti-money laundering (**AML**) and counter-terrorism financing (**CTF**) provisions. However, the recent escalation of global conflicts and matters of international peace and security have prompted a heightened focus on sanctions compliance.

Sanctions pose restrictions on a range of business activities and can be confusing, time-consuming and costly to navigate. But in this rapidly evolving area, businesses need to take steps to ensure their compliance programs are sufficient to respond to both current and new measures under Australia's sanctions legislation.

Australia operates two sanctions regimes:

United Nations Security Council sanctions

These are sanctions adopted by the United Nations (**UN**) Security Council which Australia, as a UN Member State, is required to implement under domestic law under the *Charter of the United Nations Act 1945* (Cth) (**UN Charter Act**) and associated regulations.

These sanctions are generally implemented on a geographic basis but also include global counter-terrorism sanctions.

Autonomous sanctions

These are sanctions that Australia independently adopts and implements as a matter of policy under the *Autonomous Sanctions Act 2011* (Cth) (**ASA**) and its associated regulations.

This includes Australia's Magnitsky-style thematic sanctions which are not geographically defined or limited.

With limited exceptions, all Australian individuals, bodies corporate and any legal person conducting business in Australia must comply with Australia's sanctions regimes.

UNITED NATIONS SECURITY COUNCIL SANCTIONS

Central African Republic
Counter-terrorism
Democratic Republic of the Congo
Guinea-Bissau
Iraq
ISIL (Da'esh) and Al-Qaida
Lebanon
Somalia
South Sudan
Sudan
The Taliban
Yemen

BOTH

Democratic People's Republic of Korea
Iran
Libya
Syria

AUSTRALIAN AUTONOMOUS SANCTIONS

Former Federal Republic of Yugoslavia
Myanmar
Russia/Ukraine
Zimbabwe

Thematic

Proliferation of weapons of mass destruction
Serious corruption
Serious violations or serious abuses of human rights
Significant cyber incidents

Adapted from the Department of Foreign Affairs and Trade

The escalation of the Israel-Palestine and Russia-Ukraine conflicts, as well as increasing geopolitical tensions, human rights violations and cyber security incidents have resulted in significant expansion of Australian sanctions. As at 29 August 2024, almost 8,000 individuals and entities are subject to sanctions under Australian law.

The nature of sanctions being imposed by the Australian Government is also expanding. While Australia's autonomous sanctions have traditionally been country-based, late 2021 saw the introduction of the Magnitsky-style sanctions regime. The Magnitsky-style sanctions are thematic and facilitate targeted sanctions against individuals responsible for, or complicit in, serious violations or serious abuses of human rights, significant cyber incidents, serious corruption and the proliferation of weapons of mass destruction.

Since its introduction, the Magnitsky-style sanctions regime has been used to sanction individuals complicit in corruption, political and military figures involved in human rights violations and cybercriminals.

This expansion in the number and nature of sanctions poses real risks to business. Organisations must understand the ambit of proscribed activity and keep their screening lists up to date to ensure new designations are covered by existing sanctions screening processes. The introduction of thematic sanctions requires compliance teams to look beyond red-flag countries and regions when assessing possible risks. This is particularly important for high-risk businesses, including those in export services, defence, industrial agriculture, energy and natural resources, and with foreign ownership or entities within their operational structure.

Recent Federal Court cases

Recent cases before the Federal Court have shed light on the complex and challenging area of regulation and compliance that is Australia's sanctions regimes.

All offences under the UN Charter Act and ASA are strict liability, meaning that contravention does not require a state of mind (such as intent, knowledge or recklessness) to satisfy the commission of an offence. An individual or body corporate commits an offence if it engages in conduct that contravenes a sanctions law, or a condition of an authorisation made under a sanctions law.

Contravening conduct broadly includes:

- **Sanctioned supply.** Supplying, selling or transferring sanctioned goods which (as a direct or indirect result) end up in the relevant sanctioned country, or for the use or benefit of that country or a sanctioned individual.
- **Sanctioned import.** Importing, purchasing or transporting sanctioned goods.
- **Sanctioned service.** Providing technical, financial or other services if the service assists with the above conduct, or other specified service.
- **Sanctioned commercial activity.** Engaging in sanctioned commercial activities, which can include acquisitions of interests, establishing joint ventures or granting loans to sanctioned individuals or entities, as well as engaging in particular commercial activities in respect of sanctioned countries.
- **Controlled assets.** Using or dealing with a controlled asset (owned by a sanctioned entity or individual) or allowing or facilitating this use or dealing.

It is also an offence to give false or misleading information in connection with the administration of a sanctions law.

The goods, services, commercial activities and entities or individuals that are the subject of sanctions is constantly evolving. The ASA was amended as recently as April 2024 to provide that persons or entities can be validly designated as being subject to sanctions based on past conduct or with respect to past circumstances. Businesses in high-risk industries must be alert to changes to Australia's sanction regimes.

The cases of *Alumina and Bauxite Company Ltd v Queensland Alumina Ltd* [2024] FCA 43 (**Alumina Case**) and *Tigers Realm Coal Limited v Commonwealth of Australia* [2024] FCA 340 (**Tigers Realm Case**) clarified the scope of the contravening conduct, suggesting an expanding application of Australia's sanctions regimes. In particular, O'Bryan J in the Alumina Case held that:

- The meaning of 'sanctioned supply' of 'export sanctioned goods' is to be broadly construed to include sale transactions, the transfer of title to goods, the physical delivery of goods and simply furnishing or providing the goods.
- The terms 'direct or indirect', used in the context of regulating sanctioned supply and determining whether an asset has been made available for the benefit of a designated person, are to be broadly construed. 'Indirect' is taken to mean making an asset available, including through an intermediary, agent, interposed corporate entities or via an indirect financial interest, and to encompass 'any number of degrees of remoteness of causation'.

In the Tigers Realm Case, Kennett J similarly applied a broad interpretation, noting that sanctioned exports are designed to encompass the transfer of goods 'for the benefit of' the identified country, which 'reflects a deliberate decision to extend the concept of a "sanctioned supply" beyond the physical transfer of goods into the designated country'.

The interpretation of indirectly engaging in sanctioned conduct raises the possibility of capturing entities further down an organisation's supply chain than perhaps previously considered. This interpretation, coupled with the attribution of responsibility to body corporates for the conduct of entities within their effective control under the ASA, means that Australian businesses with extraterritorial exposure within their operations, structure or business relationships should err on the side of caution. They should consider that any conduct which may fall under the scope of Australia's sanctions regimes will create material risks to their operations.

Key components of an effective sanctions compliance regime

The Australian sanctions regimes provide for limited defences. Most relevantly, bodies corporate may avail themselves of a defence if they can prove that they took reasonable precautions and exercised due diligence to avoid the contravention.

Australian businesses should ensure that their compliance systems are sufficient to support a robust defence that the company implemented 'reasonable precautions and exercised due diligence' to avoid any contravening conduct. This defence may be necessary to avoid significant monetary penalties of the greater of three times the value of the contravening transaction (if able to be determined) or 10,000 penalty units (A$3,130,000 as at 1 July 2023).[1]

While any sanctions compliance regime will be proportionate to the organisation's operational circumstances, including its sanctions risks and the nature of its activities, key components of a reasonable and effective compliance regime include:

- **Risk assessments.** A sanctions risk assessment should form part of a broader risk assessment of your business relationships. A sanctions risk assessment will need to consider sanctions risks (e.g. high-risk jurisdictions and high-risk sectors) and common sanctions red flags (e.g. prior sanctions breaches or government ownership).

1 The *Crimes and Other Legislation Amendment (Omnibus No. 1) Bill 2024*, which proposes to amend the value of a penalty unit from $313 to $330, is currently before Parliament.

- **Due diligence.** A thorough due diligence and screening process should be conducted before entering into a business relationship and continue throughout the relationship. The level of due diligence should be proportionate to the risks connected to the particular relationship or circumstances of that relationship (e.g. business relationships that are assessed at a higher risk should undergo more intense due diligence processes throughout the relationship).
- **Controls.** Businesses should implement a range of controls (proportionate to the risk) which could include training, adoption of screening tools, alerts for new or additional sanctions and external audits.
- **Review.** Sanctions compliance regimes should be regularly reviewed to assess their effectiveness and updates should be undertaken as required.
- **Culture and governance.** As with other compliance issues, sanctions compliance should be backed up by a robust compliance culture and tone from the top.

Recent sanctions law developments provide an opportunity for organisations to assess whether their sanctions compliance systems are fit for purpose and whether advice should be sought to minimise the risk of contravention of what are increasingly complex regimes.

The Australian (and international) sanctions landscape will not simplify anytime soon, and as a result, Australian businesses need to consider how they can leverage their internal and external resources to safeguard business opportunities while also positioning themselves for future-proof sanctions compliance.

