
4. Duty of Care, Skill and Diligence

Section 180(1) requires a director or officer to exercise their powers and discharge their duties with the degree of care and diligence that a reasonable person would exercise if they were a director or officer of a corporation in the company's circumstances, held the same responsibilities within the company, and had the same responsibilities as the director. The section adopts a combined objective/subjective standard: the baseline is objective (reasonable person), but this is modified by the specific circumstances of the individual director. The Business Judgment Rule (*s 180(2)*) provides a safe harbour.

RED FLAG: Director who fails to read financial reports, does not attend meetings, or does not make adequate enquiries -- potential s 180(1) breach.

RED FLAG: Large company with experienced board and sophisticated financial reporting -- higher standard will be imposed.

RED FLAG: Director with special expertise (lawyer, accountant, finance professional) -- held to the standard of a person with that expertise.

RED FLAG: Non-executive director who rubber-stamps management proposals without inquiry -- consider s 180(1) (*ASIC v Rich; Healey v ASIC*).

Step 1: Standard of Care -- Objective Baseline with Subjective Modifiers

The standard under s 180(1) is that of the reasonable person in the director's circumstances. The 'circumstances' include: (a) the nature of the company (size, type of business, complexity); (b) the director's role and responsibilities within the company; and (c) the director's own attributes (expertise, knowledge, experience).

In (*AWA Ltd v Daniels (1992)* 7 ACSR 759), Rogers CJ articulated the standard as requiring directors to be familiar with the fundamentals of the business, to keep themselves informed, to monitor senior management, and to make inquiry where circumstances suggest further investigation.

In (*ASIC v Rich (2009)* 75 ACSR 1), Austin J confirmed that the standard is assessed objectively by reference to the director's specific role, and that directors with financial expertise (e.g., a CFO with a finance background) are held to a higher standard.

In (*Healey v ASIC (2011)* 196 FCR 291), the Full Federal Court confirmed that even non-executive directors owe a duty to read financial reports carefully and to raise questions where statements appear incorrect.

Step 2: Business Judgment Rule (s 180(2))

A director or officer who makes a 'business judgment' is taken to meet the requirements of s 180(1) in respect of the judgment if they: (a) make the judgment in good faith for a proper purpose; (b) do not have a material personal interest in the subject matter of the judgment; (c) inform themselves about the subject matter to the extent they reasonably believe appropriate; and (d) rationally believe the judgment is in the best interests of the corporation.

'Business judgment' is defined in s 180(3) as any decision to take or not take action in respect of a matter relevant to the business operations of the corporation. It does not apply to the exercise of delegated administrative functions.

The rule is a safe harbour -- if its conditions are met, no breach. It does not mean courts will not assess the merits of the decision; it means the director cannot be liable if the conditions are met even if the decision later proves wrong.

'Rational belief' (s 180(2)(d)) is a lower threshold than correctness -- an irrational belief (one that no reasonable person could have held) is not protected (*Shafroon v ASIC (2012)* 247 CLR 465).

SCRIPT: Duty of Care -- s 180(1) Analysis

1. Identify the defendant and their role: Was the defendant a director or officer of the company at the relevant time? What were their specific responsibilities? (s 9; s 180(1)).

-> IF executive director/CEO/MD: higher duty -- responsible for day-to-day management, must be fully informed.

-> IF non-executive director: still owes duty -- must read financial reports, attend meetings, make inquiry where appropriate (*Healey v ASIC*).

-> IF director with specialist expertise (CFO, CLO): held to higher standard in that area of expertise.

-> COUNTER-ARGUMENT: Director will argue they had no specific responsibility for the matter in question, or that they reasonably delegated to management and were entitled to rely on management assurances (*ASIC v Rich -- delegation is not blanket absolution*).

WRITE:

[Defendant] was a [executive/non-executive] director of [Company] and was responsible for [specific responsibilities]. In those circumstances the relevant standard under s 180(1) is that of a reasonable person [with [Defendant]'s expertise/background] in [Company]'s circumstances.

2. Identify the conduct alleged to be in breach: What specific act or omission is said to fall below the standard? Failure to read reports, failure to make inquiry, failure to oversee management, entry into an imprudent transaction.

-> IF failure to read financial statements: AWA; Healey -- basic obligation to be informed of financial fundamentals.

-> IF failure to make inquiries when warning signs existed: Rogers CJ in AWA; directors must 'make inquiry' where circumstances call for it.

