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Pocklington and Jewellers Association of Australia Limited

Memorandum of Advice

Jewellers Association of Australia Limited ("JAA") is an incorporated, unlisted, non-profit, registered Australian public company limited by guarantee, which has existed since 1931. For many years prior to 7 September 2016, Colin Pocklington ("Pocklington") was a director of JAA. The circumstances surrounding Pocklington's resignation as a director of JAA on that date give rise to the advice provided below.

I have been requested to closely, and impartially, scrutinise the matters relevant to the discharge of Pocklington's duties as a director of JAA, both with respect to the expressed concerns of the board of MA, and any other matters which, in my opinion, do, or are capable of impacting upon that broad issue.

Background

Pocklington's duties as a director of JAA are defined by:

1. the constitution of JAA;

2. the provisions of the Corporations Act 2001 (Cth) ("the CA"), and;

3. the general law with respect to directors' duties.

The Constitution of JAA

The current constitution of JAA appears to have been approved on 29 October 2015. The objects of JAA (clause 1.3) include, promoting and protecting the interests of participants within the jewellery industry, promoting unity and professionalism within the industry, establishing and maintaining professional standards and a common code of conduct within the industry, and promoting business interaction within the jewellery industry.

The constitution provides for two classes of member of JAA - general and associate members (clause 2). The former category is essentially, be definition, limited to entities with commercial involvement of one kind or another in the jewellery industry. Members of the former category are entitled to vote at meetings of the company - the latter are not.

One of the three subclasses of commercial members (clause 2.2(b)(iii) (CD is "buying group entity members who are buying group entities". Pocklington and Barry Jackson are the sole shareholders in, and directors of, jewellery and Gift Buying Services Pty Ltd ("IGBS"), which trades as Nationwide jewellers (Nationwide"). Pocklington became a director of JAA through IGBS's membership of JAA. Pocklington's standing to be a director of JAA has never been in issue, and assumes no significance for present purposes.

The constitution provides that JAA must have at least five and no more than six directors (clause 8.2), and for the composition of the board by reference to classes of membership (clause 8.3). The effect of the constitution is, broadly, that commercial jewellery industry interests will always dominate the board of all-all but the sixth "co-opted" director being required to be general members of JAA. The interstices of the constitution with respect to the appointment of directors require no further analysis for present purposes.

Clause 10 of the constitution is concerned with directors' duties and interests. The provisions reflect the nature of JAA, and recognise the composition of its boards of directors at any given time. A director is not disqualified from holding office by reason of "holding any office or place of profit or employment...or being a member or creditor of any corporation...or partnership", other than the company's auditor (clause 10.2(a)(i)]. Nor is a director disqualified by "entering into any agreement" with JAA, "unless it means that the director has an actual conflict of interest with the objects of the company" (clause 10.2(a) (ii)). The broad scope of the objects of JAA, and composition of its board at any time appear to create considerable potential for possible or apparent conflicts of interest.

The constitution obliges directors to comply with a number of national governance standards (clause 10.2(b) and (CD. These do little more than reiterate the requirements of the CA and the general law: acting with reasonable care and diligence, acting honestly and fairly in the best interests of the charity, not misusing their position or information they gain through it, disclosing conflicts of interest, ensuring financial affairs are managed responsibly and avoiding insolvent operations.

Clause 10.3 of the constitution is concerned with declarations of interests by directors. A director who is "in any way, interested in a contract or proposed contract" with JAA, or "holds any office or possesses any property or enters any agreement as a result of which duties or interests might be created which are directly or indirectly in conflict" with the director's duties or interests as a director, must "declare that fact and the nature of the interest, or the nature, character and extent of the conflict" at the first board meeting after the relevant event occurs. Significantly, and not unsurprisingly having regard to the matters to which I have referred above, an obligation to disclose pursuant to clause 10 does automatically, or necessarily, preclude the board of JAA from resolving to enter into an agreement which entails the actual or potential conflict of interest which gave rise to the duty to disclose.

