HYPO NOTES - CORP

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Topic 4: Corporate Liability

Contractual Liability

<table>
<tr><td colspan="2">A company may enter into a contract directly or indirectly.</td></tr>
<tr><td>Direct Contractual Liability</td><td>Directly through board or general meeting authorization (s 198A) and proper execution (s 127)
Authorisation
- The board may delegate this authority to the CEO or others essentially making their decisions a decision of the board and the company.
o The authorization must occur in a specific meeting for a particular transaction and not as a blanket approval for all contracts (Northside)
Execution
The Contract must be signed by (a) two directors, or (b) one director and one company secretary, or (c) sole director for proprietary companies. The constitution may also impose additional execution requirements.</td></tr>
<tr><td>Indirect Contractual Liability</td><td>The company can also enter into the contract Indirectly via an agency relationship, where authority can be actual (express or implied) or apparent (s124).

<table><tr><td>1.2(a) Actual Authority</td><td>Actual authority can involve an individual with either express authority (directly granted) or implied authority (inferred from role or conduct) (s126).

1.2(a)(i) Express
Explicit authority given to an individual via the company’s constitution, an employment contract, a power of attorney, or a board resolution (Freeman; Hely).</td></tr></table></td></tr>
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<tr><td></td><td>purpose, [X] would still have exercised the power (Howard Smith; Whitehouse). Note that if [X] genuinely believed the action was in the company’s best interest, it may not be considered a breach (Darvall).</td></tr>
<tr><td>3. Consequences of Breach</td><td>

- **Civil Penalties (s 1317E):** Breaching s 181(1)(b) is a civil penalty provision, allowing ASIC or the company to seek civil sanctions, including fines and disqualification orders.
- **Involvement Liability (s 181(2)):** Liability extends to any party involved in the contravention.
- **Criminal Penalties:** If [X] acted dishonestly or recklessly, criminal liability may apply (s 184(1)).
- **General Law Remedies:** Additional remedies include injunctions, declarations, compensation, rescission, account of profits, and constructive trusts.

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Topic 7 - Duty of Care

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<tr><td colspan="2">Under s 180(1) of the Corporations Act, directors and officers are required to exercise their powers and perform their duties with the care and diligence that a reasonable person would display in similar circumstances, holding the same position and responsibilities. This duty is the same under general law and statute. Here since we are advising [ASIC/X], the advice is focused on [Statute/General Law]. (X can bring an action under statute and General Law)

To determine whether [X] has breached this duty, it is necessary to identify if [X] owes this duty, examine whether their actions meet the required standard, consider any available defenses and assess the consequences of any breach.</td></tr>
<tr><td>1. Who Owes the Duty?</td><td>

This duty applies to both directors (appointed, de facto and shadow directors) and officers.

A duty of care and diligence under s 180(1) is owed by:

- **Directors** (appointed, de facto, or shadow directors) who have formal or informal influence over corporate affairs.
- **Officers** who make key business decisions or impact the company’s financial standing.

In this case, if [X] holds a directorship or a high-level officer position (or meets criteria of a de facto or shadow director), they owe a duty to act with care and diligence.

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<tr><td>2. Determining a Breach of Duty</td><td>

Objective minimum standard
Minimum Standard of Care
Directors and officers are held to an objective standard requiring them to position themselves to understand, guide, and oversee management (Daniels v Anderson). They must meet a **minimum standard** by:

- **Understanding the Business:** Directors need sufficient knowledge of the company’s operations and industry context.
- **Staying Informed and Monitoring:** Regular review of activities and financials is required to stay informed of the company’s performance (Healey).
- **Financial Oversight:** Directors must understand financial statements, evaluate financial health, and investigate issues in reports they approve.
- **Meeting Requirements:** Directors should attend board meetings and meet as often as needed to properly monitor and guide the company.
- **Inquiry Duty:** Directors are expected to make reasonable inquiries into the company’s finances, address concerns, and act with financial literacy.