-> IF affirmative decision (e.g., entering a transaction): consider whether business judgment rule applies.

-> COUNTER-ARGUMENT: Director will argue they read the reports but they were inaccurate due to management fraud or accounting error -- consider whether reasonable reliance on management was appropriate.

WRITE:

[Defendant]'s conduct consisted of [specific act/omission -- e.g., failing to read the consolidated financial reports for [period]], failing to inquire about the large unhedged currency position despite having received a briefing document flagging the exposure]. This [did / did not] fall below the standard expected of a reasonable director in [Company]'s circumstances because [reasoning].

3. Apply the objective standard -- would a reasonable person have acted differently? Assess against the benchmark: a reasonable director in the company's circumstances, holding the same responsibilities, with the same background.

-> IF company was large and well-resourced: higher standard -- director should have systems, oversight, and external advice.

-> IF company was small and informal: standard may be lower, but basic financial literacy still required.

-> IF director's inaction caused quantifiable loss: corroboration of breach -- AWA -- loss does not prove breach but is relevant context.

-> COUNTER-ARGUMENT: Director will argue a reasonable director in the same circumstances would have acted identically, given the information available at the time and the company's structure. Hindsight bias must be excluded.

WRITE:

A reasonable director of [Company] in [Defendant]'s position [would / would not] have [specific conduct] because [reasoning -- e.g., [Company] was a large, listed company with a sophisticated board, and a reasonable person in [Defendant]'s role would have read the quarterly accounts and identified the currency

exposure, particularly given the briefing document provided / or the circumstances did not call for further inquiry because **[Company]**'s prior reports had always been accurate and there were no obvious warning signs].

4. Business Judgment Rule (s 180(2)): applies only if the conduct is a 'business judgment' (s 180(3)) -- not routine administration; director must satisfy all four conditions.

-> s 180(2)(a): Good faith and proper purpose -- subjective; not to derive personal benefit.

-> s 180(2)(b): No material personal interest in the subject matter.

-> s 180(2)(c): Informed to the extent reasonably believed appropriate.

-> s 180(2)(d): Rational belief it was in best interests of corporation -- note 'rational', not 'correct';
Shafron v ASIC.

-> COUNTER-ARGUMENT: ASIC/plaintiff will argue one of the four conditions is not met -- e.g., that the belief was irrational (*Shafron*), or that the director had a material personal interest (executive remuneration linked to performance of the transaction).

WRITE:

The business judgment rule **[applies / does not apply]** because **[reasoning -- e.g., [Defendant]'s decision to [enter the transaction] was a business judgment within s 180(3), made in good faith, without material personal interest, and [Defendant] rationally believed on the information available that it was in the company's best interests, satisfying all four conditions of s 180(2) / or condition [identify which one] is not satisfied because [reasoning], specifically [Defendant]'s belief was irrational within the meaning of Shafron v ASIC because no reasonable director could have held it].**

5. Causation and loss: Even if breach is established, plaintiff must show the breach caused the loss complained of. Counterfactual: what would have happened if the director had acted reasonably?

-> IF director would have acted to prevent the loss: causation established.

-> IF loss would have occurred regardless: no causation.

-> COUNTER-ARGUMENT: Director will argue the company would have suffered the same loss in any event because the external cause (market conditions, fraud by a third party) was the true cause.

WRITE:

[Defendant]'s breach [did / did not] cause [Company]'s loss because [reasoning -- e.g., had [Defendant] made the relevant inquiry, [Defendant] would have identified the [specific risk] and taken steps to [prevent/hedge/terminate] it, avoiding the loss of \$[amount] / or the loss would have occurred regardless because the [external cause -- e.g., counterparty fraud] was outside [Defendant]'s ability to control even with full knowledge].

