

## CORPORATIONS LAW EXAM NOTES

All references to legislation in this exam are references to the *Corporations Act 2001* (Cth) unless otherwise stated.

- S 185 and S193 confirms that sections 180-184 and sections 191-192 have effect in addition to and not in derogation of any rule of law relating to the liability of directors or officers.

## DIRECTORS DUTIES

### Director/Officer

- For general law, duties are owed by directors (including de facto and shadow directors – *Corporate Affairs Commission (NSW) v Drysdale*) as well as some senior executives (though the content of the duties at general law may differ between directors and senior executives)
- For statutory duties, they typically are owed by directors AND officers (which is broader than senior executives), though the scope of the duty depends on the specific duty

### Is X a director?

- **S9 of the *Corporations Act*** indicates that a director includes:
  - **A formally appointed director (s9(a)(i)) or an alternate director (s9(a)(ii))**
    - Minimal qualifications required to be formally appointed as a director (S201B):
      - An individual (not a company) who is at least 18 years old (S201B(1))
      - Cannot be bankrupt or under some disqualification order (due to certain criminal offences) (S206N)
    - Directors can be appointed by shareholders, or they can be appointed by the Board to fill in a casual vacancy which is later affirmed by the shareholders (depends on the company's constitution)
    - An alternate director is someone who steps in as director if the actual director cannot do their job (e.g. they are sick for a period of time)
  - **A de facto director (s9(b)(i))**
    - **A person is a de facto director if they act in the position of a director, and carry out their functions for all intents and purposes, despite not being formally appointed**
    - **It is necessary that the alleged director is exercising top level management functions** (Machwick J, *Austin*)
    - Non-exhaustive list of criteria for a de facto director (Machwick J, *Austin*):
      - **Size of the company**
        - An individual employee might be a de facto director in a small company but not a large company despite performing the same actions (they have more influence in a smaller company than a larger one)
      - **How the alleged 'director' is perceived by outsiders who deal with the company**
        - If the individual holds himself out as a director of the company, or others commonly believe him to be a director, then he may be considered a de facto director.
    - *Brick v Pipe*
      - The board allowed G, who controlled the parent company, to act as if he had been appointed managing director of B&P, which was in a group of wholly owned subsidiaries of the parent company
    - *Austin*
      - **Despite Austin resigning as a director**, he was found to be a de facto director because he continued to perform responsibilities that are typically expected of directors (including negotiating agreements with the Commissioner of Taxation and company creditors to extend terms of payment and other management roles)
  - **A shadow director (s9(b)(ii))**
    - A person is a shadow director **if the directors of the company or body are accustomed to act in accordance with the person's instructions or wishes**, despite not being formally appointed
    - (Wright J, *Buzzle Operations*) Factors to determine whether a person is a shadow director include:
      - There must be a **causal connection** between the instructions or wish of the alleged shadow director, and the directors acting on that instruction or wish
        - If the director would have acted irrespective of the alleged shadow director, that would indicate to the contrary
      - There must be evidence of **habitual compliance of the directors as a collective** (at least a majority of the Board) being accustomed to acting in accordance with the instructions or wishes of the alleged shadow director
    - It **excludes a person who merely provides advice** to the directors in the proper performance of their professional functions, or in the context of a business relationship with the directors or company or body
      - Particularly if the Board has specifically engaged/employed them to give advice on a particular matter
    - **It is possible for a company to be a shadow director** of another company (e.g. a holding company in the context of corporate groups) but only in limited circumstances (*Buzzle Operations*)

- Irrespective of S201(b) which states that only individual humans can be validly appointed directors
  - A **creditor** of a company could potentially be a shadow director (Buzzle Operations)
    - However, a creditor is not a shadow director merely because the directors feel obliged to comply with the creditor's wishes in their commercial dealings with the company (Buzzle Operations)
- A person can be found to be a director **regardless of the name given to their position** - *Mistmorn Pty Ltd (in Liq) v Yasseen* (1996) 21 ACSR 173

### Is X an officer?

- **S9** of the *Corporations Act* states that an officer includes:
  - A director **or secretary** of the corporation (S9(a))
    - Includes a de facto or shadow director (S9(b)(iii)) – *an officer is a person in accordance with whose instructions or wishes the directors of the corporation are accustomed to act*
  - **A person who makes, or participates in making, decisions that affect the whole, or a substantial part, of the business of the corporation (S9(b)(i))**
    - Requires evidence of the person's **holistic conduct** in the company on a day-to-day basis, and not confined to the role they played in relation to the alleged contravention – *Shafron v ASIC*
    - **Even if the person does not have the final say** in decision making, they can still be an officer through an involvement in the decision-making process (a question of fact and degree) – *Shafron v ASIC*
  - **A person who has the capacity to affect significantly the corporation's financial standing (S9(b)(ii))**
    - Generally would include a **CFO** – *Morley v ASIC*
  - A receiver, external administrator or a liquidator (S9(c)-(f))
- In a problem question, these will typically include a CEO, CFO, Company Secretary, General Counsel or other management level employee

