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SEMINAR

**DIRECTORS' DUTIES: RECENT DEVELOPMENTS AND  
THEIR IMPLICATIONS FOR DIRECTORS AND ADVISERS**  
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**To Whom Are the Duties of a Company Director Owed?**

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My invitation to speak at this Seminar arose out of my participation in a debate at the annual Corporate Law Workshop organized by the Business Law Section of the Law Council of Australia, which took place at Fremantle last July. The subject of the debate was the question posed by a paper given at the workshop by Professor Robert Baxt *Do Directors Owe a Duty to Employees?* The conclusion reached by Professor Baxt was that, although the law has not yet reached the stage of imposing upon a director a duty to the employees of the relevant company or to act in the interests of those employees, "*things may be changing fast.*"

After noting in his paper that the idea that directors may owe a duty to creditors is one that is probably still developing, Professor Baxt went on to predict that if Hayne J has his way,<sup>1</sup> the idea will certainly be cut back. That prediction was to be fulfilled but a few days afterwards with the decision of the majority of the High Court, of whom Hayne J was one<sup>2</sup>, in *Spies v the Queen*<sup>3</sup>.

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<sup>1</sup> Referring to the judgments of Hayne J in *Allen v Atalay* (1994) 12 ACLC 70 and *Fitzroy Football Club v Bondborough Pty Ltd* (1997) 15 ACLC 638

<sup>2</sup> The others being Gaudron, McHugh and Gummow JJ

<sup>3</sup> (2000) 74 ALJR 1263

The appellant was a director of a company, Sterling Nicholas Pty Ltd (“SN”) which was in severe financial straits and to which the appellant was indebted in a large sum. The appellant sold to SN all the shares in another company for an even larger sum and took a charge from SN to secure the balance, thus transmogrifying himself from a debtor of SN to a secured creditor of SN. The value of the shares in the other company, if they had any at all, was greatly less than the sale price.

The appellant was charged under s 176A of the *Crimes Act* 1900 (NSW) with defrauding the creditors of SN by that transaction. For whatever reason, the authorities did not charge the appellant with defrauding SN itself in contravention of s 176A, but brought an alternative charge under s 229(4) of the Companies (NSW) Code of making an improper use of his position as a director of SN to gain directly for himself an advantage.

At the trial, the appellant was convicted on the charge under s 176A, and accordingly no verdict was taken in respect of the s 229(4) charge. The NSW Court of Criminal Appeal set aside the conviction under s 176A and without ordering a new trial substituted a verdict of guilty in respect of the s 229(4) charge, in exercise of its power under s7(2) of the *Criminal Appeal Act* 1912 (NSW). The High Court in allowing the appeal ordered that the conviction under s 176A be set aside and that, if in the circumstances (the appellant having already served his sentence for the conviction) the authorities thought fit, there be a new trial of the s 229(4) charge.

The High Court majority, in a joint judgment, noted<sup>4</sup> that no doubt a person may be able to defraud the creditors of a corporation in their dealings with the corporation; but that will be because in some way or other that person has dealt with the creditor or creditors or, if he or she has not had any dealing with them, has obtained or used or prejudiced what belongs to the creditors by dishonest means. The appellant, however, had no relevant dealings with the creditors of SN and obtained no property of any creditor. Nor did he alter their legal rights. As the judgment points out<sup>5</sup>, it is not enough to constitute “defrauding” that the appellant acted dishonestly or that his or her dishonest conduct has had an effect on creditors, unless by virtue of being a director of SN he owed an independent duty to, and enforceable by, creditors of SN.

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<sup>4</sup>       ibid para [92]  
<sup>5</sup>       ibid

The majority held that he did not, citing with approval the following passage from the judgment of Gummow J in *Re New World Alliance Pty Ltd*<sup>6</sup>

“It is clear that the duty to take into account the interests of creditors is merely a restriction on the right of shareholders to ratify breaches of the duty owed to the company. The restriction is similar to that found in cases involving fraud on the minority. Where a company is insolvent or nearing insolvency, the creditors are to be seen as having a direct interest in the company and that interest cannot be overridden by the shareholders. This restriction does not, in the absence of any conferral of such right by statute, confer upon creditors any general law right against former directors of the company to recover losses suffered by those creditors ... the result is that there is a duty of imperfect obligation owed to creditors, one which the creditors cannot enforce save to the extent that the company acts on its own motion or through a liquidator.”<sup>7</sup>

The relevant paragraphs of the judgment ([93] to [97]) are appended to this paper.