The constitution effectively imports $191 and 5195 of the CA. The former is in addition to the provisions of clause 10.3 of the constitution by virtue of $193 of the CA, and requires notice to be given of a "material personal interest". The term is not defined in the CA. The learned authors of "Company Directors: Principles of Law and Corporate Governance", suggest, at p.345, that materiality is "likely to depend on whether the interest has a realistic capacity or propensity to influence the director's decisions in the administration of the company's affairs". Although the issue is not uncomplicated, for present purposes it can be assumed that a material interest would be "personal" within 5191 of the CA (see Kriewaldt v Independent Direction Ltd (1995) 14 ACLC 73).

Section 195 of the CA prohibits a director of a public company who has a material personal interest in a matter which is being considered at a directors' meeting may not be present during consideration of, or vote on the matter. The exceptions provided by 5195(2) of the CA do not assume significance, as it is not suggested that Pocklington attended, or voted at any meeting at which matter falling within 5191 of the CA was considered and/or voted on.

Clause 10.5 provided an "obligation of secrecy" or confidentiality with respect to the "transactions and affairs" and accounts of JAA.

The Corporations Act

In addition to 55191 and 195 of the CA, a number of other provisions of the CA potentially assume significance for present purposes. The provisions of Chapter 2D, Division 1 are concerned with the "general duties" of directors, and certain other company "officers". Although substantially "codifying" the general law, these provisions do not displace those principles, with which they are consistent in any event (CA, 5185).

Section 180 of the CA imposes an obligation on directors to discharge their duties with the degree of "care and diligence" that a reasonable person in that position, in that company would exercise. Section 180(2) creates the "business judgment rule", the requirements of which are satisfied if:

1. a judgment is made in good faith for a proper purpose;
2. the director does not have a material personal interest in the subject matter of the judgment, and;
3. the director rationally believed that the judgment was in the company's best interests, which is deemed to be a "rational" belief, unless the belief is one which no reasonable person in that position would hold.

A 'judgment' for the purposes of $180 is a "decision". A director who does not vote on a board resolution has not made a judgment which could breach the requirements of the rule.

Section 181 of the CA imposes an obligation on directors to act in good faith in the best interests of the company, and for a proper purpose. The importance of not voting on any board resolution which involves an actual or potential conflict of interest on the part of a director assumes significance in view of the terms of 5181 - if Pocklington had voted in favour of a board resolution by JAA to hold a significant event, knowing that Nationwide would not support it, that may not have been acting in the best interests of JAA, or in good faith, or for a proper purpose.

Section 182 of the CA prohibits improper use of his/her position by a director to gain an advantage for themselves or someone else, or to cause detriment to the company. Section 183 of the CA extends that prohibition to information obtained by being, or having been a director of the company. The causal requirement with respect to detriment is to be remembered - it is not sufficient that detriment resulted from a decision.

The general law

The constitution of JAA, and the provisions of the CA largely overlap, and overlap the general law with respect to directors' duties.

For present purposes, reference to the "five fiduciary rules" emerging from the authorities may be most instructive. The rules are:

1. the conflict of interest rule - a director must not in any matter falling within the scope of his office have an interest that conflicts or may possibly conflict with his duty to the company, except with the company's fully informed consent;
2. the conflict of duties rule - a director must not in any matter falling within the scope of his office, have an inconsistent engagement with a third party, except with the company's fully informed consent;
3. the misappropriation rule - a director must not misappropriate the company's property for personal or a third party's benefit;
4. the profit rule - a director must not use his position for personal or a third party's possible advantage, except with the company's fully informed consent, and, therefore account to the company for any profit or gain made in connection with the fiduciary office;
5. the business opportunity rule - a director, at least if engaged full-time in the company's service, must not divert any profit-making opportunity, in the same line of business as the company's present or prospective business to himself or a third party, without the company's fully informed consent.

As is readily apparent, the rules overlap. They are most readily, and usually invoked in cases involving companies which are intended to operate for profit. JAA is a non-profit company whose voting members all have their own commercial interests. Its board is potentially, legitimately, dominated, or at least influenced by the "big players" in the jewellery industry. Without intending to be cynical, or dismissive of the objects of JAA, self interest is a logical and justifiable basis

for membership of the company, and participation in its management. In these circumstances, in my view, the potential for conflicts of interest are always likely to be substantial. The reality is that, forced to choose between the best interests of JAA, and his own commercial interests, a director is likely to preference the latter.