> Recent sanctions law developments provide an opportunity for organisations to assess whether their sanctions compliance systems are fit for purpose.

Considering the impact of Australia's net zero reform agenda on property and infrastructure project delivery

By **Dr Louise Camenzuli**, Head of Environment and Planning, **Kirsty Davis**, Partner, **Paul Carrick**, Head of Real Estate, **Matthew Muir**, Deputy Head of Projects, **Ivan Brcic**, Associate and **Andrew Sharpe**, Lawyer

A recent suite of proposed reforms by the Federal and New South Wales Governments aimed at achieving net zero targets will entrench environmental compliance and sustainable project delivery requirements for both the public and private sectors in Australia.

As these reforms are rolled out, proponents of property development and infrastructure projects should continue to review their project delivery processes to ensure they are compliant and reflect changing best practice.

In April 2024, the Federal Minister for the Environment and Water, The Hon Tanya Plibersek MP, announced the roadmap for implementation of the long-awaited reforms to the *Environment Protection and Biodiversity Conservation Act 1999* (Cth) (**EPBC Act**). This announcement included the introduction of Australia's first independent national environmental protection agency, Environment Protection Australia (**EPA**), more rigorous compliance and enforcement measures and significantly increased penalties for environmental breaches.

There is also significant change underway in New South Wales with the introduction of new assessment requirements for large emitters of greenhouse gases (**GHG**) by the NSW Environment Protection Authority (**NSW EPA**) and the implementation of a new policy by Infrastructure NSW focused on decarbonising infrastructure projects delivered by NSW Government agencies.

EPBC Act reform

Following the release of its Nature Positive Plan in December 2022, the Federal Government commenced its reform of the national environmental legal and regulatory framework.

The Stage One reforms included the establishment of a Nature Repair Market, expected to open in 2025, which establishes a marketplace where individuals and organisations can undertake nature repair projects to generate a tradable certificate.

The recently announced Stage Two reforms include the introduction of three bills to Parliament, which will:

- establish the new Federal EPA;
- establish a head of the Environment Information Australia agency as a statutory officer within the Department of Climate Change, Energy, the Environment and Water;
- introduce stronger compliance and enforcement measures, including significantly increased civil and criminal penalties; and
- enshrine a statutory definition of 'nature positive' and require more regular reporting as to the state of Australia's environment.

A new Federal EPA

The *Nature Positive (Environment Protection Australia) Bill 2024* (Cth) will establish the Federal EPA, a statutory entity with considerable powers vesting in the office of the CEO of the EPA. The CEO of the new EPA is responsible for undertaking education, compliance and enforcement activities, and issuing various permits and licences.

The EPA's powers will include delivery of guidance and education to businesses on Australia's environment laws, enforcement of federal environment and other laws, and auditing businesses to ensure compliance with EPBC Act environment approval conditions. The primary focus of the EPA in the first instance will be on illegal land clearing and offsets.

Additional enforcement powers

The Minister for the Environment and Water will obtain new powers to issue 'Environment Protection Orders' (**EPOs**) where there is an imminent threat of serious damage to a protected matter, or where damage has already occurred, and to require that works are stopped, or specific actions be taken within specified timeframes.

In addition, the reforms will also increase the civil and criminal penalties for non-compliance with the EPBC Act, and courts can now impose penalties up to A$780 million for the most serious criminal offences and breaches of the civil provisions of the EPBC Act (such as breaching conditions of approval or undertaking a controlled action without approval).

These measures will bolster the enforceability of the EPBC Act and will require proponents to closely review their policies and procedures to:

- determine whether appropriate processes are in place to comply with the EPBC Act and any approvals issued under this legislation; and if not
- devise and implement new practices to ensure processes are in place to actively manage and ensure full compliance.

> With significant environmental reforms on the horizon, there are clear advantages for project proponents that plan ahead.

New controls to address climate change in planning decisions

On 20 May 2024, the NSW EPA released draft planning guidelines levelled at proponents of large-emitting projects. Under the draft EPA Climate Change Assessment Requirements (**Assessment Requirements**) and draft Greenhouse Gas Assessment Guide for Large Emitters (**Guide**), large emitters proposing new projects, or significant modifications to existing projects, will be required to prepare a GHG Assessment and GHG Mitigation Plan as part of their environmental impact assessments for planning approval.

The Assessment Requirements and Guide are only intended to apply to 'large emitters'.[1] However, the EPA has indicated that it will progressively implement GHG assessment requirements for all projects regulated by the EPA and will issue guidance for other projects that are expected to produce smaller quantities of GHG emissions. This means that while large emitters will be the first to be impacted by these reforms, proponents will increasingly be subject to these new assessment guidelines and information reporting requirements.

The guidelines specifically apply to development and infrastructure proposals in NSW. However, similar guidelines in relation to GHG emissions of proposed projects are being introduced in other states. For example, the latest version of the Environmental Factor Guideline – Greenhouse Gas Emissions published in Western Australia outlines how GHG emissions are to be considered by the environmental authority in the environmental impact assessment process. This guideline imposes requirements for projects to achieve net zero by 2050 and increases the number of large emitting projects to which stricter emissions management requirements apply.

Similarly, the Greenhouse Gas Emission Guideline was recently introduced in Queensland, and sets minimum expectations for the GHG emissions information that needs to be provided with applications for new environmental approvals and applications to amend existing environmental approvals. Applicants are required to outline the GHG emissions likely to be generated from a proposed activity and proposed measures to prevent or minimise emissions. Medium to high emitters (those with emissions over 25,000 tonnes of carbon equivalent per year) will also be required to provide a GHG abatement plan as part of their application.

Decarbonising infrastructure delivery

The NSW Government has also recently launched a policy for decarbonising infrastructure delivery as part of its Net Zero Plan. The policy is aimed at minimising carbon emissions created by public infrastructure projects and is accompanied by a technical guidance for Embodied Carbon Measurement.

Whilst the policy only applies to NSW Government infrastructure delivery agencies, at the Infrastructure and Transport Ministers' Meeting, the Ministers provided in-principle support for the use of a nationally consistent set of carbon values in the assessment of business cases for transport infrastructure projects over A$100 million. This means that government transport infrastructure providers throughout Australia could soon be required to implement strategies to decarbonise their infrastructure projects.

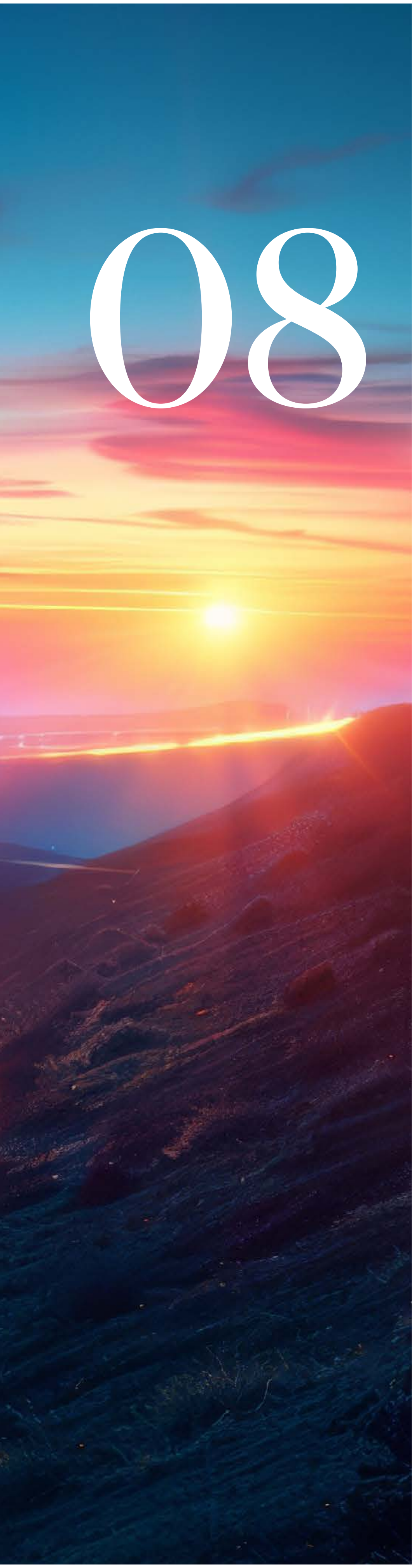
The NSW Government has not explained whether this policy could apply to the private sector through, for example, public-private partnerships. Prudently, however, all proponents who engage with government agencies on public infrastructure projects should engage with these reforms as they are likely to inform future procurement and tender requirements.