In his separate judgment, Callinan J came to the same conclusion as the majority, but by a path which did not make necessary consideration of that issue.

The decision in *Spies*<sup>8</sup> may be seen as a victory of orthodoxy over emerging heresy. Almost all of the judicial pronouncements which were thought by some to give rise to an independent duty on the part of a director to creditors of the relevant company emphasized that the duties of directors were owed to the company. All that Mason J noted in *Walker v Wimborne*<sup>9</sup> was that:

“... the directors of a company in discharging their duty to the company must take account of the interest of its shareholders and its creditors ...”.

In *Linton v Tilnet Pty Ltd*<sup>10</sup> Giles JA, in delivering the judgment of the Court of Appeal (NSW) noted<sup>10</sup> cited with approval the following passage from Cooke J’s judgment in *Nicholson v Permograph Pty Ltd*<sup>11</sup>:

“The duties of directors are owed to the company. On the particular facts of particular cases this may require the directors to consider inter alia the interests of creditors. For instance, creditors are entitled to consideration in my opinion, if the company is insolvent, or near insolvent, or of doubtful solvency, or if a contemplated payment or other course of action would jeopardise its solvency.”

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<sup>6</sup> (1994) 51 FCR 425 at 444 - 445.

<sup>7</sup> (2000) 74 ALJR para [94].

<sup>8</sup> (1975) 137 CLR 1 at 7.

<sup>9</sup> (1999) 17 ACLC 619.

<sup>10</sup> *ibid* at page 626.

<sup>11</sup> (1985) 3 ACLC at 453 at 459.

Likewise, a common law duty of care was found by the NSW Court of Appeal in *Daniels v Anderson*<sup>12</sup> to reside in company directors in addition to their fiduciary duty of care; but it was a duty owed by a director in that capacity to the company. As Clarke and Scheller JJA stated it<sup>13</sup>

“We are of the opinion that a director owes to the company a duty to take reasonable care in the performance of the office.”

When one thinks about it, it could hardly be otherwise. If the law were to impose on the directors in that capacity fiduciary and other duties in favour of creditors and other third parties like individual members and employees, it would place directors in a position of inherent potential, and at times, actual conflict between the interests of such third parties and those of the company as a whole.

### **Individual members**

In *Percival v Wright*<sup>14</sup> a director of a company bought shares from a member at a price less than that for which the director knew that a third party had expressed interest in buying all of the shares in the company. The latter proposal came to nothing, but the selling member sued the director for breach of fiduciary duty to the member in not disclosing the interest expressed by the third party.

Swinfen Eady J rejected the claim, holding that the purchasing director was under no obligation to disclose to the vendor shareholders the negotiations which ultimately proved abortive.

The decision has been criticized, not because it was based on the ground that a director's fiduciary duties are owed to the company and not to individual members, but because the application of that doctrine in those circumstances led to a supposed unfairness which ultimately led to the enactment of legislation against insider trading. The decision has, however, stood for almost a century without being overruled in Britain or not followed elsewhere in the Commonwealth, except by Mahon J at first instance in *Coleman v Myers*<sup>15</sup>, as was acknowledged by Handley JA in delivering

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<sup>12</sup> (1995) 13 ACLC 614.

<sup>13</sup> at p. 665.

<sup>14</sup> [1902] 2 Ch 421

<sup>15</sup> [1977] 2 NZLR 225. The NZ Court of Appeal in *Coleman v Myers* was of the view that the decision in *Percival v Wright* was correct on the facts of the case and of the basis of concessions made by counsel for the plaintiff.

the judgment of the NSW Court of Appeal in *Bunninghausen v Glavanics*<sup>16</sup>.

