# SUPREME COURT OF QUEENSLAND

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| CITATION: | *Australian Securities and Investments Commission v Cycclone Magnetic Engines Inc & Ors (No 2)* [2009] QSC 201 |
| PARTIES: | **AUSTRALIAN SECURITIES AND INVESTMENTS COMMISSION**<br>(applicant)<br>**v**<br>**CYCCLONE MAGNETIC ENGINES INC**<br>(first respondent)<br>and<br>**MICHEAL PETER NUGENT**<br>(second respondent)<br>and<br>**ROBERT GEORGE McCLELLAND**<br>(third respondent)<br>and<br>**STEVEN VINCENT FOSTER**<br>(fourth respondent) |
| FILE NO/S: | BS 2655 of 2007 |
| DIVISION: | Trial Division |
| PROCEEDING: | Civil Trial |
| ORIGINATING COURT: | Supreme Court of Queensland |
| DELIVERED ON: | 31 July 2009 |
| DELIVERED AT: | Brisbane |
| HEARING DATE: | 1 April 2009 |
| JUDGE: | Martin J |
| ORDER: | |

**Introduction**

**1. In this Order:**

**(a) the "Business Plan" means a document published by the First Respondent, Cycclone Magnetic Engines Inc. ("CME") entitled "Business Plan";**

**(b) The “engine” means the Cycclone Magnetic Engine as described on the website, being an engine which purportedly operates through the use of permanent magnets to supply mechanical power on demand without the need for external fuel input;**

**(c) the "Website" means a website conducted by CME.**

**Declarations**

**2. It is declared that the First Respondent:**

**(a) in breach of section 1041H of the *Corporations Act 2001* (Cth) ("the Act"), has engaged in conduct in relation to a financial product that was misleading or deceptive, or likely to mislead or deceive, in that the First Respondent represented on the Website that the engine worked when such an engine could not work.**

**(b) in breach of section 12DA of the *Australian Securities and Investments Act 2001* (Cth) ("the ASIC Act"), has in trade or commerce, engaged in conduct in relation to financial services that was misleading or deceptive, or likely to mislead or deceive, in that the First Respondent:**

**(i) on the Website, represented that the engine worked when such an engine could not work;**

**(ii) in the Business Plan, when there were no reasonable grounds to do so, represented that it would use the proceeds available to it in the following way:**

**(A) $50,000 on tooling, being certain plant and equipment in its tooling-up process, required for the assembly of its fully functioning prototype;**

**(B) $300,000 on "research and development", a term expressly defined as comprising general administrative expenses, components, raw materials, tooling (other than capital equipment), insurances and promotional costs; and**

**(C) $100,000 on salaries and wages**

**("the Expenditure Representation");**

**(c) in breach of section 12DB of the ASIC Act, has in trade or commerce, in connection with the supply or possible supply of financial services:**

**(i) falsely represented that services are of a particular quality, namely, an investment in proven technology; and**

**(ii) represented that the services had a performance characteristic or benefits they did not have, namely, an investment in proven technology,**

**in that the First Respondent on the website, represented that the engine worked when such an engine could not work**

**3. It is declared that the Second Respondent, in breach of section 12DA of the ASIC Act, in trade or commerce, has engaged in conduct in relation to financial services that was misleading or deceptive, or likely to mislead or deceive in that the Second Respondent created and provided to prospective investors the Business Plan which, when there were no reasonable grounds to do so, made the Expenditure Representation.**

**Injunctions**

**4. The First Respondent is permanently restrained, whether by itself, its servants, agents and employees or otherwise, from:**

**(a) making offers or distributing application forms for the offer of securities that require disclosure to investors under Part 6D.2 of the Act without lodging a disclosure document for the offer with ASIC and causing the offer or application form to be included in or accompanied by the disclosure document as required by section 727 of the Act;**

**(b) engaging in conduct, in relation to a financial product or a financial service, that is misleading or deceptive or is likely to mislead or deceive in breach of section 1041H of the Act by representing on an internet website, that the engine works.**

**(c) in trade or commerce, engaging in conduct in relation to financial services that is misleading or deceptive or is likely to mislead or deceive in breach of section 12DA of the ASIC Act by representing on an internet website that the engine works or by representing, by distributing to potential investors a business plan or other document, when there are no reasonable**

