Form 1
(Rule 2.1)

IN THE SUPREME COURT OF NEW SOUTH WALES No. 237028 of 2015
DIVISION: EQUITY
REGISTRY: SYDNEY
CORPORATIONS LIST

IN THE MATTER OF BBY LTD (RECEIVERS & MANAGERS APPOINTED) (IN LIQUIDATION)
ABN or ACN: 007 707 777

FILED

- 3 AUG 2016

STEPHEN ERNEST VAUGHAN AND IAN RICHARD HALL IN THEIR CAPACITY AS LIQUIDATORS OF BBY LTD (RECEIVERS AND MANAGERS APPOINTED) (IN LIQUIDATION) ACN 007 707 777 and another

Plaintiffs

J MAZZETTI PTY LTD ACN 006 705 602 AS TRUSTEE FOR J MAZZETTI PTY LIMITED STAFF SUPERANNUATION FUND (AND OTHERS) and others

Defendants

SUMMARY OF CONTENTIONS

Introduction and summary of SEGC's position

1. This Summary of Contentions is given pursuant to the direction of the Court on 20 July 2016 and is in respect of the direction or declaration sought in prayer 2 of the Originating Process filed by the First Plaintiffs (**Liquidators**) on 13 August 2015 in relation to the pooling of all (or some) of the client segregated accounts maintained by BBY (**CSAs**) and the application of reg 7.8.03(6) of the *Corporations Regulations* 2001 (**Regulations**) to the CSAs.

2. Securities Exchanges Guarantee Corporation Limited (**SEGC**) is the trustee of the National Guarantee Fund (**NGF**), a compensation fund available to meet certain claims arising from investors' dealings with participants of markets operated by ASX Limited (**ASX**). By reason of the payments of compensation already made to former clients of BBY, and pursuant to its right of subrogation under section 892F(1) of the *Corporations Act* 2001 (Cth) (**Act**), SEGC is currently a creditor and trust beneficiary of BBY.

3. SEGC:

   (a) contends that there should be pooling between the CSAs within the Equities and ETO product lines (**Equities/ETO CSAs**);

   (b) contends that there should not be pooling between the Equities/ETO CSAs on the one hand, and any of the CSAs in the Futures, FX, Saxo and IB product lines on the other;

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(c) contends that there should not be pooling between CSAs in the IB product line on the one hand, and any of the CSAs in the Futures, FX and Saxo product lines on the other; and

(d) (provided that there is no inter-product line pooling involving Equities/ETO CSAs) does not take any position on the issue of whether there ought to be pooling between CSAs in each of the Futures, FX and Saxo product lines.

Pooling within the Equities/ETO product line

4. The requirement for pro-rata distribution in reg 7.8.03(6) of the Regulations applies only within each account of a financial services licensee; pooling between accounts should only take place where the Court makes a pooling order pursuant to s 479(3) or 511 of the Act; such an order should only be made where it is appropriate; such an order will not be appropriate unless, at least, there is clear evidence of the mixing of funds across the relevant accounts and where it is not possible to work out precisely who is entitled to what moneys in particular accounts: *In the matter of MF Global Australia Ltd (in liq)* [2012] NSWSC 994 at [45]-[49], applying *In Georges (in his capacity as joint and several liquidator of Sonray Capital Markets Pty Ltd (in liq)) v Seaborn International (as trustee for the Seaborn Family Trust)* (2012) 87 ACSR 442 at [84]-[85].

5. There should be pooling within the Equities/ETO CSAs because, as appears from the Liquidators' CSA Report dated 22 December 2015 (**CSA Report**) and the Supplementary CSA Report dated 15 June 2016 (**Supplementary CSA Report**):

(a) BBY's books and records were organised by product lines, rather than by CSAs, and Equities and ETO CSAs are almost always grouped together;

(b) the "541 Account" was the primary trust account for *both* the Equities *and* ETO product lines;

(c) BBY's books and records do not appear to permit distribution of each of the Equities/ETO CSAs separately; and

(d) it would not be possible, or at least practicable, to calculate the portion of the balance of each Equities/ETO CSA attributable to any individual client.

No pooling between Equities/ETO CSAs and CSAs in any other product lines

The Liquidators' analysis does not warrant pooling between Equities/ETO CSAs and other CSAs

6. Putting to one side the "BBY Corp" transactions described in section 5 of the Supplementary CSA Report (including the transactions between the Equities/ETO CSAs and the Saxo CSAs), which are addressed below, the investigations set out in the CSA Report and Supplementary CSA Report appear to have identified:

(a) no transaction of interest between the Equities/ETO CSAs and the Futures CSAs that was not netted off by a matching transaction; and

(b) only one transaction of interest (in the amount of $300,000) from FX CSAs to the Equities/ETO CSAs, which occurred on 17 December 2014, and that amount ($0.3 million) was then paid, as part of a larger sum, from the Equities/ETO CSAs to the General Trust account ending 002 (an Other Trust account) on 18 December 2014.[1]

7. In relation to the "BBY Corp" transactions, the Liquidators do not purport to have conclusively determined whether client monies from the CSAs of non-Equities/ETO product lines were used for "Equity/ETO Funding Transactions" (which describe regular funding to the Equities/ETO business from sources described as "BBY Corp" (and the return of those funds)).[2]

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[1] See pages 45 to 46 of the Supplementary CSA Report. This transaction appears to be one of the "BBY Corp" transactions.