Moreover, Handley JA acknowledged that “*The general principle that a director’s fiduciary duties are owed to the company and not to shareholders is undoubtedly correct, and its validity is undiminished.*”

Handley JA went on, however, to state the question in *Bunninghausen* as being “*whether the principle applies in a case, such as the present where the transaction did not concern the company, but only another shareholder.*”

After an extensive review of the decided cases since 1902, Handley JA concluded that “*the decision of a high judge in Percival v Wright should not stand in the way of recognition of ....[a] fiduciary duty owed by directors to shareholders where there are negotiations for a takeover or an acquisition of the company’s undertaking [that] would require the directors to loyally promote the joint interests of all shareholders. A conflict could only arise if they sought to prefer their personal interests to the joint interest.*”<sup>17</sup>

Bearing in mind the importance placed by Handley on the fact that the transaction in question “*did not concern the company*”, it seems to be unduly pessimistic to see the *Bunninghausen* decision as a “chink in the armour” capable of being exploited at the suit of a company’s employees.

## Employees

In *Parke v The Daily News Ltd*,<sup>18</sup> Plowman J noted that:

The view that directors, in having regard to the question what is in the best interests of their company, are entitled to take into account the interests of the employees, **irrespective of any consequential benefit to the company**, is one which may be widely held ..... But no authority to support that proposition as a proposition of law was cited to me; I know of none, and in my judgment such is not the law. (Emphasis added).

These words emphasized are important: having regard to the interests of employees in general will normally be an aspect of a director’s duty to act in the interests of the relevant company.<sup>19</sup>

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<sup>16</sup> (1999) 17 ACLC 1247 at para 43.

<sup>17</sup> *ibid* paras 107,106].

<sup>18</sup> (1962) 2 ALL ER 929.

Having regard to the decision in *Spies*, the observation by Mr. Tim Bednall<sup>20</sup> that ‘*there ... appears to be no reason why directors should not owe a duty of care to employees in certain circumstances*’ is correct only if “*certain circumstances*” refers to circumstances proved by clear evidence “*that a director is acting not as the company but as the company’s agent or servant in a way that renders him personally liable*”.<sup>21</sup>

There is the further consideration that to impose on company directors a separate duty to have regard to the interests of employees in addition to their duties to their company would amount to placing them in an inherent state of conflict between the two duties.

### **Effect of Corporations Law s 1324**

Professor Baxt’s paper made the point that little use has been made of s 1324 in developing the view that directors may owe duties to others in addition to their company. Section 1324(1) provides:

“Where a person has engaged, is engaging or is proposing to engage in conduct that constituted, constitutes or would constitute:

- (a) a contravention of this Law;
- (b) attempting to contravene this Law;

...

the Court may, on the application of [ASIC], or a person whose interests have been, are or would be affected by the conduct, grant an injunction on such terms as the Court thinks appropriate, restraining the first-mentioned person from engaging in the conduct and, if the opinion of the Court it is desirable to do so, requiring a person to do any act or thing.”,

and under s 1324(1), where the Court has power to make an order under s 1324(1) against a person, it may, in addition to or in substitution for, the grant of an injunction, order that person to pay damages to any other person.

In his Workshop Paper, Professor Baxt suggested the propositions that:

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<sup>19</sup> A point recognized by Bowen LJ, when he remarked in *Hutton v West Cork Rly Co* (1883) 23 Ch D 654 at 672: “*The law does not say that there are to be no cakes and ale [sc for employees], but that there are to be no cakes and ale except such as are required for the benefit of the company*”.

- (i) a creditor or employee is entitled to seek an injunction or damages on account of a breach by a director of the duty to have regard to the interests of creditors or employees; and
- (ii) a breach of that duty cannot be waived by members.

It is not clear that the current state of authority warrants those conclusions except, as regards (ii), at a time when the interests of creditors are at risk, which is supported by *Russell Kinsela Pty Ltd v Kinsela*<sup>22</sup> and has been upheld by the High Court in *Spies*.<sup>23</sup> Three authorities were advanced in support of proposition (i);<sup>24</sup> but all of them were decisions on interlocutory applications to have a statement of claim asserting proposition (i) struck out as not disclosing a cause of action. In each case, proposition (i) was held to be sufficiently arguable to save the statement of claim, but not a point appropriately dealt with finally on an interlocutory application. Thus, all that Hayne J felt it necessary to decide in *Allen v Atalay*<sup>25</sup> was whether it was arguable that s 1324 gives standing to an unsecured creditor. That finding was sufficient to save the statement of claim. Hayne J did not “*consider that it is appropriate to determine [the question] finally on an application for summary judgment*”<sup>26</sup>, nor did His Honour feel need to resolve the question “*Whether it is necessary or appropriate to have resort to general principles of locus standi in order to determine a question of standing under s 1324 or the statute provides its own specification of standing by its reference to ‘a person whose interests have been, are or would be affected by the conduct’*.”<sup>27</sup>

