

Corporation Law

SAMPLE

Introduction

The regulation and proper operation of any company or corporation is completely dependent on the nature and manner in which the directors and other office bearers of the company perform their functions. This is so, because even though a company has a separate legal entity and it has its independent existence distinct from its members, nevertheless the company operates through its directors and office bearers and as such it is very important that they perform their tasks and duties diligently and honestly being compliant with the provisions of Corporations Law as well as their duties established under the Common Law and General Law as such.

The present discussion concerns a discussion of various duties enshrined upon Directors and other office bearers of the company under General Law as well as the provisions of the Corporations Act, 2001. For the purpose of this discussion, the nature of the post of directors and office bearers of a company in Australia has been discussed in order to gain an insight about the duties that they should be and which they are subject to. It is submitted in this regard that two landmark cases, namely *ASIC v Rich* (2003) 44 ACSR 682¹ and *ASIC v MacDonald (No 11)* (2009) NSWSC287² are pertinent to be noted as in these cases, very strong judgements have been passed with reference to the duties of directors and office bearers of the corporation. In these two cases, various facets of the duties that are entrusted upon the directors and office bearers of a corporation have been discussed.

It is further submitted that in order to ascertain the duties that are entrusted upon the directors and office bearers of the corporation, various scholarly journals have been referred to in order to give this discussion certain depth. The two landmark cases named above have been discussed in brief in order to ascertain various issues involved with the operations of the corporation.

Nature of the post of office bearer and director of a corporation

¹ *ASIC v Rich* (2003) 44 ACSR 682.

² *MacDonald (No 11)* (2009) NSWSC287.

Section 9 of the Corporations Act, 2001³ defines the term officer and director of the company. It is submitted in this regard, that the definition provided by section 9 of the Corporations Act, 2001 does not provide for the duties of the directors or office bearers of a company and merely refers to the appointment of the parties to the post of director or alternative director or to the post of officer. However as submitted earlier, it is being reiterated that a company operates through its officers as such and they are the ones who undertake to perform all the tasks that have to be performed by the company in management of its affairs and as such all the statutory responsibilities of a corporation have to be performed by the directors and office bearers of the company. It is submitted in this regard, that the director of a company stands in fiduciary capacity towards the company and its stakeholders. Since directors of a company are entrusted with performance of important functions including taking important financial decisions on behalf of the company and as such it is very important that all directors and officers of the company act in the best interests of the company.

Duties of Director of a corporation under General Law

Generally it is observed that entities created under the provisions of a statute are governed by the provisions of the particular law as such and in this regard it is submitted that since directors and officers of a company act in fiduciary capacity towards the corporation and its stakeholders they are entrusted with certain duties under General Law as well under the Law of Equity as the Commonwealth of Australia is a Common Law Country, the officers of the company are entrusted with certain duties under General Law as well and the same have been discussed briefly hereunder:

Duties of a director under general law are⁴:

General duties. Apart from the statutory duties imposed by the provisions of the Corporations Act, 2001 under Common Law, the directors and office bearers of a

³ Corporations Act, 2001.

⁴ Ian Ramsay, "Corporate Governance and the Duties of Company Directors", http://papers.ssrn.com/sol3/papers.cfm?abstract_id=924312&rec=1&srcabs=175664, accessed on 19th December 2010.

corporation may be subject to imposition of civil penalties in case they fail to perform their duties such as:

Exercise their powers and perform their obligations with prudence, due care and caution with the commensurate skills that they need to exercise and which they profess to hold as office bearers of the company and the standard of care⁵ would be that of any reasonable person in the same given situation. The various parameters on which the actions of directors and office bearers of the company are tested are as follows:

Whether the decision taken by the director or office bearer has been taken in good faith or not; Whether the director or the office bearer has or does not have any personal material interest in the subject matter of the decision taken on behalf of the company; Whether the director or the office bearer has made an informed judgement or the decision has been made recklessly; and Whether the director or the office bearer has acted under a bonafide belief that the judgement made by him is in the best interests of the corporation and various stakeholders of the company.

The directors and office bearers of the corporation are obligated to manage and perform the task of conducting the trade or business of the company in the best interests of the company and its stakeholders. This requirement is not a mutually exclusive requirement but the director and office bearer of the company are obligated to take the surrounding circumstances of the company such as the type of company, its size, the regulatory obligations etc in consideration.

The director and office bearers of a corporation are obliged to take all plausible and reasonable steps to ensure that they are placed in a position to monitor the management of the company and have a general understanding of the business and the dynamic economic conditions and their effect on the company.⁶

⁵ Neil Young, "Has directors' liability gone too far or not far enough? A review of the standard of conduct required of directors under sections 180-184 of the Corporations Act" (2008) 26 C&SLJ 21, <http://law.anu.edu.au/UnitUploads/LAWS8125-7700-LAWREP-026-CSLJ-JL-0216.pdf>, accessed on 19th December, 2010.