Factors Affecting the Duty of Care - *Here mention each director then the factor that’s relevant to them.*

The duty of care can be adjusted up due to specific roles and circumstances of individual directors (Maxwell; Rich):

- **Type and Size of Company:** In large corporations, directors may set goals, appoint CEOs, and oversee high-level strategies, whereas in smaller firms, more hands-on involvement is expected (AWA v Daniels).
- **Position and Responsibilities:** The nature of [X]’s role (e.g., CEO, CFO, chair, NED) influences the scope and expectation of duty:
  - **CEO/Managing Director:** Expected to actively inform the board on risks and ensure other directors understand transaction risks.
  - **CFO:** Responsible for generating and verifying financial data and ensuring accuracy.
  - **Non-Executive Directors (NEDs):** Though less involved daily, NEDs must still actively monitor performance and cannot fully rely on management (AWA; Healey).
  - **Chair:** Responsible for managing board meetings and company policy. In public companies, the chair has additional oversight responsibilities (AWA).
- **Experience and Skills:** The director’s expertise, qualifications, and experience are considered (Rich)

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	• **Specific Circumstances of the Company:** Unique risks and business operations, as well as industry norms, influence care expectations. **Special Considerations for Positions** Directors are accountable for understanding their specific responsibilities. Non-executive directors may rely on management but must scrutinize information independently**. In financial oversight**, directors cannot merely rely on management's assurance but **must take responsibility for understanding significant issues in financial statements and information received (Healey).** - Failure to meet these standards could constitute a breach, even if the director holds a non-executive role (Daniels). **Shifting Objective Test** When assessing whether the duty has been breached the Courts balance **foreseeable risk** against **potential benefits** of [X]'s actions (Cassimatis): • **Balancing Risk and Benefit:** Risk alone does not constitute breach if the action benefits the company; directors must weigh risks against rewards reasonably. • **Factors in Risk Assessment:** Courts assess the harm, costs, and risks against the nature of expected benefits. They consider the importance of lawful conduct, reputation, and all interests of the corporation. • **No Actual Loss Required:** Proof of loss is not essential for finding a breach; risk of harm alone may suffice.
3. Defenses/Protections Against Breach	**3.1 Delegation** Directors may avoid liability for breach of duty by properly delegating tasks or relying on the advice of others or the business judgment rule. **1. Delegation of Powers** Directors can delegate tasks to others under two main sources: • **Company Constitution:** The constitution may outline specific delegation rules. • **Statute:** Under s 198D(1), directors can delegate to committees, other directors, employees, or any person unless the constitution restricts this. Directors may also confer powers on a Managing Director (s 198C). For [X] to rely on delegation as a defense, they must demonstrate that: • **The Task Was Suitable for Delegation**: Delegation must be appropriate, especially for high-stakes transactions where greater scrutiny is expected. • **The Delegate Was Trustworthy and Competent**: [X] must have genuinely believed in the delegate's competence (Adler). • **[X] Exercised Oversight**: While delegated, [X] must still monitor or direct the delegate's actions, ensuring tasks align with company standards (s 198D(2)). Considerations for determining "reasonable delegation" include: • **Nature of the Task**: Higher scrutiny for complex or high-value tasks. • **Alertness to Issues**: [X] should have been vigilant to any risks or red flags regarding the delegate's actions, particularly in significant matters. • **Director-Delegate Relationship**: Was there a strong foundation of trust in the delegate's ability? **If [X] fails to meet these criteria** and has ignored issues or failed to supervise the delegate, the delegation defense may not apply. **3.2 Reliance** Directors can also avoid liability by reasonably relying on advice if they believe it is appropriate to do so. **s 189 provides a rebuttable presumption** that reliance is reasonable when advice is from: • **Employees** [X] believes to be reliable and competent in the relevant area, • **Professional Advisers or Experts** with suitable expertise, • **Other Directors or Officers** acting within their authority, • **Committees of Directors** with relevant authority. To rely on this defense, [X] must show that they: • **Relied in Good Faith**: [X] genuinely believed the advice was correct and acted without personal bias. • **Made an Independent Assessment**: Even with advice, [X] should have used their knowledge of the company to judge the reliability of the advice. **Reasonableness in Director Reliance** A director's reliance on advice or information is unreasonable if they are aware of clear and significant issues that any prudent person would recognize as unreliable (Daniels). Directors cannot rely solely on management's advice for important matters that fall within the board's