### Cases

<u>Case</u>	<u>Facts</u>	<u>Judgement</u>
Shafron v ASIC	<ul style="list-style-type: none"> <li>• Peter Shafron <b>was both the Company Secretary and General Counsel</b> of James Hardie               <ul style="list-style-type: none"> <li>○ The General Counsel is the internal lawyer for the company who provides legal advice</li> </ul> </li> <li>• Shafron was alleged to have breached his duty for <b>failing to properly advise</b> the Board on the defective press release regarding the insufficient funds for compensating asbestos victims and the Deed of Indemnity's actuarial forecast, which would ultimately pertain to James Hardies' inadequate compensation funding</li> <li>• ARGUMENT 1:               <ul style="list-style-type: none"> <li>○ Shafron did not deny that 'company secretary' was caught under the definition of 'officer', but he argued that <b>the alleged breach was undertaken in his role as the General Counsel</b>, not the Company Secretary, which would not fall under the definition of 'officer'</li> </ul> </li> <li>• ARGUMENT 2:               <ul style="list-style-type: none"> <li>○ In regard to S9(b)(i), he argued that he <b>only provided advice to the Board but did not have a role in actually making the decision, as the Board ultimately decides</b> whether the separation proposal should be adopted, and what information to be given to the ASX</li> <li>○ Thus he argued that he was not a person who 'participated' in making decisions that affected the whole or a substantial part of the company</li> </ul> </li> </ul>	<p><b><u>OFFICER</u></b></p> <ul style="list-style-type: none"> <li>• ARGUMENT 1               <ul style="list-style-type: none"> <li>○ The fact that Shafron was the Company Secretary was sufficient; there is <b>no need to enquire whether the breach was in the role of the Company Secretary or another part of his combined role</b></li> <li>○ Note however, that nothing in the HC's reasoning would prevent a General Counsel from being held to be an officer</li> </ul> </li> <li>• ARGUMENT 2               <ul style="list-style-type: none"> <li>○ The idea of participation directs intention to the role that a person has in relation to the ultimate act of making a decision, <b>even if that final act is undertaken by some other person</b></li> <li>○ <b>The decision in which the person participates has to be a decision significant enough</b> to fall within the statutory description of affecting the whole or a substantial part of the business of the corporation</li> <li>○ A question of fact and degree</li> </ul> </li> </ul>
ASIC v Citigroup Global Markets Australia Pty Ltd [2007] FCA 963	<ul style="list-style-type: none"> <li>• A <b>share trader</b> with a daily limit of 10 million dollars</li> </ul>	<p><b><u>NOT AN OFFICER</u></b></p> <ul style="list-style-type: none"> <li>• Federal Court Judge Jacobson J held that S9(b)(i) and (ii) described persons who were <b>involved in the management of the corporation</b>, which did not include a trader.</li> </ul>

## Duty of Care

- The statutory and general law duties of care are identical in their content and can be addressed together (*ASIC v Adler*)/Since the general law case law and statutory test overlap significantly, the court should apply the general law (*ASIC v Adler*)
- General law: **Directors and senior executives** are under an obligation to act with a reasonable degree of care, skill and diligence in the running of their company or companies.
- Statute: A **director or officer** of a corporation is required to act with the degree of care and diligence that a reasonable person would exercise in the position of the director in the corporation's circumstances and holding the same office and responsibilities (s 180(1)).

## Is X a director/officer?

### Was there a breach of the duty of care?

- Irrespective of the particular circumstances of the company, or the directors' particular position or responsibilities within the company, **ALL directors must at a MINIMUM take reasonable steps to place themselves in a position to guide and monitor the management of the company. (Daniels v Anderson)**
- The baseline standard of care required is for directors to ensure they have **knowledge of the business, to keep informed about its activities, to remain familiar with the financial accounts of the company, to make regular attendance at board meetings (Daniels v Anderson) and to have a reasonably formed view of the company's financial capacity (ASIC v Rich (2009)).**
- Although ALL directors must pass this core irreducible standard, **the standard of care can be higher as it is judged according to a reasonable director of a company**
  - **In the same circumstances (ASIC v Rich)**
    - Type of company, size & nature of business, provisions of constitution, composition of board, distribution of work between board & officers, status of company (listed/unlisted)
    - The court may **also balance the foreseeable or any possible risks of harm from the defendant directors' actions against any potential benefits to be accrued by the company**, to determine if the conduct of the director was reasonable in the circumstances (*Vrisakis v ASIC*)
      - In *ASIC v Cassimatis* (No 8) (2016) 336 ALR 209 – 'foreseeable risk of harm' is not confined to financial harm, but can include harms to all interests of the company, including reputation
    - Whilst pure personal circumstances (e.g. levels of education, experience) are irrelevant to determining a directors' standard of care, **if a director holds themselves out at appointment as having a particular skill**, they may be held to a higher standard of care in light of that skill
  - **In the same position and**
    - A higher standard of care is required of certain directors/officers, depending on their role and appointment in the company.
      - E.g. If the director is the CEO, their standard of care might be higher than non-executive directors as they are involved in the day-to-day running of the company
      - *ASIC v Vines*: defendant was director of GIO Insurance and chief financial officer of GIO group. Court stated that position of chief financial officer is recognised position in large corporations, such that there are identifiable specialised skills attaching to that office. Court held that evidence of what reasonably competent chief financial officer would have done is relevant to the determination of whether the defendant breached his statutory duty of care and diligence
  - **Having the same responsibilities**
- In terms of **financial literacy (ASIC v Healey (Middleton J)), directors must:**
  - read, understand and focus upon the contents of any reports they are required by law to approve or adopt (including financial statements)
  - consider whether the statements in any reports are consistent with the director's knowledge of the company's financial position
  - make further enquiries if necessary
  - have sufficient financial skills to perform these tasks and to be able to understand basic accounting conventions, and proper due diligence in reading the financial statements (though they are not required to audit the company's books)
  - **not rely on others advice** so extremely that would lead to a mistake in something crucial such as the disclosure of financial statements