[2] See pages 35 to 38 of the Supplementary CSA Report.

8. On balance, the Liquidators' investigations provide insufficient support for a finding of mixing (or irreversible mixing) of any magnitude between Equities/ETO CSAs on the one hand and the CSAs of other product lines, on the other hand, so as to make a pooling order appropriate. On that basis, there ought not be pooling between the Equities/ETO product line CSAs and the CSAs of the other product lines.

Pooling the Equities/ETO CSAs with other CSAs would detract from the regulatory protections that apply to ASX-traded products

9. BBY was a market participant of the ASX market (operated by ASX) as well as a clearing participant of ASX Clear (the clearing house operated by ASX Clear Pty Limited (**ASXCPL**) which clears trades on the ASX market).

10. Prior to its insolvency and suspension from participation, BBY (as a market and clearing participant) was subject to a high level of regulation and supervision by ASX and ASXCPL as set out in the CSA Report.[3]

11. The relevant provisions include, without limitation:

    (a) section 4 of the ASX Clear Operating Rules, which imposes various obligations on clearing participants - in particular, sections 4.23 and 4.24 provide for a clearing participant's obligations in relation to trust accounts and CSAs, which obligations are in addition to (and supplement) the various obligations of a financial services licensee under Part 7.8 of the Act and Regulations;

    (b) broad powers of ASX and ASXCPL under section 5 of the ASX Operating Rules and section 19 of the ASX Clear Operating Rules to monitor and enforce compliance by participants (such as BBY) with the relevant Operating Rules (including rules concerning client monies); and

    (c) specific admission requirements in section 1 of the ASX Operating Rules and section 3 of the ASX Clear Operating Rules which market participants and clearing participants must satisfy, and continue to satisfy, in order to be admitted and stay admitted as such.

12. The regulatory purpose of those measures is to protect investors dealing with participants in respect of products that are traded on the ASX market and cleared through ASX Clear (**exchange-traded products**), and their ultimate objective is to preserve investors' confidence in those exchange-traded products as well as the ASX market and clearing facility on which they were traded and cleared.

13. In the case of BBY, those investors (that is, the intended beneficiaries of the protections under the ASX Operating Rules and ASX Clear Operating Rules) will be its Equities and ETO clients.

14. The regulatory purpose of the ASX Operating Rules and ASX Clear Operating Rules will be detracted from if client monies provided to BBY in respect of exchange-traded products (i.e. funds in the Equities/ETO CSAs) are pooled with funds provided in respect of other products (such as funds in the Futures and FX CSAs) that do not have the same protections.

Pooling the Equities/ETO CSAs with other CSAs would detract from the statutory policy behind the NGF

15. Pooling of the Equities/ETO CSAs may also detract from the statutory policy behind the NGF, namely to provide a comprehensive compensation scheme to retail clients investing in exchange-traded products so as to ensure that investors' confidence in the ASX market is maintained.

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[3] See pages 22 to 24 of the CSA Report.

16. As disclosed in the *BBY ASX, APX and International Trading Terms* dated March 2014 (**Trading Terms**):

(a) "[a]*s BBY is a Trading Participant of ASX, you may make a claim on the National Guarantee Fund (NGF) in the circumstances specified under part 7.5 of the Corporations Act and the Corporations Regulations*" (page 6);

(b) "*...the National Guarantee Fund (NGF) may apply, provided the loss is connected to the ASX market and is covered by the NGF claims provisions. The NGF claims provisions are set out in Division 4 of Part 7.5 of the Corporations Act and Regulations*" (page 6); and

(c) "*...unless the transfer was taken to have been effected by a market participant of ASX or other relevant Australian securities market or a clearing participant of ASX Clear, you have no claim arising out of the transfer against the national guarantee fund under the Corporations Regulations*" (page 17).

17. In general terms, under subdivision 4.9 of Part 7.5 of the Regulations, where a market participant of ASX or clearing participant of ASX Clear becomes "insolvent" at a particular time, and property was entrusted to that participant on behalf of a client at an earlier time in connection with the participant's securities business (that is, its financial services business of dealing in "securities", which generally exclude futures, FX and other non-equity products), that client may make a "property entrusted claim" against the NGF.