At the risk of over simplification of a complex issue, the effect of the constitution of JAA, the provisions of the CA discussed above, and the fiduciary rules (particularly 1, 2, 4 and 5] is in my view that:

1. a director of JAA must be vigilant to identify any possible decision by JAA, or his own interests (at their broadest), which potentially advantages the latter over the former;
2. a director finding himself in that position must exercise his powers of control over his own, or related, interests in a manner which results in those interests not realising the potential advantage over the interests of]AA, which may in itself be a breach of the director's duties to his own interests, or;
3. a director faced with that dilemma immediately, and prior to any decision being made by the board of JAA, or, the company at a general meeting, inform JAA of the potential conflict of interest, and;
4. refrain from voting on, or attending any board meeting at which the board of JAA was considering resolutions which potentially involved conflicting interests, or;
5. if the potential conflict of interest appears indissoluble or enduring, the director should probably resign from the board of JAA.

The present circumstances

For some years, and including 2016, annual international jewellery fairs were held at Darling Harbour in Sydney ("the fairs"). The fairs were organised, promoted and managed by Expertise Events ("EE"), 3 company which specialised in event management, on behalf of JAA. That arrangement was governed by a contract between JAA and EE. If the directors were dissatisfied with EE, or its performance prior to 2016, that does not appear to have been the subject of board deliberations. The minutes of the board of JAA of 19 May 2016 (item 5) do not suggest any dissatisfaction with EE's performance. EE conducted the August 2016 fair, which was apparently commercially successful for all involved. The contract apparently expired at the end of September 2016. JAA apparently had the right to extend the contract. It appears not to have done so.

Save with respect to the jewellery fairs referred to above, EE has never had any commercial, or contractual connection with Pocklington, or with any interest of his. The closest to any such association was the submission of a quote by Nationwide Travel, a company related to Pocklington, to provide accommodation for an optical fair which EE was to conduct in 2013. The quote, submitted in 2012, was not accepted.

The fairs provided for jewellery industry and consumer trade, on a large scale. Nationwide, and the other two largest players in the jewellery industry (Leading Edge and Showcase), the latter of which was also represented on the board of JAA, were provided with space at the fairs without being required to pay for such space, although the cost of fitting out such space was born by them. In short, the arrangement was viewed by JAA as being significantly beneficial to it, in ways which do not need to be detailed, and are not suggested to have previously assumed significance.

By May 2016, for reasons which probably do not matter, a number of the directors of JAA had determined that JAA would "run its own fair in 2017 in Sydney", according to the minutes of the board meeting held on 19 May 2016.

The minutes of that meeting record the resolution of the board that five of JAA's six directors, including Pocklington, "have a conflict of interest due to their involvement as exhibitor, in the Jewellery Fairs organised" by EE. I presume that to be by virtue of the contractual arrangements between EE and the interests of those five directors, which had been in existence in essentially the same terms for years.

The minutes note that Pocklington abstained from voting on the resolution to run JAA's "own fair". I am instructed that Pocklington informed the meeting that the board should not assume that "we will be part of it". Whether others would choose to recall his saying so is unknown. The minutes do not record more than Pocklington's abstention from voting.

Under the heading "Action items", the minutes of the board meeting identify a number of reasons for the proposed break away from EE. Included in the list of such items, and, at least consistent with Pocklington's assertion that he did not expressly or impliedly convey support for the proposed JAA fair, was the notation, at "k", "include floor plan with buying groups (seek confidential decision from buying groups in the near future)". The buying groups are Nationwide, Showcase and Leading Edge.

As mentioned above, preparing for, and conducting the 2016 fair appears to have been the priority between the May board meeting, and 8 September 2016, the date previously set for the next meeting. On 7 September 2016, Pocklington emailed the board, advising that Nationwide would be continuing with the EE fair, rather than the proposed JAA fair. Pocklington stated that he considered it important to indicate Nationwide's position prior to the meeting of JAA's board, and that, in the circumstances, he had a "significant commercial conflict", and should not be "part of the board discussion tomorrow".