⁶ ASIC, "Directors' Responsibilities: The reality v the myths", [http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Directors_responsibilities_August2006.pdf/\\$file/Directors_responsibilities_August2006.pdf](http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Directors_responsibilities_August2006.pdf/$file/Directors_responsibilities_August2006.pdf), accessed on 19th December 2010.

Requirement to act in good faith towards the company and its stakeholders is one of the most important duties imposed on the director or office bearer of a company and this duty is both a common law duty as well as one enshrined under section 180-184 of the Corporations Act, 2001. Directors and office bearers of a company must be of conflict avoiding nature and avoid conflict of interest with that of the company's ;

Duties of Directors and Office bearers of Company under Corporations Law

Apart from the aforementioned duties of directors and office bearers of a company or corporation, there are certain statutory duties imposed upon them by the virtue of the Corporations Act, 2001. Some important provisions in this regard have been enlisted briefly as hereunder:

Section 180 of the Corporations Act, 2001:

This is one of the most important provisions of the Corporations Law in the context of director's and office bearer's duties under the statute and it imposes a duty to take reasonable care and caution and follow business judgement rule at all times while performing the functions of the company. Business judgement rule refers to taking a decision in the best interests of the company after due diligence in a manner in which a reasonable and prudent person would act in such a scenario.

Section 181 of the Corporations Act, 2001:

This section casts a duty to act in good faith at all times while acting in official capacity as the director or office bearer of the company. This rule acts both as a defence as well as a provision under which stringent liability can be imposed as this is the rudimentary requirement from the directors and office bearers of a company as they act in fiduciary capacity towards the company.

While section 182 of the Act imposes a duty not to make improper use of position to make personal gains or for someone else at the cost of company's interests, section 183 of the Act prohibits abuse of the information gained through their position to gain an advantage for themselves or cause detriment to the company.

Section 184 of the Corporations Act, 2001 is very important as it criminalises certain acts and offences committed by the directors and office bearers of the company.

Section 588G of the Act imposes a duty upon the directors and office bearers of the company not to trade when the company is insolvent or when they are of the belief that the company would definitely go bankrupt if it undertakes the particular transaction.⁷

Sections 191-195 of the Corporations Act, 2001 entrust upon the directors and office bearers of a company to disclose any material interest in the subject matter of decision to the members of board of directors in advance. Sections 285 to 318 of the Corporations Act, 2001 provide for duties pertaining maintain proper records of financial transactions and to ensure that financial reporting is being done properly.

In case the director or office bearer of a company does not perform these obligations, the courts may make a declaration of a contravention and impose a:

- Monetary penalty – a pecuniary penalty up to AUS\$200,000;
 - Disqualification order – to disqualify persons from managing companies;
- and/or
- Compensation order- to compensate the company for damage suffered by it.

Under the Corporations Act, directors and office bearers of the company may be criminally liable if they violate following provisions as per section 184 of the Corporations Act, 2001:⁸

- If the directors and office bearers of the company exercise their powers and discharge their duties recklessly or dishonestly. This omission or act must be coupled with intention or utmost recklessness in order to give birth to criminal liability; or

- Failure to prepare proper financial accounts and ensure accurate reporting of financial records.

⁷ Corporate Governance and Director's Duties In Australia, <http://www.afic.am/CG/CorporateGovernanceAndDirectors'DutiesInAustralia.pdf>, accessed on 19th December 2010.

⁸ Director's duties and responsibilities in Australia, http://www.pwc.com.au/legal/assets/GuideDirectors_Apr08.pdf, accessed on 19th December 2010.

If a director is found to be criminally liable, he may be fined up to AUS\$200,000 and/or imprisonment of up to five years.

❑ falsification of records is something which the office bearers or the directors of a company should never indulge into because making false announcements is illegal and in this regard the landmark case of ASIC v MacDonald has been discussed in the later part of this discussion. Directors and office bearers of a corporation may also be held civilly and criminally liable for such conduct under the Corporations Act.

The Corporations Act, 2001 prohibits insider trading and market rigging and any director or office bearer engaged in such activities may be subject to civil or criminal liability.

ASIC v Rich (2003) 44 ACSR 682

The aforementioned case has been a landmark case in many ways and in this case various principles regarding the disqualifications of directors were decided upon by the Supreme Court of New South Wales. In this case the main issue that had come up for the Court's consideration was whether the executive directors of One. Tel Telecommunications had failed to perform their duties in good faith and honestly in furtherance of provisions enshrined in sections 180 to 184⁹ of the Corporations Act, 2001. In this case it was alleged by ASIC that the executive directors of the company failed to perform their duties diligently in the months leading to collapse of the company. It was alleged by ASIC that the executive directors of the company violated their duties to keep the board of directors of the company about the company's solvency, true financial position of the company and the liabilities of the company prior to the collapse of the company. The Court held that the executive directors of the company had violated the provisions of section 180 of the Corporations Act, 2001. The Hon'ble Court held that Mr Keeling, the joint managing director of the company failed to properly assess the financial position of the company prior to its collapse and failed to inform the board of directors of the company about the same. In this regard, the statement of Justice Kirby when the case went before the Hon'ble High Court of Australia is incumbent to be discussed and the following is submitted as follows:

⁹ Ibid n3.