Next steps for property and infrastructure project proponents

With significant environmental reforms on the horizon, there are clear advantages for project proponents that plan ahead. Proponents that begin reviewing their policies and procedures now and take stock of their current data-gathering capabilities will be far better placed to navigate the incoming changes. In particular, proponents should:

- review their existing environmental compliance systems and identify opportunities to refine and update internal reporting requirements;
- update policies and procedures relating to reporting of environment-related breaches;
- review their existing measurement and data collection capabilities to ensure that they will be able to meet reporting requirements;
- carry out a risk assessment of dependencies on offsets both for specific projects and within the business more generally – the EPA's focus on offsets is likely to attract scrutiny towards proponents who rely too heavily on offsets to manage environmental harm;
- identify opportunities to reduce carbon emissions in their supply chains; and
- develop low carbon options for project delivery (such as in materials, structure and on-site emissions) that can be readily incorporated into government tenders.

1 Large emitters are entities whose activities will be/are carried out on premises with an existing environment protection licence under the *Protection of the Environment Operations Act 1997* (NSW) and are likely to emit 25,000 tonnes or more of scope 1 and 2 emissions (CO2-e) in any financial year during the operational life of the project (based on planned operational throughput and as designed).



Nuclear energy in Australia: a regulatory roadmap to inform decision-making

By **Anna White**, Partner, **Tracey Greenaway**, Head of Energy and Natural Resources, **Anthony Lepere**, Partner and **Milaan Latten**, Senior Associate

As pathways to achieve net zero are increasingly being discussed internationally and domestically, the role that nuclear energy might play in Australia's energy transition is drawing mixed views.

While various prohibitions exist under Commonwealth and State legislation relating to nuclear energy, this does not preclude the potential for nuclear energy to be investigated as part of a broader political, technical and social licence debate. To progress that conversation, formulating a regulatory roadmap for how a nuclear energy program might function in Australia would help to further inform decision-making about Australia's future energy mix.

At the Conference of Parties to the United Nations Framework Convention on Climate Change held in December 2023 (**COP28**), the 198 signatories (including Australia) recognised the need for deep, rapid and sustained reductions in greenhouse gas (**GHG**) emissions in a nationally determined manner, taking into account the Paris Agreement and different national circumstances pathways and approaches. In doing so, COP28 expressly called for States Parties to accelerate zero and low-emission technologies, including, for the first time, nuclear energy.

In other developments, the *Declaration to Triple Nuclear Energy* was endorsed by 22 countries at COP28 (and two countries after the event). This Declaration set out a goal of tripling global nuclear energy capacity by 2050 and inviting shareholders of international financial institutions to encourage the inclusion of nuclear energy in energy lending policies. While Australia did not sign the Declaration, it reflects the different views held internationally about the role that nuclear energy can play in the energy transition, and that it is reasonable, in Australia, to responsibly discuss and consider the role that nuclear energy could play in Australia's future energy mix.

International Atomic Energy Agency guidance

TThe International Atomic Energy Agency (**IAEA**) is an autonomous international organisation for scientific and technical cooperation in the nuclear field established under the United Nations framework that 'works for the safe, secure and peaceful uses of nuclear science and technology, contributing to international peace and security'. Australia is a founding member of the IAEA and party to a range of international treaties and conventions that form the substance of international nuclear law.

The IAEA has published extensive guidance to assist member states in their investigations into, and development of, a nuclear energy program. That guidance has been developed and revised with input from the direct experience of member states and provides a helpful base for any country in developing a regulatory roadmap for nuclear energy.

In June 2024, the IAEA updated its *Milestones in the Development of a National Infrastructure for Nuclear Power*, which identifies three phases and associated milestones for developing a nuclear energy program.

Phase 1 Considerations before a decision to launch a nuclear energy program is taken.

Associated Milestone: Ready to make a knowledgeable commitment to a nuclear energy program.

Phase 2 Preparatory work for the contracting and construction of a nuclear energy plant after a decision has been taken.

Associated Milestone: Ready to invite bids/negotiate a contract for the first nuclear energy plant.

Phase 3 Activities to implement the first nuclear energy plant.

Associated Milestone: Ready to operate the first nuclear energy plant.

When a nuclear energy facility reaches the end of its working life, decommissioning follows, for which the IAEA has published separate guidance.

The phased approach is significant. It means work can be done in Phase 1 to inform a considered decision – removed from ideological debate and focused on intergenerational equity and a balanced and reliable energy mix – on whether to undertake the work to prepare for a nuclear energy program in Phase 2 and implement that program thereafter.

Legal framework

A legal framework is one of a number of specific infrastructure issues that would need to be developed in Phase 1 and could help inform go/no-go parameters on nuclear energy. Any legal infrastructure would then be enacted in Phase 2, ready for application in Phase 3 should a decision to progress with nuclear power be made. The legal framework would need to:

- implement relevant international conventions and other instruments, including the *Vienna Convention on Civil Liability for Nuclear Damage*, the *Protocol to Amend the Vienna Convention on Civil Liability for Nuclear Damage* and the *Revised Supplementary Agreements Concerning the Provision of Technical Assistance by the IAEA* (the domestic application of international conventions and other instruments which Australia has already ratified, such as the Treaty on Non-Proliferation of Nuclear Weapons and the Convention on Nuclear Safety, would need to be considered to assess whether any amendments are required to reflect a nuclear energy program);

- establish an independent regulatory body with statutory powers, functions, technical capabilities and resources to regulate nuclear facilities and activities, including authorisation, inspection and enforcement; and
- repeal the existing prohibitions on nuclear energy and enact comprehensive legislation for all areas of nuclear law as would be required for civilian nuclear energy to the extent that it differs from the operation of a research reactor producing medical isotopes and specialised industrial materials (including, for example, new legislation concerning radiation protection, transport of radioactive and nuclear materials and export and import controls and amendment to existing legislation concerning environmental protection and foreign investment).

While this would be significant and complex work, there is existing legislation on which Australia could draw directly (including, for example, the mining of uranium under the *Radiation Protection and Control Act 2021* (SA), radiation safety under the *Australian Radiation Protection and Nuclear Safety Act 1998* (Cth) and the management and transport of radioactive waste under the *National Radioactive Waste Management Act 2012* (Cth)).

Regulatory framework

Important work to establish a regulatory body must be undertaken in Phase 1 so that it would be ready to operate from early in Phase 2 if the decision is to proceed. Expanding and substantially reshaping the role of an existing regulatory body, such as the Australian Radiation and Protection and Nuclear Safety Agency (ARPANSA), is one option to consider. This would present the opportunity to draw on existing institutional experience and personnel capabilities. ARPANSA, established under the *Australian Radiation Protection and Nuclear Safety Act 1998* (Cth), is responsible for licensing nuclear reactors for research or production of radioactive material for industrial or medical use.

Alternatively, an entirely new body (or bodies) could also be established. In either scenario, as the IAEA notes, recruiting and retaining appropriately trained personnel and maintaining the independence of the regulatory body (including an independent board) are key.

Bilateral and multilateral cooperation

Cooperation agreements with one or more existing nuclear energy nation states would play an important role in informing the investigations and law reform work required in Phases 1 and 2 and other capacity building required for nuclear energy infrastructure. Australia has some familiarity with such agreements – it has bilateral nuclear cooperation (safeguards) agreements with 43 countries to ensure Australia's exported uranium is used exclusively for peaceful purposes.

Looking ahead

In parallel with steps being taken to assess the social licence position, Australia could investigate possibilities for a nuclear energy program in a responsible and sustainable way consistent with current law.

While significant legal and regulatory reforms would be required to establish the infrastructure to support an actual nuclear energy program, IAEA guidance demonstrates that there is extensive international experience upon which Australia can draw, with opportunities for cooperation. Such a collaborative, evidence-based and incremental approach could also have synergies for other technologies to be investigated as part of achieving deep, rapid and sustained reductions in GHG emissions.

Developing a regulatory roadmap as described above, even in draft, would help chart some of the steps necessary to enable an informed discussion about whether there is a role for nuclear energy in Australia's future energy mix. A regulatory roadmap would complement other preparatory work considering the technical, economic, environmental and social feasibility of nuclear energy in Australia, without prejudicing public policy decisions to be made by governments, nor legislative reforms to be debated by parliaments.

“ In parallel with steps being taken to assess the social licence position, Australia could investigate possibilities for a nuclear energy program in a responsible and sustainable way consistent with current law.

To disclose or not to disclose? A step towards clarity on continuous disclosure

By **Andrew Lumsden**, Partner, **Katrina Sleiman**, Partner, **Abigail Gill**, Head of Investigations and Inquiries and **James North**, Head of Technology, Media and Telecommunications

Navigating continuous disclosure rules is both an art and science. The decision as to when to inform the ASX about information that 'a reasonable person would expect to have a material effect on the price or value of its securities' is never simple, and the myriad case-specific facts only serve to highlight the complexity of advising in this area.

To add to this, the range of issues that may have material financial impacts, such as cyber incidents and ESG-related disclosures, is ever-widening.