	specific responsibilities, particularly in reviewing financial accounts and statements, which they must examine personally and cannot delegate or avoid (Healey). **Business Judgement rule** If [X] made a **business judgment**—a decision about the company's business activities—they may be protected from liability under the **business judgment rule**, provided they meet all the limbs in s180(2): 1. **Good Faith and Proper Purpose (s 180(2)(a))**: [X] must have made the decision honestly and with the intent of benefiting the company, rather than serving any personal interest. This ensures the decision was genuinely for the company's benefit. 2. **No Material Personal Interest (s 180(2)(b))**: [X] must not have any significant personal interest in the decision. This means the judgment should not benefit [X] personally beyond their general desire to see the company succeed. A material personal interest would disqualify them from relying on this rule. 3. **Informed Judgment (s 180(2)(c))**: [X] must have taken reasonable steps to become informed about the decision before making it. Reasonableness here depends on factors like: o The importance of the decision, o Costs and time involved in gathering information, o [X]'s confidence in others investigating the matter, and o The information available at the time. o [X] does not need to know everything but must have enough information to make an informed choice. 4. **Rational Belief in the Company's Best Interests (s 180(2)(d))**: [X] must genuinely believe the decision was in the company's best interests. This belief must be rational, meaning any reasonable director in their position could see it as a beneficial decision, even if the outcome wasn't guaranteed. It only needs a reasonable basis, not a certainty of success. If all these conditions are met, [X] may be protected under the business judgment rule, shielding them from liability for a breach of the duty of care and diligence under s 180(1).
Consequence of Breach	Therefore since none of the defences apply there is a contravention of s180(1). • **Civil Penalty (s 1317E):** Breaching s 180(1) is a civil penalty provision, with possible outcomes such as fines, compensation orders, or disqualification. • **No Criminal Penalty:** Breach of this duty does not lead to criminal sanctions. • **General Law Remedies:** Remedies may include injunctions, declarations, rescission, compensation, and, in serious cases, constructive trusts or account of profits.

Topic 8 – Insolvent Trading

Who Owes the Duty?	The duty to prevent insolvent trading under s 588G applies to directors, including appointed, de facto, and shadow directors. For the duty to apply, three elements must be established under s 588G(1).
2. Setting up the Duty (s 588G(1))	**2. Setting up the Duty (s 588G(1))** For s 588G to apply, the following elements must be satisfied: 1. **Debt**: The company must have incurred a debt. o A debt arises when a company enters a contract that creates an unavoidable financial obligation, including conditional obligations (*Southern Cross Interior*). Additional forms of debts include: ▪ **Dividends**: The obligation is incurred when declared or paid. ▪ **Share Capital Reduction**: The debt arises when the reduction takes effect. ▪ **Buy-Backs**: The debt is incurred upon entering the buy-back agreement. ▪ **Uncommercial Transactions**: A debt is incurred when the transaction is entered into. o **Involuntary obligations** like tax do not qualify as debts because they are not voluntarily incurred (Hawkins). 2. **Insolvency**: The company must have been insolvent at the time the debt was incurred or became insolvent due to incurring the debt. o Insolvency is defined as the inability to pay debts as they fall due (s 95A). o **Indicators of insolvency** (Plymin) include trading losses, unpaid taxes, creditor demands, and an inability to secure financing or equity capital. 3. **Reasonable Grounds to Suspect Insolvency**: There must be objective grounds to suspect that the company was insolvent at the time of incurring the debt. o Directors are required to meet a standard of financial competence, actively monitor the company's financial status, and inquire where necessary (Friedrich). o Courts may cross-reference insolvency indicators (Plymin) to determine if reasonable grounds existed.