He stated that being the director of a company is a “privilege to be earned each day [which]... may be withdrawn for misconduct but also for incompetent, improper or lax activities in the functions of corporate management.”¹⁰

It is submitted that the views of Hon’ble Justice Kirby submitted above very clearly establish the nature of duties that the directors of a corporation are entrusted with. It is submitted that the aforementioned case witnessed a great expansion in the nature of the duty to act in good faith and to take the decisions of the company while keeping the best interests of the stakeholders of the company in mind. Accordingly, it is submitted that this case has established various benchmarks in regard to the duties of directors and officers of a company. In this case, the general performance of the board of directors was discussed and the manner in which the flow of information to the members of board of directors was also delved upon by the Court of Law. It is also submitted in this regard, that the court emphasised upon the need to establish a mechanism for prudent regulation of the performance of financial functions of the company. The Court laid special stress upon the need to ensure public announcement of financial information and this was one of the major issues in the instant case.

ASIC v MacDonald (No 11) (2009) NSWSC287

There were various issues in the aforementioned cases raised by the ASIC citing violation of various statutory duties enshrined in sections 180-184 of the Corporations Act, 2001 thereby contravening the duty to act in good faith and as such they were liable to be subjected to financial penalties (civil in nature). The first issue in consideration was that the Draft ASX announcement made by the company was false and it is submitted in this regard, that making false public announcements is a contravention of the provisions of the Corporations Act, 2001 and as such liable for imposition of penalties. ASIC alleged that there was failure to make declaration in regard to DOCI by the Company to ASX was also false and misleading and this action was violative section 1001 of the Corporations Act, 2001 and in this regard, the General Counsel and company secretary along with the Chief Executive Officer to advise the Board of Directors of the company that the DOCI information was required to be disclosed was violative of the duties of directors and officers of the company

¹⁰ ASIC, “Directors’ Responsibilities: The reality v the myths”, [http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Directors_responsibilities_August2006.pdf/\\$file/Directors_responsibilities_August2006.pdf](http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Directors_responsibilities_August2006.pdf/$file/Directors_responsibilities_August2006.pdf), accessed on 19th December 2010.

under section 180 of the Corporations Act, 2001 and it made them liable to imposition of civil penalties as such. Another relevant issue raised in this case was pertaining to approval of defective announcement in relation to ASX announcement by the same officer was a violation and contravention of the good faith requirement enshrined by the provisions of section 181 of the Corporations Act, 2001. The Hon'ble Supreme Court upheld a lot of ASIC's allegations against the company and in this case there were violations which had denied to the sufferers of the asbestosis disease on account of the operations of James Hardie Corporation's operations and the funds assured to be for the benefit of the sufferers of the aforementioned disease were misappropriated and false information in this regard was provided vide public announcements media announcements etc. It is submitted in this regard, that the actions of the directors and officers of the defendant company made them deserving to be penalised and the same was done quite rightly in the instant case. It is further submitted that in the instant case, there were wide ranging violations of the good faith provisions and requirements enshrined by the Corporations Act, 2001. The Hon'ble Court even held that the test of section 52 of the Trade Practices Act, 1974 was satisfied vide the draft ASX announcement and that it was definitely a violation of the provisions of the Corporations Act, 2001. In this case Hon'ble Justice Gzell also discussed the duties of directors and officers of a company from the perspective of Corporate Governance and held that 10 directors of the company along with certain officers such as the company secretary and general counsel of the company had breached the statutory duties imposed upon them vide section 180 of the Corporations Act, 2001. Public announcements made by the directors and officers of the company must be true or believed to be true after a prudent and just analysis of the facts must be made because in this case the announcements made by the company assured the victims of the operations of the James Hardie Corporation that there was adequate funds for taking care of the compensation earmarked for the aforementioned victims and as such the actions of the director and officers of the company amounted to severe and gross violation of the provisions of Corporations Act, 2001.

Conclusion

It is submitted here that a perusal of the aforementioned submissions would clarify that the directors and office bearers of a company are entrusted with onerous responsibilities and duties which they must perform with utmost sincerity and honesty

at all times because the provisions of the Corporations Act, 2001 provide for stringent action in case of statutory violations by the aforementioned members of the company. In this regard, it is submitted that in addition to the statutory duties, the directors and office bearers of the company are also saddled with common law duties and the duty to act judiciously and equitably at all times so that the sanctity of the corporation as an independent legal entity remains untarnished and moreover the trust that the shareholders and other stakeholders of the company pose in them is not shaken because as responsible members of a company, the directors and office bearers of company are obliged to act in good faith and in case they fail to do so, not only do they incur personal criminal and civil liabilities as exemplified by the landmark cases discussed above, they also let down the company that they are members of.

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