Key Cases -- Duty of Care

Case	Principles	Watch Out / Application
<p>AWA Ltd v Daniels (1992) 7 ACSR 759 (NSWSC -- Rogers CJ)</p>	<ul style="list-style-type: none"> • Directors must be familiar with the fundamentals of the business in which the company is engaged -- wilful ignorance of the company's core activities is no defence. • Directors are required to keep themselves informed about the activities of the company on a continuing basis -- not merely at the time of their appointment. • Directors must monitor senior management and must not blindly accept management assurances -- where circumstances call for further inquiry, the director must make that inquiry. • Where a director has delegated responsibility to a competent person, the director is still obliged to follow up if warning signs arise that the delegation is not being competently exercised. • The case involved the largest reported commercial loss in Australia at the time -- caused by an unhedged foreign exchange exposure which the board failed to monitor despite being briefed on the risk. • Rogers CJ distinguished the minimum standard (applicable to all directors) from a higher standard applicable to directors with specialist expertise or specific portfolio responsibilities. 	<p>Baseline statement of directors' duty of care under s 180(1) and the general law -- must cite in any duty of care question; the 'keep informed and monitor' principle is central</p>
<p>ASIC v Rich (2009) 75 ACSR 1 (NSWSC -- Austin J)</p>	<ul style="list-style-type: none"> • Confirmed the combined objective/subjective standard: the baseline is a reasonable person, but that baseline is calibrated by the director's specific circumstances, role, and expertise. • A director with financial or accounting expertise is held to the standard of a reasonable person with that expertise in their role -- they cannot claim ignorance of financial matters within their specialty. • De facto directors are included within the scope of the duty of care: the test is whether the person 	<p>Primary modern authority for the content and standard of the duty of care; Austin J's synthesis of the objective/subjective standard is the leading statement</p>

	<p>performed the functions normally performed by a director.</p> <ul style="list-style-type: none"> • Austin J analysed the company's financial position in detail using expert evidence and confirmed that insolvency is to be assessed at specific points in time, not retrospectively across the whole period. • A director's reliance on management reports is only reasonable if the director has no information that should have put them on notice that the reports were unreliable. • The case concerned the collapse of One.Tel; ASIC alleged that the non-executive directors failed to monitor the company's financial position adequately. 	
<p>Healey v ASIC (2011) 196 FCR 291 (Full Federal Court) -- the 'Centro Properties' case</p>	<ul style="list-style-type: none"> • Non-executive directors are required to read and understand the financial statements placed before them -- they cannot simply defer to management or auditors. • The full Federal Court upheld ASIC's case against Centro Properties' non-executive directors who signed off on financial accounts that incorrectly classified short-term debt as long-term. • The error was significant: it materially misrepresented the company's liquidity position to investors. • Directors' duty is not merely to attend meetings but to engage with the substance of what is presented -- a director who signs a document without understanding its contents breaches the duty. • The 'minimum irreducible standard' for all directors includes reading and comprehending financial reports -- this is not delegable. • The defence that the error was made by management and auditors did not excuse the directors from personal liability -- they had independent obligations to verify the reports. 	<p>Non-executive director standard -- even passive directors with limited involvement must read and understand financial reports; rubber-stamping is a breach of s 180(1)</p>
<p>Shafron v ASIC (2012) 247 CLR 465 (HCA)</p>	<ul style="list-style-type: none"> • The business judgment rule in s 180(2)(d) requires a 'rational belief' that the judgment is in the best interests of the corporation. 	<p>Business judgment rule -- 'rational belief' is not the same as any honest belief; the belief must survive an</p>

	<ul style="list-style-type: none"> • A 'rational belief' means more than a subjective, honest belief -- it must be one that is not irrational, i.e., one that a reasonable person could have formed on the available information. • A belief that no reasonable person could have held does not qualify for the business judgment rule safe harbour, even if the director subjectively held that belief honestly. • The case involved James Hardie's former company secretary and general counsel, Shafron, who was found to have failed in his duty in advising the board on the adequacy of the asbestos compensation fund. • The High Court confirmed that 'officer' within s 180(1) includes company secretaries and general counsel who occupy positions of significant influence. • The business judgment rule is a safe harbour with strict conditions -- if condition (d) is not met (rational belief), the protection is unavailable regardless of good faith. 	<p>objective reasonableness assessment; also clarifies 'officer' scope</p>
<p>ASIC v Vines (2005) 55 ACSR 617 (NSWSC)</p>	<ul style="list-style-type: none"> • An officer or director who has a specialist professional background (law, finance, accounting) is held to the standard expected of a reasonable person with that background in their role. • Vines was CFO of HIH Insurance and was found to have breached his duty of care in preparing misleading prospectus disclosures. • The court rejected the argument that the standard should be assessed purely by reference to the general director standard -- the specific expertise of the person raises the bar. • A CFO who signs off on financial statements that are materially incorrect is held to the standard of a reasonable, competent CFO -- not merely a reasonable lay director. • The case illustrates that ss 180-183 duties apply to officers (including CFOs and company secretaries) as well as directors. 	<p>Specialist expertise raises the standard; always apply where defendant has a professional background that is relevant to the alleged breach</p>