18. Pursuant to reg 7.5.71 of the Regulations, the total amount that may be paid out of the NGF in connection with property entrusted claims arising from BBY's insolvency is limited to $11.4 million (being 15% of the minimum amount of the NGF as at 17 May 2015). If the total value of property entrusted claims made by former BBY clients (and allowed by SEGC), plus any costs and interest payable on those claims, exceed $11.4 million, the compensation payable to individual BBY clients will need to be pro-rated and reduced accordingly.

19. If Equities/ETO CSAs are not pooled with CSAs in other product lines SEGC does not anticipate that the statutory cap will be exceeded. If Equities/ETO CSAs are pooled with CSAs in other product lines SEGC anticipates that there is a real prospect that the statutory cap will be exceeded (especially given the ongoing payments of legal costs and remuneration out of those CSAs). In that situation, compensation which those clients might receive from the NGF will be pro-rated and reduced accordingly. SEGC contends that such an outcome is contrary to the legitimate expectation that BBY clients who invested in exchange-traded products had or may have had (based on the statements in the Trading Terms set out above) that they would be compensated in accordance with the terms of the Act and Regulations. A pooling order in the present case would undermine investors' confidence in the compensatory scheme provided by the ASX market and therefore the legislative policy behind the NGF.

20. To the extent necessary, SEGC will also contend that the availability of compensation from the NGF to Equities/ETO clients should not be treated as a basis for, or a reason in favour of, pooling between Equities/ETO CSAs and the CSAs of other product lines. If funds of the NGF fall below the prescribed minimum amount, SEGC is required to consider appropriate actions, which may include requiring ASX or its participants to pay a levy to SEGC in order to raise funds.[4]

Saxo monies were not trust monies

21. SEGC will contend that, prior to 17 May 2015, clients in the Saxo product line (**Saxo clients**) were unsecured creditors of BBY; that BBY did not hold money on trust for its Saxo clients; and that any money paid from the Saxo CSAs should not be treated as trust money. On that basis, *even if* there were net movements of funds from Saxo CSAs to Equities/ETO CSAs, those fund movements do not constitute "mixing of trust funds" so as to justify pooling of the CSAs.

[4] See sections 889I and 889J of the Act

22. According to the *BBY Online Trader PDS* dated June 2013 (**PDS**),[5] which explains the terms of an OTC derivative product known as "BBY Contract" that was issued by BBY and was the only product available to, and traded by, Saxo clients:[6]

(a) moneys paid by Saxo clients to BBY for BBY Contracts were initially deposited into a client moneys trust account maintained by BBY (referred to in the PDS as the "BBY Trust Account");

(b) BBY was permitted by law to use moneys in the BBY Trust Account to pay itself for its hedge of Saxo clients' BBY Contracts and to meet obligations incurred by BBY in connection with margining or settling dealings in derivatives (including, but not limited to, BBY Contracts);

(c) pursuant to the *BBY Online Account Terms* dated June 2013 (**Online Account Terms**),[7] a Saxo client could not make a payment into the BBY Trust Account without also directing that all of those funds be withdrawn to pay BBY for credit to the client's trading account. BBY's general policy was that it would immediately withdraw from the BBY Trust Account all of the money deposited and pay it as "Margin" to BBY itself for the Saxo client's BBY Contracts; and

(d) moneys withdrawn from the BBY Trust Account to pay BBY became BBY's own moneys (and ceased to be held on trust for the client).

23. The PDS descriptions of BBY Contracts (and the treatment of client monies received by BBY in respect of those contracts) are consistent with the Online Account Terms as well as the relevant provisions of the Act and Regulations, particularly s 981A(2)(c) of the Act.

24. SEGC will contend, based on the above, that money paid out from the Saxo CSAs prior to 17 May 2015 was <u>not</u> trust money (but BBY's own money). Any trust that might have arisen pursuant to reg 7.8.03(4) only arose on 17 May 2015 and applies only to money held in the Saxo CSAs as at (or after) 17 May 2015.

No pooling between CSAs in the IB product line and CSAs in other product lines

25. The Liquidators' CSA Report and Supplementary CSA Report identified no transaction of interest between CSAs in the IB product line and CSAs in the other product lines. In the absence of any evidence of mixing (let alone irreversible mixing), pooling is not justified.

3 August 2016

Clayton Utz

James Hutton
Eleven Wentworth Chambers

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[5] According to the Client Application Form dated July 2014, by selecting the Saxo product line and signing the application form, a Saxo client acknowledges that: (i) it has received, read and understood the Online Account Terms and will be bound by all on them on acceptance of the application form; (ii) it understands that BBY Contracts are synthetic derivative products that are not exchange traded; and (iii) it has received, read and understood the PDS.

[6] See section 3.9 of the PDS.

[7] See section 4 of the Online Account Terms.