**grounds to do so, that the first respondent will use moneys available to it in a specified way; and**

**(d) in trade or commerce, in connection with the supply or possible supply of financial services:**

**(i) falsely representing that services are of a particular quality, namely an investment in proven technology; or**

**(ii) representing that the services had a performance characteristic or benefits they did not have, namely an investment in proven technology, in breach pf section 12DB of the ASIC Act, in either case, by representing that the engine works.**

**5. The Second Respondent is permanently restrained, whether by himself, his servants, agents and employees or otherwise, from:**

**(a) distributing application forms for the offer of securities that require disclosure to investors under Part 6D.2 of the Act without lodging a disclosure document for the offer with ASIC and causing the offer or application form to be included in or accompanied by the disclosure document as required by section 727 of the Act; and**

**(b) in trade or commerce, engaging in conduct in relation to financial services that is misleading or deceptive or is likely to mislead or deceive in breach of section 12DA of the ASIC Act by representing, when there are no reasonable grounds to do so, that the first respondent will use moneys available to it in a specified way.**

**Costs**

**6. The first and second respondents are to pay the applicant's costs of and incidental to this application.**

**Discharge of other orders**

**7. The orders made by Byrne SJA on 4 May 2007 with respect to the third and fourth respondents are discharged.**

CATCHWORDS: COSTS – Where the successful applicant was not successful on all points – whether costs orders should made with respect

to particular issues which were won or lost by each party - whether the unsuccessful respondents should pay the applicant's costs – whether the successful applicant should pay any of the unsuccessful respondents' costs.

*ASIC v P Dawson Nominees Pty Ltd* [2008] FCAFC 123
*Colgate Palmolive Co v Cussons Pty Ltd* (1993) 46 FCR 225
*Interchase Corporation Limited v ACN 010 087 573 Pty Ltd* [2001] QCA 191
*Waters v PC Henderson (Aust) Pty Ltd* [1994] NSWCA 338

s 12DA *Australian Securities and Investments Act 2001* (Cth)
s 1041H, Part 6D.2 *Corporations Act 2001* (Cth)

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| COUNSEL: | Mr S J Keim SC with Ms E Longbottom for the applicant<br>Mr J B Rolls for the first and second respondents<br>Mr A J H Morris QC with Mr L Jurth for the third and fourth respondents |
| SOLICITORS: | Applicant on own behalf<br>Garland Waddington Solicitors for the first and second respondents<br>DLA Phillips Fox for the third and fourth respondents |

[1] In this matter two further issues need to be resolved:

(a) What orders should be made consistent with the findings published on 24 March 2009; and

(b) What costs orders should be made.

**The orders**

[2] ASIC on the one hand and CME and Mr Nugent on the other disagree about the appropriate terms of an order which would reflect the findings I made in my judgment of 24 March 2009.

[3] ASIC seeks declarations with respect to "the invention" and "the prototype". They are concepts which originated in ASIC's pleadings and were used by them as a means of defining the "scientific" basis for the invention. The findings I made, though, were with respect to the "engine" which was referred to on the website. I have, in general, adopted the draft minutes of order supplied by ASIC but, in order to more accurately reflect my findings I have confined the relief to the "engine" as defined in the order.

**Costs**

*A. With respect to CME and Mr Nugent*

[4] ASIC seeks an order against these parties for its costs, including reserved costs.

[5] CME and Mr Nugent contend that ASIC should pay their costs or, alternatively, there should be no order as to costs.

[6] So far as these respondents were concerned, ASIC was substantially successful. It did not succeed on its application to wind up CME, nor did it establish that the patent representation was made, but it did achieve substantial declaratory and injunctive relief.

[7] I was referred to the transcript of earlier proceedings in this matter before Byrne J. In those proceedings, interlocutory injunctions were granted which effectively stopped the conduct of which ASIC complained. His Honour inquired of Mr Keim SC about the worth of pursuing a winding-up in those circumstances. This was a question which any applicant should ask itself. I think that the continuation of these proceedings was justified for at least two reasons:

(a) CME and Nugent were subject to interlocutory injunctions only. They made no offer of an undertaking to discontinue the conduct I have found to be in breach of the various statutes.

