HERBERT SMITH FREEHILLS

RIO TINTO AGREES A$750,000 PENALTY WITH AUSTRALIAN WATCHDOG OVER MOZAMBIQUE DISCLOSURE BREACH

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Legal Briefings – By **Tony Damian and Amelia Morgan**

Long-running dispute ends as ASIC drops claims against Rio Tinto's former executives and company agrees fine

ASIC and Rio Tinto Limited (Rio Tinto) recently reached a settlement regarding an alleged continuous disclosure breach by Rio Tinto in relation to its Mozambique coal assets following the company's 2011 acquisition of Riversdale Mining Limited (including a $750,000 pecuniary penalty).

IN BRIEF

- In a judgment delivered on 7 March 2022, and following the admission made by Rio Tinto, Justice Yates of the Federal Court of Australia declared that Rio Tinto had contravened its continuous disclosure obligations by failing to disclose that its Mozambique coal assets were no longer economically viable as long-life, large-scale, "Tier 1" coking coal resources from late December 2012 to mid-January 2013.
- Yates J ordered that Rio Tinto pay the pecuniary penalty of $750,000 agreed with ASIC, noting the maximum penalty for a single breach of the continuous disclosure provisions at the time was $1 million (but is now significantly larger in circumstances where the entity has knowledge that, or is reckless or negligent with respect to whether, information is materially price sensitive).
- As part of the settlement, the proceedings against the former Chief Executive Officer and Chief Financial Officer of Rio Tinto were dismissed.

- The settlement follows the $100,000 penalty paid by Rio Tinto to ASIC in 2008 in relation to an infringement notice served by ASIC alleging Rio Tinto had failed to comply with its continuous disclosure obligations in relation to its acquisition of Alcan Inc.

- The matter is an example of ASIC's continued willingness to prosecute alleged breaches of continuous disclosure obligations, noting the recent proceedings by ASIC against Austal Limited and GetSwift Limited.

BACKGROUND

The facts and admissions that had been agreed between the parties in relation to the matter are summarised below.

In 2011, Rio Tinto acquired Riversdale Mining Limited, which was comprised, principally, of mining and exploration assets in Mozambique and also acquired tenements and exploration licences adjoining the Riversdale assets.

Rio Tinto's annual report for the year ending 31 December 2011 released in March 2012 noted that:

> *"The Moatize basin in Mozambique is home to one of the best undeveloped coking coal resources in the world. Rio Tinto has the largest licence holding in that region and owns Tier 1 resources which are long life, will be cost competitive and will have substantial expansion options. Rio Tinto plans to significantly grow these assets and sees this region providing a development opportunity that is long term and will achieve sustainable growth over a 50-year-plus timeframe. Whilst saleable production will initially be constrained by existing rail and port infrastructure, feasibility studies into infrastructure solutions and mine expansions at Benga and the adjacent Zambeze Project are continuing in 2012."*

Rio Tinto's annual review for the same period also noted that:

> *"(a) We are well placed to capitalise on our leadership position. Our portfolio includes some of the world's best assets – from our world-class iron ore operations in Australia to the huge potential of our growth projects there and in Mongolia, Guinea and Mozambique;*
>
> *(b) During 2011 we completed the acquisition of Riversdale, which has now been renamed Rio Tinto Coal Mozambique. This provides a substantial Tier 1 coking coal development pipeline in the emerging Moatize Basin;*
>
> *(c) We continue to grow our world class portfolio of energy assets through the development of the recently acquired Hathor and Riversdale projects and increasing production at existing operations;*

(d) Our strategic investment in the highly prospective Moatize Basin in Mozambique gives us access to one of the largest undeveloped coking coal regions in the world and underlines our commitment to Africa;

(e) Through the development of Mozambique's massive coal reserves we can help meet that demand and contribute to the transformation of the country's economy."

In addition, from 8 August 2012 to 17 January 2013, the parties agreed that Rio Tinto publicly represented, including in its 2012 half-year report that:

- the company's coal projects in the Moatize Basin were highly prospective;
- there was an opportunity to grow and develop a world class basin of high quality coking coal through the relevant projects and tenements; and
- the relevant projects and tenements were long-life Tier 1 coking coal resources.

In December 2012, an internal report was made available to executive officers of Rio Tinto which concluded that the exploration and development potential of the Mozambique mining assets was not as Rio had indicated in the representations above. However, the substance of the adverse findings and conclusions about the Mozambique assets was not announced to the ASX until 17 January 2013.

REASONS FOR THE COURT'S JUDGMENT

CONTINUOUS DISCLOSURE CONTRAVENTION

Rio Tinto admitted (and the Court was satisfied on the basis of the agreed facts), that Rio Tinto contravened its continuous disclosure obligations by failing to disclose the adverse findings and conclusions regarding the company's Mozambique coal assets in the internal report until 17 January 2013.