True it is that, *Airpeak Pty Ltd v Jetstream Aircraft Ltd*,<sup>28</sup> Einfeld J on a similar application actually held that a creditor has standing under s 1324 to bring claims for breach of directors’ duties under *Corporations Law*ss 232(4) and (6) as then in force.

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<sup>20</sup> In a paper *The Implications of the WA Case for Directors: Paradise or Purgatory* presented at the 1995 Corporate Law Workshop

<sup>21</sup> *Trevor Ivory Ltd v Anderson* [1992] 2 NZLR 517 at 527

<sup>22</sup> (1986) 4 ACLR 215 esp per Street CJ at p 233

<sup>23</sup> (2000) 74 ALJR para [93]

<sup>24</sup> *Allen v Atalay* (1994) 12 ACLC 7; *Airspank Pty Ltd v Jetstream Aircraft Ltd* (1997) 15 ACLC 715 and *Vanmark Holdings Pty Ltd v P W Jess & Associates Pty Ltd* (2000) 34 ACSR 222

<sup>25</sup> (1994) 12 ACLC 7.

<sup>26</sup> *ibid.* p9.

<sup>27</sup> *ibid.* p 10.

<sup>28</sup> (1997) 15 ACLC 715

In his editorial comment on *Spies*,<sup>29</sup> Professor Baxt correctly points out that the High Court did not have to consider whether a creditor is entitled to apply for and obtain a remedy under s 1324. But the majority judgment in *Spies* suggests that, at the most, a creditor might be able to obtain an injunction under s 1324 only to prevent the members of a company from ratifying a breach by its directors of statutory duty to the company to the extent that it requires them to have regard to the interest of creditors when the company is insolvent or nearing insolvency.

### **Directors' Duties owed to the State**

Thus far, this paper has been concerned with the civil law. Let us now move to the criminal law, in which can be seen an increasing tendency in recent years to impose on company directors criminal liability for crimes committed by their companies. Two justifications are commonly advanced for doing so:

- the supposed difficulty of establishing corporate criminal liability, having regard to the requirements established by the House of Lords in *Tesco Supermarkets v Natrass*<sup>30</sup> that the offence must have been committed by a senior officer of the company who represents the directing mind and will of the company; and
- that pursuing directors and managers individually will promote better corporate performance because individuals managing companies would have a vested interest in ensuring that their companies performed well in order to avoid personal criminal conviction, any resultant fines, stigma and, or worse, going to gaol.<sup>31</sup>

Criminal liability is imposed upon directors and managers for offences by their companies in one of two ways:

- a director or manager is criminally liable for the company's offence if it can be proved by the prosecution that the director participated in the offence;<sup>32</sup>

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<sup>29</sup> (2000) 18 CSLRJ 393

<sup>30</sup> [1972] AC 153

<sup>31</sup> Sue Streets *Prosecuting Directors and Managers in Australia: Brave New Response To An Old Problem* 22 MULR 693.

<sup>32</sup> eg s 494(1) of the *Environmental Protection and Biodiversity Conservation Act 1999* (Cth)

- a director or manager is criminally liable for the company's offence unless he or she proves that the contravention occurred without his or her knowledge or that he or she exercised due diligence to prevent the contravention.<sup>33</sup>

The fairness of the first approach is not beyond debate; but at least all elements of the offence must be proved by the prosecution. The second approach - strict liability unless one can prove innocence - can be thought fair only if one believes that, if a corporation commits an offence, heads must roll cost what it may.

In the light of those general comments - much more could be added in detail - I would like to conclude this paper with a short analysis of the Victorian State Government's proposed *Crimes (Industrial Manslaughter) Bill*, which was exposed for comment in early October with a deadline for comments by 3 November. The analysis formed the appendix to a submission on the Bill by the Australian Institute of Company Directors and it is included in this paper because it is important that corporate lawyers, who seldom have occasion to venture into criminal law involving death or serious personal injury, make their clients aware of this important and, in many ways, dangerous legislative adventure sooner rather than later. As the author of the analysis, I carry responsibility for its shortcomings. The analysis should, of course, be read with the proposed Bill and its accompanying explanatory memorandum at one's elbow.