On 9 September 2016, in response to an earlier brief email from the executive director of JAA, Pocklington tendered his resignation from the board of JAA.

Later the same day, and in response to Pocklington's offer to resign from the board, the chairman wrote/emailed him, confirming that the resignation had been accepted, and effectively suggesting, albeit in reliance upon some curiously illogical grounds, that Pocklington had breached his duties as a director of JAA, and that his previous membership of the

board “constituted an undisclosed conflict of interest”. The reference to the resolution with respect to conflicts of interest on the part of five directors recorded in the May board minutes was not referred to by the chairman, notwithstanding that he was one of the conflicted five. The logic of the letter appears to be that, by staying with EE, Pocklington was impermissibly conflicted, whilst the other four directors were not, presumably because they were not staying with EE.

The chairman’s letter requested disclosure of a number of commercially sensitive documents by Pocklington. By letter dated 12 September 2016, Pocklington replied to the chairman‘s letter, but provided no documents. In his response, Pocklington set out the basis of Nationwide’s arrangements with EE, which he asserted the board had been well aware of for many years. I understand that the arrangements are verbal, and not recorded in any document in any event. Nationwide’s arrangements with EE are the same as EE has with the other two major buyer groups. In my view, Pocklington thus fully responded to the first of the chairman’s requests. The request by JAA was not inappropriate in the circumstances.

Albeit in a different context, in the course of his response, after detailing the terms of Nationwide’s arrangements with EE, Pocklington stated that “the above is the full extent of the verbal agreement with EE”, but did not expressly state, as I am informed is the fact, that there were no other agreements of the kind to which the chairman’s second question was directed. Similar observations apply to the third of the Chairman’s questions. In the absence of a reasonable basis for asking them, and I perceive none, the second and third questions were not, in my View, questions which Pocklington was obliged to answer. In any event, the answers to both would have been in the negative.

The chairman responded to Pocklington’s letter on 14 September 2016. The letter commenced with a series of acknowledgments which would not readily coalesce with suggestions of breach of Pocklington’s duties as a director of JAA - if they were ever made. The letter proceeded however to paraphrase, inaccurately, the terms of Pocklington’s email to the board of 7 September 2016, by suggesting that the conflict was referrable to Nationwide’s “business association” with EE. With hindsight, Pocklington might have better expressed himself by referring to a “potential” significant commercial conflict if he were to remain on the board of JAA when he knew that his interests would support what might be viewed as a rival fair to that proposed by JAA, rather than any conflict of interest which then existed, or, but for JAA’s split from EE, was likely to arise. If a conflict of interests on Pocklington’s part existed at that time, it had existed for years, as it had for four other directors of JAA, as the May board meeting minutes recorded. The balance of the chairman’s letter implies that the board accepted the clarification which Pocklington had provided on 12 September 2016.

The next development seems to have occurred on 23 September 2016, when the chairman emailed Pocklington, and sought to meet with him “personally to chat”. Pocklington responded, by email dated 26 September 2016, suggesting that the “first step” should be an apology from JAA.

Later the same day, the chairman emailed Pocklington, declined to secure any apology, raised the “possibility of other conflicts which may not have been disclosed”, and suggested that Pocklington’s “stated conflict of interest actually extends beyond the Jewellery Trade Fair, which you have declared and which no one is disputing”. Pocklington’s undoubtedly sound legal advice was not to participate in the proposed “chat”. As will be seen, in my view, the most important statement by the chairman in the correspondence/ email trail is the acknowledgment that JAA accepted Pocklington’s statements with respect to the only contractual arrangements which had existed or were in existence between his interests and EE.

Although there was further, and apparently uneventful correspondence concerning possible defamation proceedings, I gather that JAA has lost interest in the conflict of interest controversy.

Discussion

The fact that JAA recorded its acceptance of Pocklington’s clarification, or explanation with respect to the “Jewellery Trade Fair”, and its failure to even hint at the nature, much less extent, of other “possible” conflicts, creates some difficulty in providing the comprehensive advice which has been sought from me.