(b) In this type of case, ASIC is not a private litigant. It has the function, among other things, of monitoring and promoting market integrity and consumer protection in the Australian financial system.[1] As was observed by the Full Court of the Federal Court of Australia in *ASIC v P Dawson Nominees Pty Ltd*:[2]

> "[49] ASIC's regulatory role is vital to the proper functioning of the Australian financial and investment system, on which the prosperity of the Australian community is dependent."

In the absence of any indication that CME and Nugent would cease their offending behaviour, it was appropriate for ASIC to continue to seek final relief.

[8] This is not a case in which it would be appropriate to attempt to dissect the claims made by ASIC and to make an order for costs with respect to particular issues which it won or lost. I agree with the statement of Mahoney JA in *Waters v PC Henderson (Aust) Pty Ltd*,[3] where he said:

> "… Unless a particular issue or group of issues is clearly dominant or separable, it will ordinarily be appropriate to award the costs of the proceedings to the successful party without attempting to differentiate between those particular issues on which it was successful and those on which it failed."

[9] ASIC was substantially successful against CME and Mr Nugent. CME and Mr Nugent should bear the costs of their unsuccessful opposition.

*B. With respect to Mr McClelland and Mr Foster*

[10] These gentlemen seek their costs on an indemnity basis against ASIC. ASIC had the unique privilege of having examined these two respondents prior to the commencement of this action. They had no choice but to comply and to answer what was asked of them. This gives to any party an obvious advantage of considerable size.

[11] These respondents point out, quite properly, that a large part of their case was proved by the cross-examination of a witness called by ASIC, namely Mr Nugent. That came about because the respondents, in general, required ASIC to prove its case strictly and,

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1 s 12A *ASIC Act*

2 [2008] FCAFC 123

3 [1994] NSWCA 338

in order to prove some matters, ASIC apparently felt compelled to call Mr Nugent. It was not revealed at trial why these matters could not have been established through the administration of interrogatories for which, I have no doubt, leave would have been granted.

[12] It was also contended for these respondents that there were allegations made against them which should not ever have been made and that those allegations caused significant prolongation of the proceedings and the trial. It was also contended that ASIC put in issue matters which, given ASIC's role as a "model litigant", should not have been disputed. These matters were ultimately proved and formed, in part, the basis upon which no orders were made against these respondents. It was also said that an inference could be drawn that these proceedings were "commenced or continued for some ulterior motive, or because of some wilful disregard to the known facts with a clearly established law".[4]

[13] I do not think that that inference is open to be drawn. I did find that there had been breaches of the legislation, but because of the short period of time for which they had been directors and their low level involvement in CME's activities that it was inappropriate to make orders against them.

[14] Taking that into account, though, it is necessary to consider other matters which tell against these respondents. The conduct of these gentlemen prior to trial in requiring strict proof of matters which should not have, in modern litigation, been pursued was a sign of the manner in which they conducted their response to the claims by ASIC. Prior to receiving legal representation, these respondents filed substantial affidavits which were clearly objectionable but were relied upon (even after legal representation was obtained) until ASIC was put to the cost of objecting to them.

[15] In the circumstances of this case, I think that an appropriate order, which recognises the fact that these respondents were found to have breached legislation but for other reasons no orders were made, can be accommodated by making no order as to costs. I am fortified in that view by the analysis of the provisions of r 689 of the *UCPR* by McPherson JA in *Interchase Corporation Limited v ACN 010 087 573 Pty Ltd.*[5] From [77] to [85] his Honour considered the meaning of the word "event", and referred to the fact that, in that case, the particular defendant had lost on the substantial matters but succeeded in having no order made against him in a manner somewhat similar to the outcome of the instant case. As McPherson JA said:

> "It was not the specific result that in this case constituted the 'event' in the proceedings. To regard it as the 'event' would, as Lord Finlay recognised in the case referred to caused such injustice as to call for the exercise of the power conferred by rule 689(1) of making 'another order'…"[6]

[16] That approach is the one which commends itself to me in the circumstances of this case and I make no order as to costs so far as the third and fourth respondents are concerned.