In particular, from December 2012, the parties agreed that Rio Tinto was aware that:

- there was a reduction in expected recoverable and mineable volumes of coking coal, or reduced degree of confidence in the potential economic extraction of the coal deposits from the relevant projects and tenements;
- the quality and quantity of the relevant coal resources was not as previously expected;

- the coal projects were not highly prospective;
- the relevant projects and tenements did not provide an opportunity to grow and develop a world class basin of high quality coking coal; and
- the relevant projects and tenements were no longer economically viable as long-life, large-scale, Tier 1 coking coal resources.

It was agreed by the parties that this information was not generally available for the purpose of section 676 of the Corporations Act but, if it had been, was information that a reasonable person would have expected, to have a material effect on the price or value of Rio Tinto's securities. It was also agreed that the contravention was "serious" for the purpose of the Corporations Act.

The Court pointed to the agreed facts that:

- the internal report was provided to Rio Tinto's executive officers;
- its contravention occurred over a period of almost a month; and
- during the period in which Rio Tinto was required, but failed, to notify ASX of the relevant information, approximately 31 million shares (with a total value of approximately $2 billion) were traded on the ASX.

Interestingly, the Court did not discuss the effect of the 17 January 2013 announcement (which disclosed an expected impairment of Rio Tinto's Mozambique assets, amongst other things) on Rio Tinto's share price. In particular, it is interesting to note that Rio Tinto's closing share price on 17 January 2013 (noting the announcement appears to have been released about 6.30pm AEST post-market close) was $64.60 and its opening share price on 18 January 2013 was $65.50.

PECUNIARY PENALTY

ASIC and Rio Tinto agreed that Rio Tinto would pay a pecuniary penalty of $750,000 (noting the maximum statutory penalty for a single contravention of the continuous disclosure provisions, as a 'financial services civil penalty provision' at the time, was $1 million). However, the Court was required to be satisfied that the relief was appropriate in all the circumstances.

The Court noted the purpose of a civil penalty in promoting the public interest in statutory compliance, that the contravention was "serious" for the purpose for the Corporations Act, and other relevant factors submitted by the parties being:

- Rio Tinto's standing as a mining and metals company;
- Rio Tinto's market capitalisation;
- the fact that the contravention occurred over almost a month and that during the period in which the contravention occurred a substantial number of shares were traded; and
- that the internal report was received by executive officers of Rio Tinto.

ASIC also agreed there were a number of mitigating factors, including that the contravention was not deliberate or reckless, did not arise out of a failure to exercise due care and skill and that no officer or employee of Rio Tinto knowingly, wilfully, fraudulently or dishonestly contravened any legal obligation (in this regard, see below regarding the 2019 changes to the continuous disclosure regime in the Corporations Act). It was further noted that Rio Tinto had not previously been found to have breached its continuous disclosure obligations.

It was noted that the parties had agreed that Rio Tinto had assessed the implications of the internal report carefully, but did not appreciate that it was necessary to notify ASX of the information (which was submitted to be an inadvertent error, noting the internal processes in place to ensure Rio Tinto complied with its continuous disclosure obligations).

In light of these factors, Yates J was satisfied that the $750,000 pecuniary penalty was appropriate relative to the maximum statutory penalty that could be imposed.

COMMENTARY

The matter is an example of ASIC's continued willingness to prosecute alleged breaches of continuous disclosure obligations, noting significant market misconduct remains an enforcement priority area for ASIC.

For example, in 2021, ASIC commenced proceedings against Austal Limited for continuous disclosure contraventions with regards to earnings guidance relating to its US shipbuilding business. In addition, late last year, GetSwift Limited was found by the Federal Court to have contravened its continuous disclosure obligations, following the case commenced by ASIC in 2019.

The pecuniary penalty imposed on Rio Tinto in this matter was only $750,000 (in light of the $1 million statutory maximum penalty that existed at the time), noting it was agreed by the parties that the contravention was not deliberate, reckless and did not arise out of a failure to exercise due care and skill.

It is important to note, however, that following changes made to the Corporations Act, if an entity knows, or is reckless or negligent with respect to whether, information would, if it were generally available, be materially price sensitive, the maximum pecuniary penalty for companies for a breach of continuous disclosure obligations is significantly larger (although civil penalty liability for entities no longer exists where the requisite knowledge, recklessness or negligence does not exist). In particular, in such circumstances, a company will be liable for up to the greater of currently $11.1 million, three times the benefit obtained and detriment avoided or 10% of annual turnover (currently capped at $555 million). As such, if a contravention is found to have occurred and the requisite fault aspect and other required conditions are satisfied, a breach of the continuous disclosure provisions in the Corporations Act could have a much larger financial impact for disclosing entities.

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If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.

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