

Lecture 9 and 10

Directors' Duties

Sources of Directors' Duties

- General law – s 9
 - Fiduciary duties – Principles and rules of common law and equity
- Statute
 - Restated fiduciary duties
 - Additional duties and obligations
 - s 185 – statutory duties additional to general law

Who Owes Duties?

- General law duties
 - Directors
- Statutory Duties
 - ss 180 and 181 – Directors and officers
 - ss 182 and 183 – Directors/officers/employees
 - s 588G – Directors
 - s 9 – extended definitions of Alternate/de facto/shadow director

1. Duties of loyalty and good faith

- Act in good faith in best interests of company
 - Directors must act “bona fide” in best interests of company
 - *Greenhalgh v Arderne Cinemas*
 - Directors and officers must exercise powers/discharge duties in good faith in best interest of company
 - s 181(1)(a)

2. Exercise powers for proper purpose

- Directors must exercise powers for a proper purpose
 - *Permanent Building Society v Wheeler*
- Directors and officers must exercise powers/discharge duties for a proper purpose
 - s 181(1)(b)
- **Matters to consider:**
 - **Objective element** – purpose for which power granted AND
 - **Subjective element** – purpose actually motivating use of power
 - **Mixed purpose** - “But for” test
 - *Whitehouse v Carlton Hotel*

3. Avoid conflicts of interest

- Directors must avoid conflict of interest
 - *Aberdeen Railway v Blaikie*
- Directors, officers and employees must not improperly use position
 - s 182

- Directors, officers and employees must not improperly use information obtained from position (Personal gains or to company's detriment)
 - **s 183**
 - ***ASIC v Vizard***

4. Additional obligations

- Director with material personal interest in matter relating to affairs of the company must notify board
 - **s 191(1)**
 - "material personal interest" has capacity to influence vote – ***McGellin v Mt King Mining***
 - "Affairs of the company" – **s 53**; business, trading, transactions, dealings, property, liabilities, profits, losses
- EXCEPTIONS to disclosure
 - As a member of the company, in common with other members
 - Remuneration as director
 - Contract subject to approval of members
 - Guarantee/security given by director for company debts
 - Contract with related body corporate arising just because of directorship of related body corporate (RBC def **s 50**)
 - Pty Company and other directors aware
 - **s 191(2)**
 - **s 192**
 - Standing notice possible to other directors if wished
- Effect of Disclosure of material personal interest
 - **s 194** - Pty Company
 - May vote on matter
 - Retain benefits
 - Company cannot avoid transaction
 - **s 195** – Public Company
 - Must not be present when matter considered by board and must not vote on matter
 - Exceptions:
 - other directors resolve
 - ASIC approval (**s 196**)
- Fiduciary must not place themselves in position where duty and interest conflict
 - ***Phipps v Boardman***
- Liability can be avoided if full disclosure AND shareholder approval
 - Can be modified by constitution – ***Woolworths v Kelly***
- Related Party Transactions – PUBLIC ONLY
 - **s 208**
 - Prohibition on giving 'financial benefit' to related party
 - **s 229**
 - Financial benefit includes provision of finance/property, buying /leasing asset, supplying/receiving services
 - **s 228**

- Related parties include parent company; directors and spouses, parents or children; related party in last six months likely to be related party in future; entity controlled by related party
- EXCEPTIONS (**s 210-16**)
 - Arm's length terms, no less favourable – **s 210**
 - Reasonable remuneration, Reimbursement – **s 211**
 - <\$5,000 benefit per financial year – **s 213**
 - Court order – **s 216**
 - Otherwise need shareholder approval – **s 208**
 - Person involved in contravention is in breach (no offence by company) – **s 209**
 - **ASIC v Adler**