A number of recent cases, including the Zonia Holdings case,[1] have helped to shed some light on the nature of continuous disclosure obligations and, in particular, dealing with unknowns, confidentiality and materiality. Outside the specifics of the case, the judgment provides useful guidance for a wide range of issues including the difficult issue of cyber incident disclosure and when information should be disclosed to the ASX.

The decision as to how and when to disclose investigations and threatened claims, whether they are initiated by a regulator or another party, is never simple and there are often good commercial and legal reasons why a listed entity might not disclose these matters. Sometimes the decision as to whether to disclose is impacted by the nature of the information or the status of the matter and the desire to avoid disclosing material that would 'paint an entirely inaccurate and incomplete picture of the state of affairs',[2] and make the disclosure of the material misleading.

In Zonia Holdings, the Court had some sympathy with that perspective and affirmed that the basic principle behind the continuous disclosure provisions was that investors must be put in a position that allows them the opportunity to assess the value of disclosed information for the purpose of making an investment decision. Here, the Court was persuaded that some of the material alleged to have been required to have been disclosed was incomplete in important respects and omitted important contextual matters. The Court found that if the Bank had disclosed the information alleged to be required to be disclosed, it would, without more information, have created a misleading picture.

Disclosure of regulatory investigations

The Zonia Holdings judgment also provides a number of useful insights for answering the question of when a listed entity needs to disclose a regulatory investigation. First, the Court held that the requirement for 'awareness' is not to be assessed by what information **could** have been discovered as the result of an internal investigation, nor does it extend to information that was discovered with the benefit of hindsight. Rather, the appropriate starting point is whether a relevant person should have 'formed an opinion or drawn an inference' from the facts provided.

Second, the Court's determination of 'materiality' demonstrates that whether a regulatory investigation ought to be disclosed is highly fact dependent and largely informed by context. The Court recognised that a failure to uphold legislative obligations, such as those under the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (**AML/CTF Act**), is a serious issue.

However, an issue that warrants regulatory investigation does not necessarily result in a 'financially significant' outcome that would materially affect an entity's share price or value. Consequently, non-compliance or the commencement of a regulatory investigation alone may not at the time meet the threshold of material regulatory information that must be disclosed.

Given the highly contextual nature of this determination, some matters that informed the Court's decision included that:

- although some contraventions involved a large number of transactions, the underlying cause was a single coding error (as opposed to a systematic issue), the issue was rectified and the transactions only represented a small percentage of the total transactions in the Bank's overall monitoring process;
- while investors can expect entities to implement measures to mitigate risks, investors would generally understand that financial institutions have operational risks;
- some of the non-compliance was historical and not an ongoing problem; and
- there was a lack of certainty as to whether AUSTRAC was likely to commence enforcement proceedings and impose a civil penalty, particularly when AUSTRAC's preferred approach at that the time was cooperative engagement.

1 *Zonia Holdings Pty Ltd v Commonwealth Bank of Australia Limited* (No 5) [2024] FCA 477.

2 *Zonia Holdings,* [577].

Interestingly, the Court found that the issue of disclosure turns on whether the information is going to have a 'material effect' on the price or value of an entity's securities. That is, whether the information is likely to influence people who commonly invest in shares. Materiality is a vital 'filter' for disclosure because it ensures that listed entities don't over-disclose.

In *Grant-Taylor v Babcock & Brown Limited (in Liquidation)* [2015] FCA 149 1, the Full Court suggested it should first determine what disclosure ought to have been made. That may involve more than a simple correction but also contextual information that explains the economic effect of that information.

Materiality of information is determined at the time the alleged disclosure should have occurred. There seems to be a growing body of opinion that, in determining if the information would have had a 'material effect' on the price or value of an entity's securities, it is not determinative (but may be relevant) that when the information was released, the price of the entities' securities did move in a material way.

Third, one important qualification to the continuous disclosure obligation is where the material is, and remains, 'confidential'. The Court explored the question of confidentiality and found that information that is not generally available is not necessarily confidential information. Many aspects of a listed entity's day-to-day business are not generally available, but that does not mean that those aspects, or information that is generated for internal management purposes, is necessarily confidential.

Disclosure of cyber incidents

Earlier this year, the ASX updated ASX Listing Rules Guidance Note 8 to include a new example to demonstrate when ASX thinks information in relation to a cyber incident should be disclosed. The example supports the position adopted in Zonia Holdings whereby disclosure is not usually required where the entity cannot yet ascertain the materiality of the issue to the price or value of its securities due to limited information.

Interestingly, the example suggests that incomplete information about an ongoing cyber incident is unlikely (by itself) to justify delaying disclosure of known information. However, it affirms the position in Zonia Holdings that disclosure needs to be reviewed in context and through the lens of whether the disclosure will create a misleading picture.

This element of the reasoning suggests there is real value in preparing a 'dummy' announcement and reviewing it critically to ensure that it doesn't create a misleading picture of the circumstances. It would be beneficial for the disclosure team to put themselves in the shoes of an investor who is likely to ask, '*Why am I being told this? What is the significance of what I'm being told, and what are the consequences for the issuer?*'

Where the issue being considered involves a possible regulatory breach, Zonia Holdings makes it clear that the regulator's then-known attitude to the issue is significant information for an investor's decision-making. Context is important because the reasonable investor is not concerned with 'mere theoretical possibilities'. The reasonable investor wants meaningful information on the significance and consequences of what they are being told in order to make an informed and rational decision on whether to acquire or dispose of securities. The absence of such material from an announcement can 'paint a misleading picture'.[3] When considering the regulator's known attitude to the issue, it is important to keep in mind that the Office of the Australian Information Commissioner (**OAIC**) is becoming increasingly vigilant with respect to cyber incidents, as highlighted by recent enforcement activity and OAIC's prioritisation of data breaches.

In the context of cyber incident disclosure, it is interesting that the example in ASX Listing Rules Guidance Note 8 suggests that confidentiality is maintained when dealing with a relevant regulator on a confidential basis. However, given the ability for data and privacy regulators such as the OAIC, to impose civil penalty provisions, it may not be possible to maintain confidentiality once affected individuals are notified. The Court's consideration of confidentiality in relation to regulatory investigations in Zonia Holdings is instructive for listed entities determining when they should disclose potential cyber-related regulatory investigations. The Court indicated that the Bank's potential exposure to regulatory enforcement action was confidential information given it was 'insufficiently definite to warrant disclosure'.

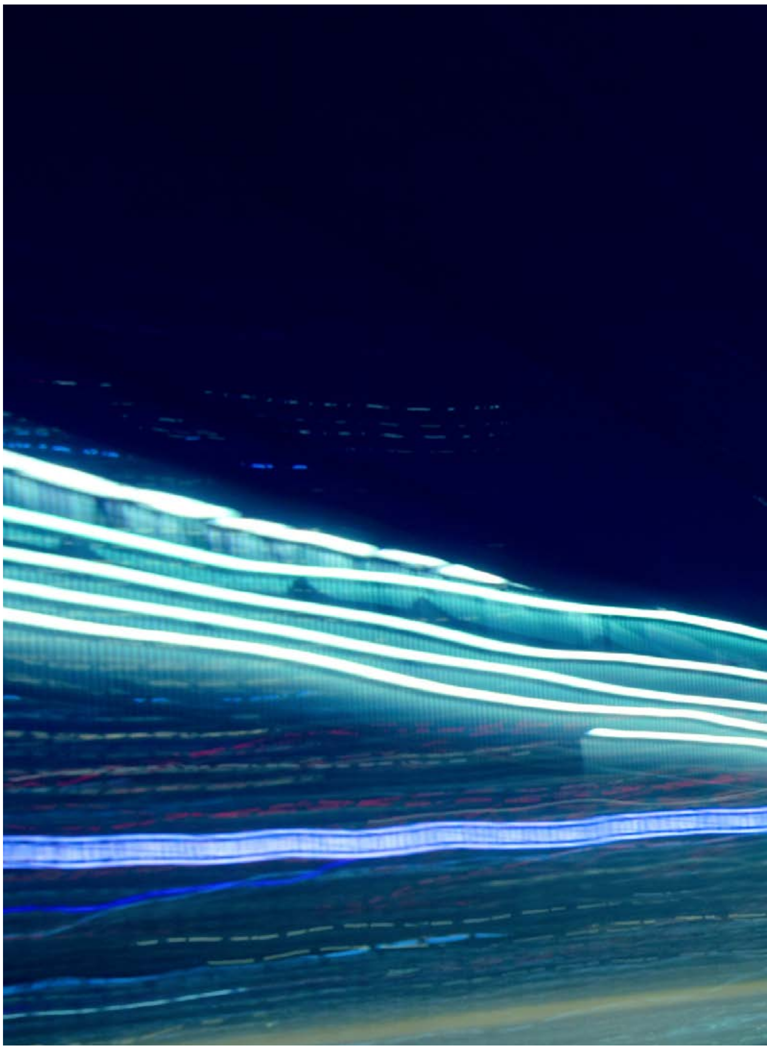
Key takeaways

In Zonia Holdings, the Court found it relevant that, when assessing if a particular matter if disclosed would be likely to have a material effect the price or value of securities, market participants understand that regulatory issues (including matters of non-compliance) arise in respect of large organisations and that regulators conduct investigations in relation to those issues on a regular basis. In most cases there would not be an expectation in the market that these engagements would, as a matter of course, be disclosed by ASX announcements. Instead, what is required is greater certainty regarding a financially significant outcome that will be a consequence of the investigation.