### **Purposes of the Bill**

The purposes of the Bill, as stated in s1, are:

- (a) *to create new criminal offences of corporate manslaughter and negligently causing serious injury by a body corporate; and*
- (b) *to impose criminal liability on directors and senior managers of a body corporate in certain circumstances; and*
- (c) *to increase penalties in health and safety legislation; and*
- (d) *to make other miscellaneous amendments to health and safety legislation.*

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<sup>33</sup> eg s 169 of the *Protection of the Environment Operations Act 1997* (NSW)

The health and safety legislation referred to consists of the **Occupational Health and Safety Act 1985** (“OHSA”), the **Dangerous Goods Act 1985** (“DGA”) and the **Equipment (Public Safety) Act 1994** (“EPSA”). The penalties under that legislation are doubled and, in many cases, are more than doubled.

### **Strict secondary liability for company officers**

One of the miscellaneous amendments to health and safety legislation is a radical increase in potential liability of an “officer” of a body corporate where the body corporate commits an offence against OHSA.

OHSA s52(1) presently provides:

Where an offence against this Act committed by a body corporate is proved to have been committed with the consent or connivance, or to be attributable to any wilful neglect on the part of, an officer of the body corporate or person purporting to act as such an officer, that officer or person is also guilty of that offence and liable to the penalty for that offence.

For an officer of a body corporate to be convicted under that section, two things must be proved:

- that a body corporate has committed an offence against OHSA; and
- that the offence was committed with the consent or connivance, or was attributable to wilful neglect on the part of, an officer of the body corporate or a person purporting to act as such,

and the burden of proving both matters lies on the prosecution.

The Bill would repeal s52(1) and insert a new s52A(1) which provides:

if it is proved that a body corporate has committed an offence against this Act, an officer of the body corporate is guilty of that offence and liable to the penalty for that offence unless the officer proves that:

- (a) the officer was not in a position to influence the conduct of the body corporate in relation to the commission of the offence by the body corporate; or
- (b) the officer, being in a position to influence the conduct of the body corporate in relation to the commission of the offence by the body corporate, used due diligence to prevent the commission of the offence by the body corporate.

For the purposes of proposal OHSA s 52A(1), “officer” means (see s 52A(3)) in relation to a body corporate:

- (a) a director, secretary or executive officer of the body corporate;
- (b) a person in accordance with whose directions or instructions the directors of the body corporate are accustomed to act; or
- (c) a person concerned in the management of the body corporate. (s 52A(3)).

The Bill proposes corresponding amendments to DGA and EPSA.

### *Comment*

What is an “executive officer” in this context? There appears to be no definition.

It will be seen that, although the prosecution will still have the burden of proving that the relevant body corporate has committed an offence against the Act, once that is proved any *officer* of the body corporate is guilty of that offence unless he or she discharges the burden of proving (a) or (b). The penalty is 12 months imprisonment or 1500 penalty units or both.

It has in recent times become regrettably common with offences of a regulatory nature carrying a fine to impose a strict liability on company directors and executive officers, with the defence having the burden of proving lack of fault. That is unjust and contrary to inherited legal principles, even in the case of “regulatory” offences carrying a fine. It is doubly so in the case of offences, such as proposed by s 52A(1), punishable by imprisonment.

### **New Criminal Offences by Body Corporate**

The new criminal offence of corporate manslaughter is set out in clause 12 as follows:

“A body corporate which kills a person by negligence is guilty of the indictable offence of corporate manslaughter and liable to a fine not exceeding 50,000 penalty units.”

Likewise, the new criminal offence of negligently causing serious injury is to be constituted by clause 13 under which:

“A body corporate which causes serious injury [defined in Crimes Act s15 as including a combination of injuries] to another person by negligence is guilty of an indictable offence and liable to a fine not exceeding 20,000 penalty units.”