5. Exercise reasonable care and diligence

- Tort of negligence and equitable duty of care – Director in breach if:
 - Director owes **DUTY** to exercise reasonable care
 - Duty if **BREACHED**
 - Breach **CAUSES** loss/damage to company AND
 - **Loss/damage** not too remote for recovery
 - **s 180(1)**
 - Director/officer must use care and diligence that a reasonable person would use if:
 - Director/officer in corporation's circumstances AND
 - Occupied same office and same responsibilities
 - **ASIC v Vines**
- **Matters to consider**
 - **Objective element** – What would a 'reasonable person' do
 - **Subjective element** – consider company's circumstances, person's office and responsibilities
 - Company Circumstances
 - Type of company
 - Size and nature of enterprise
 - Composition of board
 - Distribution of responsibilities between board and others
 - **Commonwealth Bank v Friedrich**
 - Position and Responsibilities
 - Chair - **ASIC v Rich**
 - CEO - **Daniels v Anderson**
 - Executive Director/non-executive director - **Daniels v Anderson**
 - Directors appointed because of special skill/experience must give company benefit of skills/experience - **Gold Ribbon v Sheers**
 - Directors appointed because of special skill/experience must pay attention to other aspects of business - **Daniels v Anderson**
 - Minimum standard all directors must:
 - **Daniels v Anderson**
 - Become familiar with company's business
 - Keep informed about business operations
 - Be familiar with financial position

- **ASIC v Adler**
 - Have opinion of company's solvency
 - Attend board meetings unless exceptional circumstances
- **s 180(2) - DEFENSE TO ALL**
 - Make judgment in good faith for proper purpose
 - No material personal interest
 - Informed about subject matter to extent believe reasonably appropriate AND
 - Rationally believe judgment in company's best interest
 - THIS IS A DEFENSE to alleged breach of **s 180(1)** and general law duties
- **s 189 - RELIANCE ON INFORMATION/ ADVICE**
 - Director can rely on information/expert advice from:
 - Reliable/competent employee
 - Professional advisor/expert on matter within expertise
 - Another director/officer on matter within their authority
 - Committee of directors on matter within its authority
 - If reliance was in good faith and after making independent assessment (considering director's knowledge and complexity)
- Prevent insolvent trading
 - **s 588G**

PRACTISE QUESTION 1 (QUESTION INCLUDED IN FULL PDF):

Consequences of Breaches of Duty

Members' Rights and Remedies

- Consider again the lengthy question about Tortellini Ltd:
- a. Who could take action against Vivian for breaches of directors' duties? What are the likely consequences?
 - Company suffers harm
 - Chaser could bring **statutory derivative action - s 236**

PART A

- a. Pursuant to s 236, the person applying to bring the action [member etc] is required to bring an application for leave
 - The criteria for bringing an application for leave s 237
 - b. S 237 - application for leave
 - Elements required for s 237 to be satisfied
 - i. Company is unlikely to bring the action
 - 1. Discuss - YES it's unlikely because the directors who are in breach of the directors duties [s 198A s 124]
 - 2. Sued by the company by their breach
 - ii. Act in good faith - loyalty and honesty
 - 0. Have a good cause of action - breaches of directors duties causing harm to the company
 - iii. In best interests of the company
 - 1. Selling of shares wasn't in the best interest of the company
 - a. Objective for issuing shares is to raise equity capital
 - 2. Company is suffering harm, company is suffering loss
 - a. Directors forced to pay
 - b. Statutory derivative action - NOT IN BEST INTEREST IN THE COMPANY IF YOU SUE PEOPLE WITHOUT MONEY
 - i. PRACTICAL MATERS
 - 3. Look at type of business, what effect it a has on this business
 - 4. **S 237(3)** - rebuttable presumption
 - THIS IS NOT IN THE COMPANY'S BEST INTEREST IF YOU BRING ACTION
 - a. Is there a third party involved, directors needed to have made a decision in regards to this third party - BUSINESS JUDGEMENT RULE
 - Acting in good faith and for proper purpose
 - Not having material interest
 - Informing yourself on the issue
 - In the best interest of the company
 - b. If those have been satisfied, your decision to bring action against the company is not in the best interest of the company.
 - c. **OUTCOME: not valid - NO THIRD PARTY**
- b. Need to see if you have sufficient evidence/prove to court you have sufficient action in order to bring the action
- c. 14 days notice of this application

4. The ISSUE OF SHARES

a. Rescission - RESCIND THE ISSUE AND CANCEL THE SHARES

i. Remedy for which the *TRANSVAAL LANDS v NEW BELGIUM* is the case

b. Going after those directors for compensation - for the **loss of money that has just been suffered - s 1317H**

i. STATUTORY COMPENSATION

c. S 206C

Pecuniary penalty order of up to 200,000 because of breach of civil penalty provisions

Statutory compensation order

ASIC - can call statutory derivative order