Similarly, when confronted with a cyber incident, an entity's ASX disclosure obligation needs to be assessed by reference to the entity's actual knowledge at the time. This can be assessed by preparing a draft announcement based on the facts as far as they are known.

Those 'facts' might include:

- A description of the incident
- The material facts
- Any material impact on operations or financial position
- The action the entity is taking in response to the breach
- Whether the incident is continuing
- When the entity expects to be in a position to update the market



3 *Zonia Holdings*, [606].

The draft should then be carefully reviewed, having consideration to the following questions:

How helpful is it to an investor and is it material?

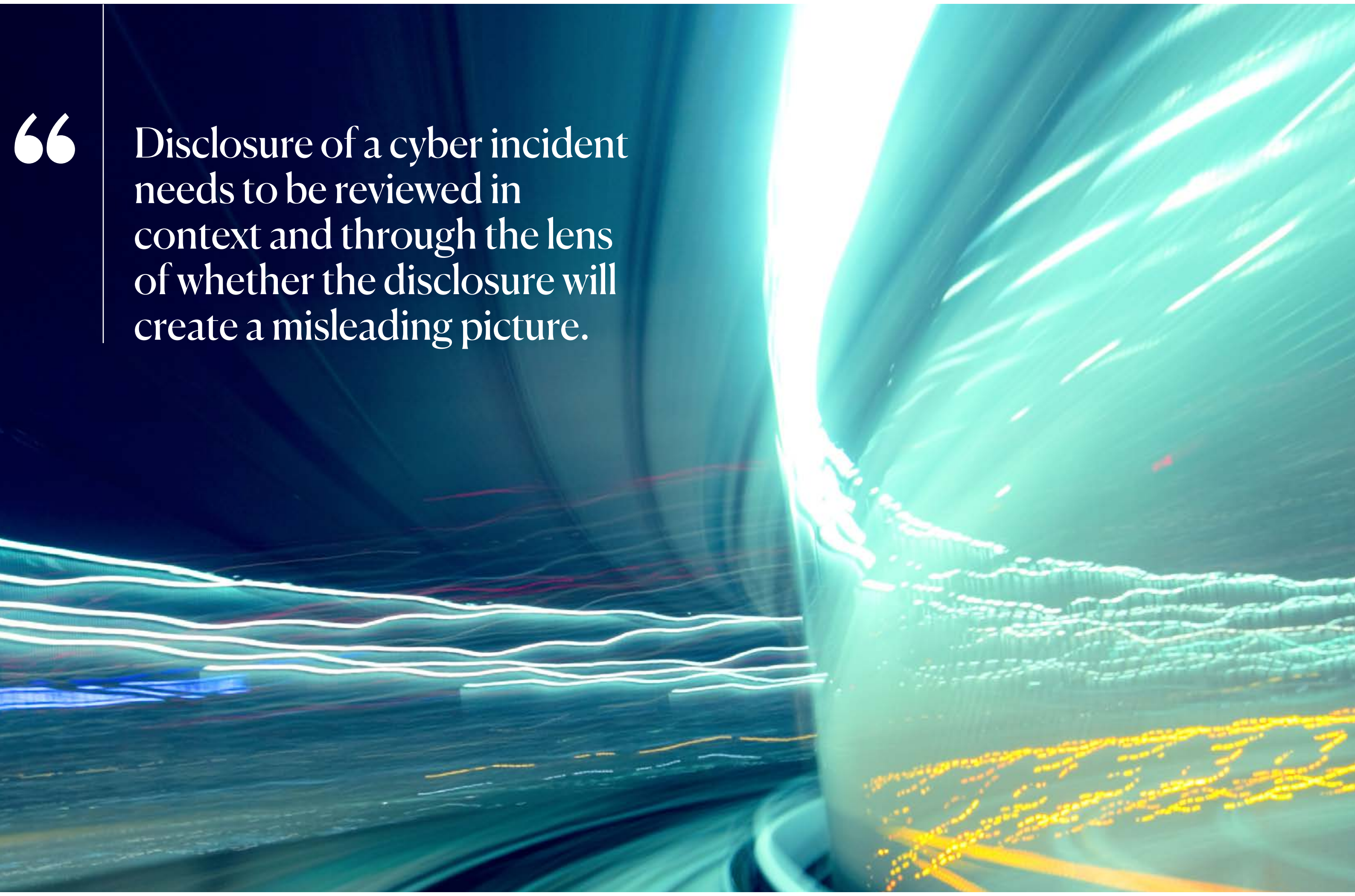
Is the information confidential and is it likely to remain so?

Does the announcement create a misleading picture?

Can the picture be enhanced to help investors be put in a position that allows them the opportunity to assess the value of disclosed information for the purpose of making an investment decision?

It is also important to keep in mind that the 2021 amendments to the continuous disclosure laws introduced state of mind into the test. For a listed entity to be liable to compensate security holders, it needs to be shown that the issuer knew or was reckless or negligent about whether the information would, if generally known, have a material effect on the price or value of its securities. The key question is then which individual(s) must have the requisite state of mind for the entity's state of mind to be established. Recognising that this question is not easily answered, the Federal Government has recently agreed to amend the Corporations Act to expressly provide how state of mind can be attributed to the entity within the continuous disclosure regime.

While the Zonia Holdings class action did not directly bear on climate-related disclosure or ESG, the case could be interesting for listed entities as they begin to consider how a regulatory investigation touching on these issues may impact on their continuous disclosure obligations. The question of when an organisation became aware of relevant information and what inferences it drew, or should have drawn, from the information will likely be relevant for these two issues as well as cyber incidents.



“Disclosure of a cyber incident needs to be reviewed in context and through the lens of whether the disclosure will create a misleading picture.

The expansion of corporate work health and safety and environmental enforcement in Australia

By **Nick Le Mare**, Head of Employment and Labour, **Anna White**, Partner, **Danika Casey**, Special Counsel, **Nicholas Finlay**, Senior Associate and **Ashley Rooney**, Associate

Significant changes to work health and safety (**WHS**) and environmental laws are progressively being introduced across Australian jurisdictions with the express aim of making it easier for regulators to prosecute corporations for serious offences while at the same time making it harder for corporations to avoid the costs of non-compliance.

What are the key changes that are likely to result in heightened levels of enforcement activity from regulators and how can corporations mitigate their exposure?

Compliance with work health and safety (**WHS**) and environmental laws continues to be an area of increasing criminalisation and scrutiny. However, even with the availability of existing serious offences (such as those involving reckless or wilful conduct) and the introduction of new serious offences (such as industrial manslaughter), to date there have only been a handful of successful prosecutions against corporations for such offences.

It is primarily for this reason that significant changes to WHS and environmental laws – including bans on certain insurance arrangements, the introduction of new environmental offences and enforcement tools, and substantial increases to maximum penalties – are progressively being introduced across Australian jurisdictions.

'Watering down' of existing serious WHS offences

Existing serious offences under WHS laws are being progressively amended across Australian jurisdictions to include alternative fault elements that are easier for prosecutors to prove.

In some jurisdictions,[1] prosecutors now have the option of seeking to prove either the objective fault element of negligence or the intentional fault element of recklessness for serious offences. In a criminal law context, reckless conduct is intentional and generally requires the prosecution to prove a conscious choice by a duty holder to take an unjustified risk (a state of mind). Negligence, however, is an objective fault element, and does not require state of mind to be proved. Arguably, this makes negligence an easier element to prove than recklessness.

Again, these changes which have the effect of 'watering down' the fault elements for existing serious offences will improve a regulator's ability to prove essential elements of the offences.

These changes to WHS offences align with environmental offence provisions in various Australian jurisdictions, including the Commonwealth,[2] Western Australia[3] and Queensland,[4] where negligence has expressly been a component of fault for some time.

Introduction of new offences, duties and powers

A number of new WHS and environmental offences, duties and powers have also been, or are proposed to be, introduced across Australian jurisdictions. The most significant new offences under WHS laws are the industrial manslaughter offences, which have now been introduced in all Australian jurisdictions, other than Tasmania (where relevant amendments are still before the Parliament). In addition to carrying significant penalties, some jurisdictions[5] also allow for alternative verdicts to be returned by a Court in proceedings for an industrial manslaughter offence.

