

Our defamation laws might have let Enron get away with it

The law
A defamation claim is a quick, cheap, tax-deductible way for a company to shut critics up. That shouldn't be the case.

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The hurricane ripping through Blue Sky Alternative Investments is showing no signs of easing – but the challenges faced by our fourth estate in accurately reporting on this controversy are unacceptable and should prompt a radical review of Australia's defamation laws.

The idea that criticism of a company may involve imputations about a director personally leaves our media hamstrung. This should be ringing alarm bells for the efficient operation of markets and informed discourse on company performance.

After Glaucus released a public report and shorted the company in a move that wiped two-thirds off Blue Sky's market cap, analysts started comparing Blue Sky shares to a pair of dress shoes from Aquila (which Blue Sky coincidentally owns): they looked like quality when you purchased them, but they were never going to last.

While most of the Blue Sky coverage has focused on the company's failure to meet its obligations to the market, of particular interest is the involvement of John Hempton, Australia's most recognised short-seller. Hempton was reported in *AFR Weekend*'s Chanticleer column of April 6 to have offered unsolicited advice to Blue Sky executive director Elaine Stead via direct message on Twitter.

The parts of Hempton's advice that made it into the Chanticleer column after the *Financial Review*'s legal checks were uncontroversial and, unsurprisingly, spot on. Hempton called for Stead to seek independent advice. Should there be any suggestion of foul play, Hempton told Stead to call on her colleagues to resign and for the board to be replaced. Should they refuse, it would fall upon her to resign.

But what is far more intriguing than this common-sense recommendation, is *AFR Weekend*'s (quite justified) refusal to republish most of the 80 messages from Hempton to Stead for fear of being sued for defamation.

These laws were not designed to inhibit free sharing of information about companies, but that is precisely what they do.

This raises a serious question: are our defamation laws depriving the market of information that it needs to deliver efficient market outcomes?

In Australia, the general rule is that only individuals can be defamed. However, market participants still operate in a legal straitjacket when speaking about corporations. They are too frightened of publishing strong criticism of a company because that criticism may involve imputations about a director personally.

Under the uniform defamation legislation, it is a defence to the publication of defamatory matter if the defamatory imputations are substantially true. But the burden of establishing the truth lies on the defendant. The inevitable result is that market participants are hesitant to make their views known to the market. The threat of defamation is always looming.

The case of Quintis is a good example. In 2013, TFS Corporation, the predecessor to Quintis made threats of defamation to silence two shareholders who questioned the independence of the board and alleged improper conduct. Coincidentally, four years later Glaucus issued a research report describing Quintis as a "Ponzi scheme" and ran a successful short-selling campaign.

That Glaucus report was two years in the making and was not the first of its kind. Taylor Collison prepared an earlier report called "Foray Into Sandalwood Accounting" that foreshadowed troubled performance for Quintis and inspired Glaucus to step up research of its own.

The Australian legislative environment creates an information asymmetry and imbalance that impairs the efficient operation of the market. This is the opposite to the United States, where short-sellers take megaphones to Wall Street and engage the market without fear of retribution. In many instances, US defamation law reverses the burden of proof so that statements are presumed to be true unless proved otherwise.

If the great short-selling stories of companies such as Enron and Valeant Pharmaceuticals had been set in Australia, our defamation laws may have got in the way. These laws were not designed to inhibit the free sharing of information about companies and their performance, but that is precisely what they do. A defamation claim is a cheap, convenient and tax-deductible way for companies to silence their critics.

The burden of proof should be reversed for statements relating to the performance of public companies. If the law operated in that way, the likes of John Hempton may feel more comfortable about sharing their views in broad daylight. If we want our market to operate efficiently and optimally, it is time for some blue sky thinking on Australia's defamation law.

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