For the reasons noted above, irrespective of the drafting intention, corporate governance of JAA is likely to be fraught by possible conflicts between the duties and interests of directors by reason of the provisions of its constitution. The minutes of the board meeting of 19 May 2016 graphically illustrate that reality.

For reasons which are not difficult to understand, and are sound, the provisions of the constitution of JAA referred to above do not mean that a director’s commercial interests cannot ever be contrary to the interests of JAA. Provided that the director promptly, fully and accurately discloses the actual or potential conflict of interest, and abstains from participating in the board‘s consideration of any issue involving a conflict of interests, and abstains from voting on any resolution with respect to it, the director will not be in breach of his duties under the constitution.

Pocklington promptly disclosed the conflict of interest which he perceived had arisen in View of JAA’s apparent desire to split from EE and run its own fairs in future. To the extent that JAA has revealed what it perceives to be the source of the conflict of interests, Pocklington’s explanations have been accepted. In my view, Pocklington acted with propriety in recording at the May meeting that JAA should not assume that his commercial interests would support JAA’s fair. His resignation from the board in September, prior to the board meeting, by which time Pocklington perceived that his loyalties were divided, or about to be divided, was in my view proper. Although, having regard to the constitution, and JAA’S subsequent acceptance that Pocklington had satisfactorily explained the conflicts which troubled the board, he may properly have remained a director, albeit needing to abstain from board deliberations and votes with respect to JAA’s major annual activity in the foreseeable future, Pocklington’s decision to resign was sound, and possibly in JAA’s interests.

By his resignation from the board, Pocklington avoided potentially offending $180 of the CA. Had he taken part in consideration of, or voted on any resolution concerning the fairs, Pocklington may have breached 5180 of the CA, and probably would have breached $195 of the CA. Neither of those things occurred.

Nothing to which JAA has referred establishes a breach of 5181, 5182 or $183 of the CA in my view.

As suggested above, had Pocklington voted on the resolution to split from EE, he may have breached one or more provisions of $181, whichever way he voted, but particularly if he had voted to split, knowing, or suspecting that his commercial interests would not be supporting the JAA fair, rather than the EE fair. Whilst still a director of JAA, and as soon as he perceived that he was conflicted, Pocklington acted in good faith, and in what he reasonably perceived to be in JAA's interests by making clear, in May 2016, that Nationwide might not be part of any separate JAA fair. He did so for a proper purpose— not allowing JAA to mistakenly assume that Nationwide would be part of JAA's plans. As soon as he knew that Nationwide would not be part of JAA's plans, and before JAA was committed to any such plans, Pocklington made that fact clear to the board, and resigned from the board.

I have not seen anything, or read any suggestion, that Pocklington used his position to gain an advantage in breach of 5182 of the CA. The board of JAA accepted that he had not, or has not persisted with any suggestion that he had. Nationwide received no benefits or advantages from EE which were unduly favourable to Nationwide compared with the other two majors, or commercially inappropriate or unjustifiable. The arrangements of all three majors had been known to, and approved by, or at least acquiesced in, by the board for many years. Nor does it seem to be suggested that EE benefited improperly or excessively as a result of Pocklington's directorship of JAA.

JAA may suggest, but has not to date, that Pocklington's conduct caused JAA detriment. His decision to remain with the BE fair after 2016 may cause JAA detriment in View of the importance of Nationwide to the success of any jewellery fair conducted in Sydney. That however would be the result of Pocklington exercising his powers as a director of IGBS, to which he owed fiduciary duties as a director, not to be part of the JAA fair, rather than any breach of director's duty to JAA.

Other than by suggesting, erroneously in my view, that Pocklington was bound to support JAA's fair, irrespective of his business judgment with respect to the commerciality of doing so, I cannot see how his actions could fall within the scope of 5182 of the CA. Different considerations might arise had Pocklington, before or after he resigned from the JAA board, lobbied entities who might participate in the JAA fair in preference to the HE fair to support the latter, but no suggestion of that nature has arisen, or been hinted at. Pocklington should of course be diligent not to do anything of that kind, consciously or unconsciously. Had Pocklington remained on the board of JAA, there would have been the potential for him to have breached 5183 of the CA, even if he did not attend during consideration of matters relating to the fairs, much less vote on resolutions with respect to them, by reason of information which was directly or indirectly related to the fairs becoming known to him. Pocklington's resignation averted those risks.