This is intended to serve as another incentive for prosecutors to commence proceedings for the more serious offence of industrial manslaughter, as a verdict can still be returned for a less serious offence (subject to evidence proving that offence) if the Court is not satisfied that an industrial manslaughter offence has been proved.

New offences, duties and powers have also been introduced to environmental laws, expanding the enforcement toolkit available to regulators. These include:

- at the Commonwealth level, those proposed to be introduced by the Stage Two environmental legislation reforms, including:
  - new Environment Protection Orders and expanded scope for environmental audits; and
  - the establishment of a new independent Commonwealth environmental protection agency, Environment Protection Australia, which is to be a 'tough cop on the beat';
- in New South Wales, new offences for the illegal dumping of litter or waste, along with expanded NSW Environment Protection Authority enforcement tools, which include two new types of Environment Protection Notices (being Preliminary Investigation Notices and Recall Notices), an expanded scope for Clean-up Notices and a new power to issue public warning statements; and

1 Section 31 of the Model Work Health and Safety Act has been amended to include both fault elements, with these changes having already been adopted in the Commonwealth, South Australian, Australian Capital Territory and New South Wales jurisdictions. Amendments are currently before the Parliament in Queensland. Other harmonised jurisdictions may also adopt this amendment in due course.

2 See sections 494 and 495 of the EPBC Act.

3 See, for example, sections 49 and 50 to 50B of the *Environmental Protection Act 1986* (WA)

4 In Queensland offences committed 'wilfully' attract higher penalties, that term being defined to include 'gross negligence'.

5 Alternative verdicts are currently available for industrial manslaughter offences in the Commonwealth, Western Australian, Australian Capital Territory, Northern Territory and South Australian jurisdictions. Amendments to introduce alternative verdicts for industrial manslaughter offences have been passed in New South Wales and are currently before the Parliament in Queensland.

- in Queensland, new Environmental Enforcement Orders, along with a new standalone duty to restore the environment where an incident involving contamination resulting in unlawful environmental harm has been permitted or caused, and an offence for failing to comply with the general environmental duty where that failure causes, or is likely to cause, serious or material environmental harm. These reforms bring Queensland more into line with the regime in Victoria, where a positive duty to manage contaminated land and an offence for failing to comply with that State's general environmental duty have been in place since 2021.

Increasing penalties and prohibitions on WHS insurance

Alongside the changes previously discussed, harsher penalties continue to be introduced to reflect the seriousness of WHS and environmental breaches.

The maximum penalties attaching to WHS offences have dramatically increased across most jurisdictions, with the highest maximum penalty available against a corporation currently sitting at A$25 million. Mechanisms to continually increase the maximum penalties for offences under WHS laws have also been adopted in some jurisdictions.[6] Likewise, bans on insurance (including contractual indemnity arrangements) against penalties for breaches of WHS offences are also being progressively adopted across jurisdictions,[7] with the aim of ensuring that financial consequences are borne directly by a corporation, rather than being shifted to insurers.

Maximum penalties attaching to environmental offences in New South Wales have also risen recently, while the most dramatic increase is proposed to be introduced at the Commonwealth level, where penalties up to A$780 million could be imposed for the most serious offences under the *Environment Protection and Biodiversity Conservation Act 1999* (Cth). These penalty reforms align penalties for serious environmental offences with the civil penalty regimes for serious corporate and financial crimes under the *Corporations Act 2001* (Cth) and the *Australian Securities and Investments Commission Act 2001* (Cth). The increased penalties reflect a significant shift in recognising the potential seriousness of environmental crime.

Key takeaways

The changing regulatory landscape will almost inevitably lead to an increase in enforcement activities by regulators under applicable WHS and environmental laws.

Regulators will be keen to use the recent and ongoing legislative changes to their full force, and this will include an increase in regulatory action against corporations that are not prioritising compliance with WHS or environmental laws, exposing them to the potential imposition of significant penalties.

Employers who prioritise their WHS and environmental performance and compliance should ensure their management systems and processes are appropriately calibrated to take account of these changes.

> “The changing regulatory landscape will almost inevitably lead to an increase in enforcement activities by regulators under applicable WHS and environmental laws.

6 The Model Work Health and Safety Act has been amended to include tiered monetary penalties for offences. These changes have been adopted in the Commonwealth jurisdiction. New South Wales has also adopted a formula for annually increasing the amount of a penalty unit for WHS offences.

7 WHS insurance is now banned in the Queensland, New South Wales, Australian Capital Territory, South Australia, Victoria and Western Australia jurisdictions. Amendments to introduce a ban on WHS insurance have been passed in South Australia.

11 How will Australia's new sustainable finance taxonomy impact the mining sector?

By **Tracey Greenaway**, Head of Energy and Natural Resources, **Anthony Lepere**, Partner and **Jo Dodd**, Partner

Following the development of sustainable finance taxonomies in the European Union, ASEAN and other relevant markets, the Australian Sustainable Finance Institute (**ASFI**) is currently developing an Australian taxonomy. The taxonomy reinforces the Federal Government's ambition to drive a net zero transition both domestically and internationally through a variety of regulatory tools.

Designed to mobilise private capital towards sustainable economic activities that meet climate change mitigation objectives, the taxonomy is complex, evolving and will be subject to ongoing review. However, an opportunity exists now for mining sector participants to influence the types of minerals, activities and thresholds that will fall within the taxonomy and contribute to a workable framework.

Sustainable finance taxonomies are science-based frameworks that provide guidance to market participants on how to identify projects, assets and activities that are low-carbon (or compatible with low-carbon economic development) or that are environmentally sustainable. Their aim is to direct investments to the activities most needed for the transition to net zero and environmental sustainability. Taxonomies can help align investments with national environment policies and sustainable development plans and are increasingly used as a governmental tool to facilitate compliance with the Paris Agreement goal of limiting global warming to below 1.5 degrees Celsius by the end of the century.

There are currently over 40 sustainable finance taxonomies in place or under development globally, which aim to implement multiple climate, environmental and social objectives. At this stage, however, most focus on achieving climate change objectives as a priority. Key objectives include '**climate change mitigation**' which focuses on reducing greenhouse gas emissions and achieving decarbonisation of sectors across the economy and '**climate change adaptation**' which focuses on building the adaptability and resilience of assets and activities across all sectors and helping stakeholders to address the current and expected adverse impacts of climate change.

Taxonomies can be used by financial institutions and corporates as frameworks for reporting, setting disclosure obligations and for 'labelling' financial products. They can also provide guidance on parameters for developing and implementing energy transition plans that align with net zero objectives. For example, the EU introduced a taxonomy in July 2020 and under new rules large, listed EU companies have started to report against two of the EU taxonomy's key objectives – climate change mitigation and climate change adaptation. Initial evidence is that companies, public entities and financial investors are increasingly using the taxonomy for business strategies, transition planning, investing and lending. If implemented effectively and continuously, taxonomies can be a significant driver of change.

> "If implemented effectively and continuously, taxonomies can be a significant driver of change.

Does Australia have a sustainable finance taxonomy?

The Australian Taxonomy Development Project commenced in July 2023. It is a joint industry-government initiative, led by the Australian Sustainable Finance Institute (**ASFI**) in partnership with the Commonwealth Treasury, to develop an Australian sustainable finance taxonomy. The project has an initial climate change mitigation objective and a significant transparency focus, and is seeking to strengthen transparency, improve financial market regulation and drive growth in sustainable finance markets. It also identifies six priority economic sectors to focus on:

1.	Electricity generation and supply (energy)
2.	Minerals, mining and metals
3.	Construction and the built environment
4.	Manufacturing and industry transport
5.	Agriculture
6.	Land

These priority sectors were selected for inclusion in the taxonomy because they provide the greatest potential to contribute to the Federal Government's net zero ambitions (including its Net Zero Plan) and support the Future Made in Australia strategy. They are a mix of high-emitting sectors, those that are instrumental in facilitating the transition to net zero, and/or those that have a substantial role in a net zero economy based on current technological readiness levels. Importantly, one of these sectors is minerals, mining and metals.

While the taxonomy will initially be voluntary, the Federal Government is considering embedding the taxonomy in Australia's regulatory architecture, meaning it may ultimately become interlinked with Australia's climate-related financial disclosure regime, which will commence on 1 January 2025. It is therefore important for all market participants who engage in (or with) the mining sector (including lenders, equity investors and those engaged in the mining sector more broadly) to build an early understanding of the activities that are considered as contributing to net zero.

Why a focus on minerals, mining and metals?