The concept of negligence for the purposes of cl 12 and 13 is expounded in proposed new s14A, under which “*the conduct of a body corporate is negligent if it involves:*

- (a) such a great falling short of the standard of care that a reasonable body corporate would exercise in the circumstances; and
- (b) such a high risk of death or (really) serious injury -

that the conduct merits criminal punishment for the offence.”

#### *Comment*

The drafting of those provisions is difficult to follow. For example:

- notwithstanding the Bill’s title, the provisions are not limited to deaths or serious injuries at the workplace; that is acknowledged in the EI (paras 27 - 30) and justified on the ground that if liability were so limited, “anomalies could result”. On the other hand, there would be even greater uncertainty about the possible applications of provisions like cls 12 and 13 outside the workplace than inside the workplace.
- the Proposed Bill appears to equate a corporation with a natural person, for example:
- although at common law a body corporate can be convicted of manslaughter through the act of a senior officer who represents the directing mind and will of the body corporate, it is (to say the least) straining language to refer to an incorporated body as itself killing or causing serious injury, and
- the adjective “reasonable” sounds odd when qualifying an incorporated body lacking a separate mind of its own.
- the usage of “really serious injury” is a tautology : when does serious injury become “really” serious injury?

- a serious and substantial fault of the provisions is to define the new, and serious, criminal offences by the yardstick of “conduct [which] merits criminal punishment”, which is subjective.

### **Negligence Elaborated**

In determining whether a body corporate is negligent, the conduct of the body corporate as a whole, or in relation to relevant activities, or both, may be considered (s14A(4)) and, s14A(5) provides that for the purpose of s14A(4) the conduct of any number of employees, agents or officers of the body corporate may be aggregated.

Under proposed s14A(6), the negligence of a body corporate may be evidenced by the failure of the body corporate:

- (a) *adequately to manage, control or supervise the conduct of one or more of its employees, agents or officers; or*
- (b) *to provide adequate systems for conveying relevant information to relevant persons in the body corporate; or*
- (c) *to take reasonable action to remedy a dangerous situation in which an officer has actual knowledge; or*
- (d) *to take reasonable action to remedy a dangerous situation identified in a written notice served on the body corporate by or under an Act.*

S14A(6) is, however, expressed to operate without limiting s14A as a whole. Nevertheless, the provision gives some indication of the sort of precautions and controls which a body corporate should put in place if the draft legislation becomes law.

### *Comment*

These provisions are difficult to follow in the following respects:

- by directing regard to be had to conduct “as a whole” whether or not in relation to “relevant activities”, by which is presumably meant the activities giving rise to the alleged offence

- the notion of aggregating conduct of “any number of” employees etc. This is an attempt to overcome the difficulties of obtaining a manslaughter verdict against a company where:
  - ◆ the alleged offence cannot be laid to the charge of a senior officer representing the directing mind and will of the company; and/or
  - ◆ the alleged manslaughter or serious injury was the consequence of a concatenation of acts or omissions by a number of persons, none of which amounting to manslaughter, with the result that the company itself cannot be convicted of manslaughter.

The notion of aggregation defies the common law principle that the criminality or otherwise of a person’s independent acts or omissions must be determined by reference only to those acts or omissions. The notion amounts to convicting two natural persons acting independently on the basis the acts or omissions of them both. The inherent unfairness of the notion is self-evident. And it must be remembered that the notion is sought to be introduced into a crime carrying severe punishment, custodial and non-custodial.

### **New Criminal Liability - Directors and Officers**

If it is proved that a body corporate has committed an offence against s12 or 13, criminal liability is imposed by s14B on any “senior officer” of the body corporate -

- (a) *who was organisationally responsible for the conduct, or part of the conduct, of the body corporate in relation to the commission of the offence by the body corporate; and*
- (b) *who, in performing or failing to perform his or her organisational responsibilities, contributed to the commission of the offence by the body corporate; and*
- (c) *who knew or ought to have known that, as a consequence of his or her conduct, there was a substantial risk that the body corporate would*

*engage in conduct that involved a high risk of death or really (sic) serious injury; and*

- (d) *whose conduct involved such a great falling short of the standard of care that a reasonable senior officer would exercise in the circumstances that the conduct merits criminal punishment for the offence.*

Criminal liability under s 14B that requires proof of four elements: organisational responsibility; contribution to the relevant body corporate's offence; knowledge (actual or constructive) of risk; and grossly negligent conduct. The burden of proof lies on the prosecution.