There is no suggestion that Pocklington has used, or could use, information about JAA, a non-profit company in any event, in a manner which offended $183 of the CA.

The matters discussed above also have application to the "five fiduciary rules". As the rules, and particularly rules 1, 2, 4 and 5, make clear, a director may permissibly have a conflict of interest and duty- the decisive factor is the company's fully informed consent to such conflict. JAA's constitution adopts those rules. The nature of JAA, the composition of its board, and the reality that directors of JAA do not have to, and cannot be expected to place the interests of JAA above their own commercial interests, mean that the current controversy was always likely to arise.

In my view, by resigning from the JAA board, when he did, and in the circumstances in which he did, Pocklington averted any possible breaches of the rules.

Conclusion

I could take up considerable space attempting to second guess what unstated potential conflicts of interest and duty JAA may have imagined in September 2016. Doing so would be neither useful, nor instructive. It could reasonably be assumed that, if JAA considered that it had any basis for complaint with respect to Pocklington's conduct as a director, it would by now have revealed that basis.

I have earlier (pages 4-5) endeavoured to summarise the scope of the duties of a director of JAA with respect to actual or potential conflicts of duty and interest. In summary, my views are:

1. the director was vigilant to identify a possible decision by JAA which potentially disadvantaged JAA, albeit not necessarily to the advantage of Pocklington's interests over those of JAA. For all anyone could know, Pocklington's decision not to support JAA's fair may be proven to be disadvantageous to his interests. JAA's interests may be advantaged by the split from EE;
2. the director's actions did not result in his interests being advantaged over those of JAA. Time might, or might not, vindicate Pocklington's judgment, but it cannot reasonably be suggested that, if he is proven right, and JAA would have been better off staying with EE, its detriment was in some way caused by or contributed to by Pocklington's decision not to go with the JAA fair;
3. the director promptly, and accurately, informed the board of the dilemma which he perceived, and resigned from the board, rather than risk allowing his own interests to deflect him from his duty;
4. the director fully discharged his statutory, and constitutional, obligations when faced with a "material personal interest";

5. to the extent that the potential conflict of interest appeared indissoluble or enduring, the director resigned from the board.

In “Fiduciary Obligations”, at 219, Finn suggests that the definition of “interest” for the purposes of the conflict of duty and interest rule, in “rudimentary terms” “signifies the presence of some personal concern of possible significant pecuniary value in a decision taken, or a transaction effected, by a fiduciary”. As was the case with Pocklington, there did not need to be the prospect of pecuniary advantage or disadvantage, the prospect of “significant pecuniary value” was sufficient. In my view, there was that prospect, and Pocklington’s response to it was consistent with his duty to JAA. The fact that he may not have understood, or articulated it in those terms is not the point— his actions were as they should have been.

Finn also suggests, again at 219, that there is a “specific problem area in interests”, being “the indirect interest created through membership in a company”, such as the present controversy involved. The law recognises that the conflict rule “must be applied realistically to a state of affairs which discloses a real conflict of duty and interest and not to some theoretical or rhetorical conflict” (Boulting vA.C.T.A.T (1963) 2 QB 606 at 638). In my View, Pocklington’s response to a real potential conflict of duty and interest was as the law required. I have not been made aware of any other allegation or circumstance which could be considered more than a theoretical or rhetorical conflict.

0n the evidence available to me, JAA does not have, and has not had, reasonable grounds for suggesting, or implying that Pocklington failed to declare a conflict of duty and interest to the board of JAA whilst he was a director of JAA.

Ian Coleman SC

Culwulla Chambers

9 March 2017

** NOTE: This pdf has been recreated by Jeweller from the original in order to upload to the website in a more readable format. In doing so, the editor corrected a spelling error at page 3, paragraph 9. The original legal advice read: “The minutes not that Pocklington abstained from voting…” and it has been changed to: “The minutes note that Pocklington abstained from voting…”. In some cases the text incorrectly read IAA instead of JAA.*