There are two key reasons for the focus on the minerals, mining and metals sector:

1. **Critical and strategic minerals.** Large quantities of metals are required for the clean energy infrastructure and technology that supports a global energy transition. As a result there is expected to be significant growth in demand for relevant critical metals including copper, nickel, lithium and cobalt. This creates opportunities for the Australian mining sector. However, the Government wants to ensure that related mining activity is undertaken in an environmentally and socially sustainable way.
2. **Iron ore.** Steel is a key component of most modern technologies and infrastructure and its principal raw material is iron ore. Iron ore is Australia's largest resources export, accounting for 41% of total mining export earnings. It is therefore a vital mineral for Australia's economy. However, there is a recognition that decarbonisation is a key factor in the ongoing sustainability of the iron ore sector and an appropriate area of focus.

In general, once priority sectors are identified for inclusion in a taxonomy, the economic activities within each priority sector are analysed to determine which activities contribute meaningfully to the taxonomy's objectives (i.e. to climate change mitigation). This task is complex and, in the context of the Australian mining sector, quite novel, as to date mining activities have only been included in other global taxonomies to a limited extent.[1] This means there is limited guidance on the types of activities that should be considered as contributing to the energy transition and emissions reduction.

This creates an opportunity for the Australian mining sector and related stakeholders to influence how these activities (and minerals) are perceived globally, and ASFI is encouraging all stakeholders to contribute to the discussion and development of these criteria.[2]

1 The Taxonomy Technical Expert Group (**TTEG**) is the body tasked with developing the initial phase of the taxonomy in consultation with the Australian Council of Financial Regulators' Climate Working Group (**CWG**) and ASFI.

2 The IFC Net Zero Roadmap to 2025 for Copper & Nickel Mining Value Chains and the Climate Bonds CRM criteria provide some guidance. There will be a second round of public consultation in Q4 2024. ASFI is engaging with a range of stakeholders including First Nations people, environmental NGOs and organisations involved in developing international taxonomies.

What activities are eligible for inclusion in the taxonomy?

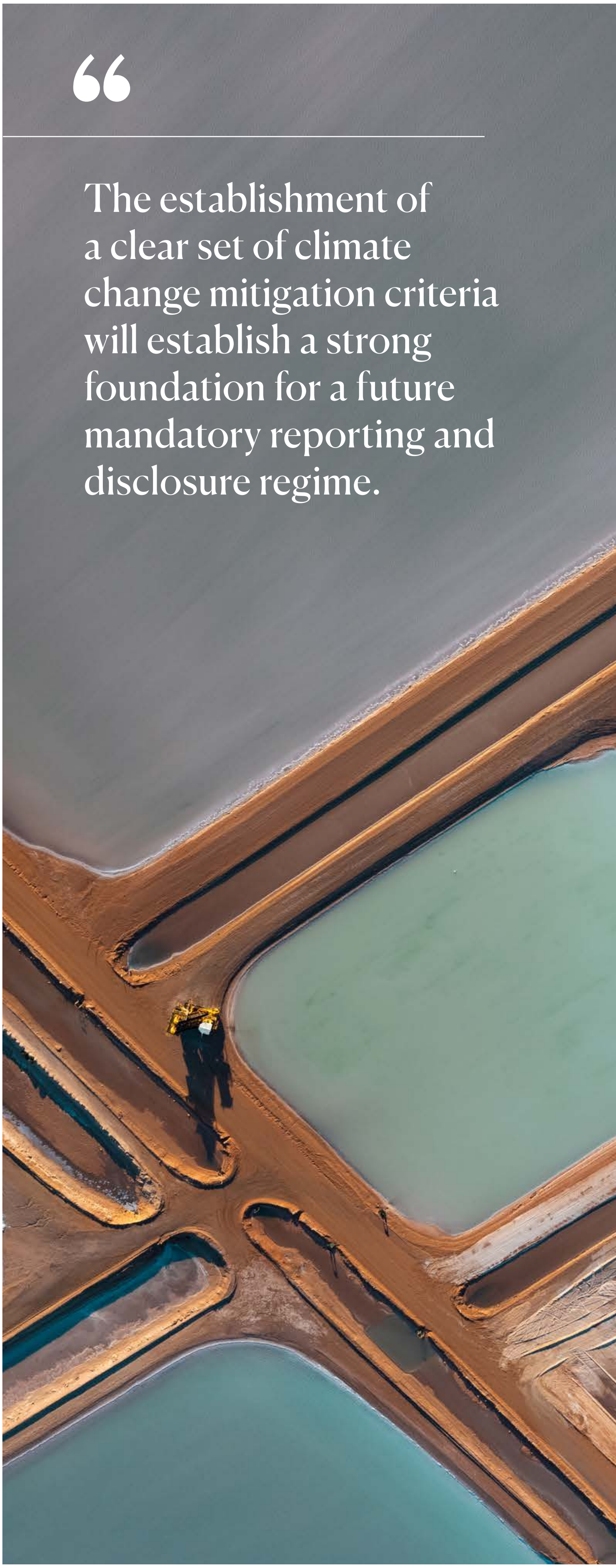
Two filters apply to determine whether an activity is eligible for inclusion in the taxonomy. These are:

1. **Nature of the activity.** Each of the minerals selected for inclusion in the initial phase of the taxonomy has been classified as a 'green' or 'transition' activity because:
   - they have a role in the global economy post 2025;
   - the risk of locking in future high carbon emissions is moderate (although can be mitigated); and/or
   - they can be decarbonised across scope 1, 2 and 3 emissions.
2. **Performance of the activity.** To be classified as green or transition, separate technical screening criteria (**TSCs**) also need to be satisfied. These TSCs (still under development and subject to consultation) define the specific substantive performance requirements, thresholds and/or other metrics the activity must meet. In the next phase of development, further social and environment-focused criteria will also be applied.

The proposed TSCs currently apply to operating mines and are slightly different for each mineral. However, as a general rule, to achieve transition status, a mine site must be implementing eligible measures to address more than 50% of its fuel costs and/or 50% of scope 1 emissions (at 2020 baseline) via 'eligible measures', including:

- electrifying or powering the vehicle fleet by low carbon fuels;
- switching electricity sources (from grid non-renewables and on-site diesel generation to grid or on-site renewable power generation); and
- deploying energy storage technology.

To achieve green status, emissions must be reduced under a sliding scale to zero by 2036. Iron ore is treated slightly differently because it has a significantly larger contribution to emissions in Australia. As a result, in addition to implementing eligible measures at the mine site, scope 3 emissions reduction targets must also be met to achieve transition status. This is intended to incentivise less CO_2 intensive forms of iron reduction.



"The establishment of a clear set of climate change mitigation criteria will establish a strong foundation for a future mandatory reporting and disclosure regime.

Additional targets must be met to ensure green status for iron ore, including a reduction in mine site emissions and scope 3 emissions. The scope 3 reduction requirement can be satisfied by having:

- an offtake agreement in place to supply more than 25% of the current volume of iron ore to a low carbon steel producer (with more than 50% of volume produced at the mine site agreed to be part of the offtake agreement by 2030); or
- offtake agreements with whole entities that are decreasing steel production emissions in line with a 1.5 degrees Celsius pathway.

These emissions reduction targets are acknowledged to be ambitious and to have the objective of accelerating emissions reduction and the growth of low carbon steel production domestically and internationally.

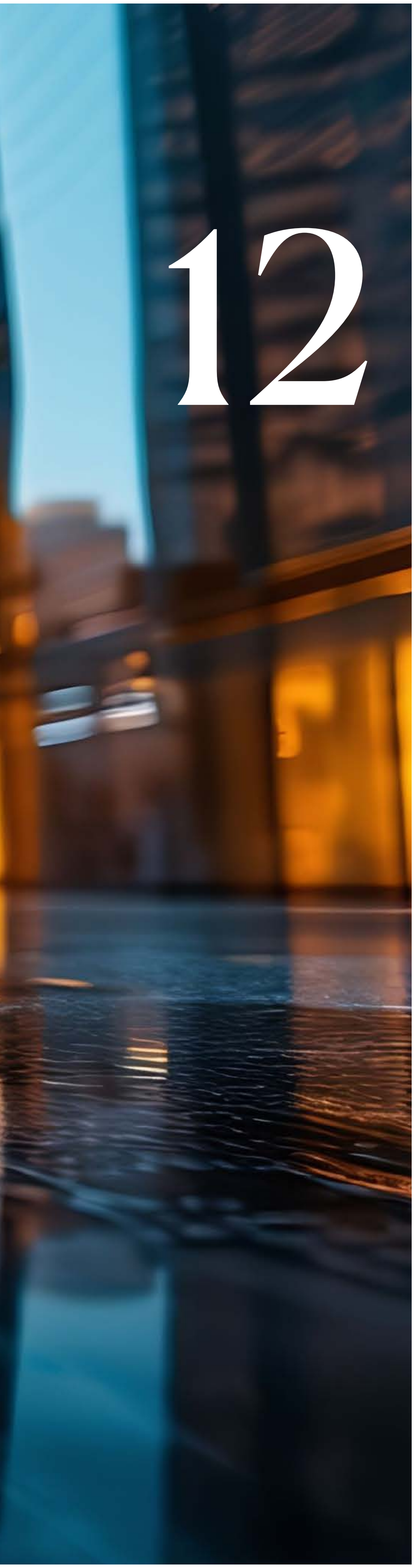
Looking ahead

The development of the taxonomy reinforces the Federal Government's ambition to drive a net zero transition both domestically and internationally through a variety of regulatory tools, and we can expect to see financiers and companies prioritise investments in activities with green or transition status.