**Orders**

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4 *Colgate Palmolive Co v Cussons Pty Ltd* (1993) 46 FCR 225

5 [2001] QCA 191

6 At [85]

[17] I make the following orders:

**Introduction**

1. In this Order:

   (a) the "Business Plan" means a document published by the First Respondent, Cycclone Magnetic Engines Inc. ("CME") entitled "Business Plan";
   (b) The “engine” means the Cycclone Magnetic Engine as described on the website, being an engine which purportedly operates through the use of permanent magnets to supply mechanical power on demand without the need for external fuel input;
   (c) the "Website" means a website conducted by CME.

**Declarations**

2. It is declared that the First Respondent:

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   (b) in breach of section 12DA of the *Australian Securities and Investments Act 2001* (Cth) ("the ASIC Act"), has in trade or commerce, engaged in conduct in relation to financial services that was misleading or deceptive, or likely to mislead or deceive, in that the First Respondent:
      (i) on the Website, represented that the engine worked when such an engine could not work;
      (ii) in the Business Plan, when there were no reasonable grounds to do so, represented that it would use the proceeds available to it in the following way:
         (A) $50,000 on tooling, being certain plant and equipment in its tooling-up process, required for the assembly of its fully functioning prototype;
         (B) $300,000 on "research and development", a term expressly defined as comprising general administrative expenses, components, raw materials, tooling (other than capital equipment), insurances and promotional costs; and
         (C) $100,000 on salaries and wages
         (“the Expenditure Representation");
   (c) in breach of section 12DB of the ASIC Act, has in trade or commerce, in connection with the supply or possible supply of financial services:
      (i) falsely represented that services are of a particular quality, namely, an investment in proven technology; and
      (ii) represented that the services had a performance characteristic or benefits they did not have, namely, an investment in proven technology,

   in that the First Respondent on the website, represented that the engine worked when such an engine could not work

3. It is declared that the Second Respondent, in breach of section 12DA of the ASIC Act, in trade or commerce, has engaged in conduct in relation to financial services that was misleading or deceptive, or likely to mislead or deceive in that the Second Respondent created and provided to prospective investors the Business Plan which, when there were no reasonable grounds to do so, made the Expenditure Representation.

**Injunctions**

4. The First Respondent is permanently restrained, whether by itself, its servants, agents and employees or otherwise, from:
   (a) making offers or distributing application forms for the offer of securities that require disclosure to investors under Part 6D.2 of the Act without lodging a disclosure document for the offer with ASIC and causing the offer or application form to be included in or accompanied by the disclosure document as required by section 727 of the Act;
   (b) engaging in conduct, in relation to a financial product or a financial service, that is misleading or deceptive or is likely to mislead or deceive in breach of section 1041H of the Act by representing on an internet website, that the engine works.
   (c) in trade or commerce, engaging in conduct in relation to financial services that is misleading or deceptive or is likely to mislead or deceive in breach of section 12DA of the ASIC Act by representing on an internet website that the engine works or by representing, by distributing to potential investors a business plan or other document, when there are no reasonable grounds to do so, that the first respondent will use moneys available to it in a specified way; and
   (d) in trade or commerce, in connection with the supply or possible supply of financial services:
      (i) falsely representing that services are of a particular quality, namely an investment in proven technology; or
      (ii) representing that the services had a performance characteristic or benefits they did not have, namely an investment in proven technology, in breach pf section 12DB of the ASIC Act, in either case, by representing that the engine works.

5. The Second Respondent is permanently restrained, whether by himself, his servants, agents and employees or otherwise, from:
   (a) distributing application forms for the offer of securities that require disclosure to investors under Part 6D.2 of the Act without lodging a disclosure document for the offer with ASIC and causing the offer or application form to be included in or accompanied by the disclosure document as required by section 727 of the Act; and
   (b) in trade or commerce, engaging in conduct in relation to financial services that is misleading or deceptive or is likely to mislead or deceive in breach of section 12DA of the ASIC Act by representing, when there are no reasonable grounds to do so, that the first respondent will use moneys available to it in a specified way.

**Costs**

6. The first and second respondents are to pay the applicant's costs of and incidental to this application.

**Discharge of other orders**

7. The orders made by Byrne SJA on 4 May 2007 with respect to the third and fourth respondents are discharged.