The establishment of a clear set of climate change mitigation criteria to voluntarily perform to and report against will establish a strong foundation for a future mandatory reporting and disclosure regime for entities that use the taxonomy (and we can expect this to follow).

Further, the 'eligible measures' criteria for reducing scope 1, 2 and 3 emissions at mine sites signals an increased push towards decarbonisation through vehicle fleet electrification, energy storage, renewable energy and low carbon fuels – we can expect to see a proliferation of decarbonisation projects to facilitate this.

Australia's sustainable finance taxonomy is complex, evolving and will be subject to ongoing review. However, an opportunity exists now for mining sector participants to influence the types of minerals, activities and thresholds that will fall within the taxonomy and to contribute to a workable framework.



Preparing for ATO review in an ever-evolving tax landscape

By **Cameron Blackwood**, Head of Tax, **Luke Imbriano**, Partner, **Craig Boyle**, Special Counsel and **Julia Bolodurina**, Senior Associate

Focusing on tax through the lens of governance, and not just the tax returns lodged and positions adopted, is not a new concept. Both the Federal Government and the Australian Taxation Office (**ATO**) have placed an increased emphasis on tax governance and evidence, tax reporting and the regulation of tax practitioners in recent years, and this is only set to continue.

Together with a number of recent tax developments, trends in case law and the ever-increasing regulatory scrutiny of corporate taxpayers, some form of ATO review should be expected. Taxpayers should establish and maintain robust internal tax governance frameworks which appropriately manage risks and ensure positions are documented with supporting objective and contemporaneous evidence.

In Australia, the ATO has been at the forefront of ensuring corporate tax compliance – both in articulating what the regulator expects and reviewing corporate tax governance through the 'Justified Trust' program. The ATO summarises its tax governance expectations for both boards and management generally as follows:

Boards

1. **Have a formalised tax control framework in place, which can include the tax risk appetite of the group.**
2. **Clearly understand roles and responsibility for tax risk management.** This includes ongoing briefings by management for directors regarding tax risk management strategies and allocating tax risk to an appropriate and independent board sub-committee, for example an audit committee.
3. **Be appropriately informed.**
4. **Regularly assess policies and controls.**

Management

1. **Ensure sufficient capacity and capability**
   - Roles and responsibilities clearly understood
   - Senior management confident of capacity and capability
   - Significant transactions identified
2. **Ensure IT controls are in place**
   - Controls in place for data
   - Record-keeping policies are determined
3. **Assure the flow of information from accounting records**
   - Control frameworks are documented, including procedures for reviewing tax returns and supporting workpapers and document retention
   - Procedures to explain significant differences
   - Complete and accurate tax disclosures
4. **Deal with law and administrative updates**

   Legal and administrative changes are addressed, including assessing whether such changes require updates to the internal control framework as well as reviewing and implementing changes.

These principles are expanded upon in the ATO's *Tax risk management and governance review guide*, which was developed for large and complex corporations conducting business in Australia. In addition, the regulator's income tax management and governance publication, which is intended to assist taxpayers in preparing for a Top 1,000 combined assurance review, builds on this framework and sets out the ATO's rating system for assessing a taxpayer's tax governance, including how the taxpayers may evidence the existence of key controls.

Even with good governance, expect an ATO review

All taxpayers in the Top 1,000 public and multinational taxpayer population, and Top 500 and Next 5,000 private group populations, will be regularly reviewed by the ATO. Having good tax governance is critical. Taxpayers must be ATO 'audit ready', which means having contemporaneous objective evidence to support all material tax positions, as well as supporting tax legal advice and/or engaging early with the ATO.

Recent developments

The focus of the Federal Government and the ATO on tax governance, tax reporting and the regulation of tax practitioners is also reflected in a number of recent developments:

- **Reforms of regulatory arrangements for tax practitioners.** This includes the introduction of the *Treasury Laws Amendment (Fairness and Accountability) Act 2024* (Cth) (which included promoter penalty law reform, extending tax whistleblower protections, Tax Practitioners Board (**TPB**) reform and information sharing between government agencies about misconduct) and consultation on the registration requirements for tax practitioners.
- **Increased scrutiny of taxpayer claims for legal professional privilege.** This is particularly the case in a non-legal context (but noting the ATO's expectation for taxpayers to provide detailed information to justify such claims). The ATO's views and expectations regarding privilege claims and the surrounding governance environment in which they were made takes on even more significance given the willingness of the Tax Commissioner to challenge incomplete claims, as seen in recent high profile Federal Court proceedings.

- **The overall tendency for new tax legislation to contain detailed and specific reporting and self-executing anti-avoidance provisions.** For example, the new thin capitalisation rules and their incorporation of a highly specific anti-avoidance rule and the 'equity funded' special dividend rules. This approach can make obtaining appropriate comfort for what are clearly commercial transactions challenging.

Recent Court decisions

The way Australia's anti-avoidance provisions are being used by the ATO is particularly relevant for the expectations placed on boards and management regarding the identification of significant transactions and ensuring adequate corporate tax function capability.

Specifically, recent litigation on the general anti-avoidance rule (**GAAR**), known as Part IVA (which can impose tax where a transaction is undertaken for sufficient tax reasons) illustrates the ATO's expansive interpretation and reliance on these provisions where tax risk is perceived by the ATO to be high. In turn, from a tax governance perspective, the length of time taken for Part IVA proceedings to be resolved highlights the need for strong corporate governance processes to be in place from the time of the transaction and beyond.

For example, in *Minerva Financial Group Pty Ltd v Commissioner of Taxation* [2024] FCAFC 28 (**Minerva**), the 'true gist' of the schemes to which Part IVA was asserted by the ATO to apply was the taxpayer's failure to exercise its discretion as trustee of a unit trust to make distributions to the holder of special units in the trust. In rejecting the ATO's argument, the Full Federal Court observed that there was nothing extraordinary about distributions flowing in accordance with the trust constitution and that such payments were not an objective matter that pointed to a party carrying out the scheme for the dominant purpose of enabling the taxpayer to obtain a tax benefit. The decision highlighted the requirement to consider the specific commercial consequences achieved by the relevant transaction, and that the relevant factors pertinent to determining the taxpayer's purpose must not be viewed in isolation.

This reasoning is consistent with another recent Part IVA decision in favour of the taxpayer, *Mylan Australia Holding Pty Ltd v Commissioner of Taxation (No 2)* [2024] FCA 253 (**Mylan**). In Mylan, the ATO's argument was narrowly focused on the tax implications of the 'scheme', while the Federal Court emphasised the need to consider the broader commercial rationale surrounding the relevant transaction, observing that the tax benefit cannot be considered apart from other factors, nor is obtaining or desiring a tax benefit sufficient for Part IVA to apply.

Looking ahead

The ATO's increased emphasis on tax governance and evidence, together with other recent developments and trends, is illustrative of the ever-increasing regulatory scrutiny that corporate taxpayers face, demonstrating the need for taxpayers to establish and maintain robust internal frameworks to address and appropriately manage tax risks.

This includes having detailed records supporting the existence of internal tax controls which are in line with and have regard to ATO guidance, as well as support for any tax positions taken. Recent cases on Part IVA also illustrate the importance of having contemporaneous evidence and documentation in place to support the commercial rationale behind significant transactions, which taxpayers should expect will be subject to ATO scrutiny.

13

Unpacking the EU's Corporate Sustainability Due Diligence Directive

By **Dr Phoebe Wynn-Pope**, Head of Responsible Business and ESG and **Kate Gill-Herdman**, Special Counsel

In this latest, special episode of Essential ESG, Phoebe Wynn-Pope and Kate Gill-Herdman unpack the European Union's Corporate Sustainability Due Diligence Directive (**CSDDD**).

One of the most significant corporate responsibility reforms made globally in recent years, the impact of the CSDDD is going to be felt well beyond the European Union, including in Australia. Phoebe and Kate consider the likely impacts on Australian businesses and discuss what organisations can do now to prepare.

Click to listen

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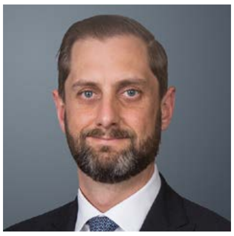
< Previous | Contents



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