The penalty is imprisonment of up to five years or up to 1800 penalty units or both (corporate manslaughter) or up to two years imprisonment or 12 penalty units or both (serious injury by negligence).

### ***Senior officer***

Under proposed s14B(5), "senior officer" in relation to a body corporate means -

- (a) *director, secretary or executive officer of the body corporate;*
- (b) *a person in accordance with whose directions or instructions are directors of the body corporate are accustomed to act; or*
- (c) *a person concerned in the management of the body corporate.*

The requirement that the senior officer be 'organisationally responsible' is - as is stated in E1 para 85 - an important part of the test that is designed to cover only directors and senior managers who are actively involved in the relevant body corporate's management of the conduct which caused death or serious injury. Accordingly, in determining whether a senior officer of a body corporate is organisationally responsible for the conduct, or part of the conduct, of the body corporate in relation to the commission of the offence by the body corporate, consideration may, under s 14B(3) be given to:

- (a) *the extent to which the senior officer was in a position to make, or influence the making of, a decision concerning the manner in which the conduct, or that part of the conduct, was performed;*
- (b) *the participation of the senior officer in a decision of the board of directors of the body corporate; and*
- (c) *the degree of participation of the senior officer in the management of the body corporate.*

### **Knowledge of risk**

The third element of an offence against s 14B is that the relevant “senior officer” knew **or ought to have known** that, as a consequence of his or her conduct, there was a substantial risk that the relevant body corporate would engage in conduct that involved a high risk of death or really (*sic*) serious injury.

The E1 itself (at para 96) refers to the view that the words “or ought to have known” inappropriately impose liability on the basis of an objective test. Given that the liability sought to be imposed is criminal liability for an offence amounting to secondary manslaughter, one would have thought that view to be clearly right.

### **Additional Corporate Punishment**

It will have been seen that the new offences of corporate manslaughter (cl 12) and causing serious injury (cl 13) carry the substantial fines of up to 50,000 and 20,000 penalty units respectively. In addition to, or instead of, imposing those penalties cl 14C empowers the court to order that the relevant body corporate do any one or more of the following:

- (a) publicize as specified by the court the offence, any consequent deaths or serious injuries, and any penalties imposed;
- (b) take action specified by the court to spread the publicity in (a), eg by notice in an annual report or by notice to shareholders;

- (c) perform specified acts or establish or carry out a specified project for the public benefit (eg to develop and operate a community service) even if the project is unrelated to the offence: (cl 14C(2)).

In making such an order, the court may (*inter alia*) impose any other requirement that it considers necessary or expedient for enforcement of the order or to make the order effective (cl 14C(3)). The total cost to the body corporate of compliance with such an order must not exceed:

- for corporate manslaughter - \$5M; and
- for serious injury - \$2M.

### *Comment*

Cl 14C is contrary to the principle that a statute creating a criminal offence should specify the nature and amount (or maximum amount) of the punishment for the offence.

If s14C is to be enacted at all, it should only be on the basis that it is at the request, or with the consent, of the relevant body corporate and that an order under s14C is in lieu of a conviction and fine under cl 12 or 13.

### **If the Bill becomes law, what precautions should directors and other “senior officers” take?**

We have already noted that the provisions of the Bill about conduct evidencing negligence by a body corporate provide some guidance as to the procedures and controls which ought to be adopted to negative negligence. The same applies to the provisions defining organisational responsibility on the part of senior officers.

Nevertheless, there will inevitably be difficulty in coping with the requirement that the conduct of any number of employees be aggregated for the purpose of determining whether the body corporate has been negligent for the purposes of proposed s14A.

The larger the body corporate, the greater that problem will be. On the other hand, the larger the body corporate, the greater its ability to absorb the additional costs of establishing and maintaining corporate procedures and a corporate bureaucracy

devoted to OH and S in general, and in particular to ensuring that the precautions indicated in s 14A(6) are taken.

### **Directors' and officers' insurance**

A major problem for directors and senior officers with the Bill is that criminal liability imposed by it would be outside the cover of any directors' and officers' liability insurance. In the first place, an insurance policy insuring against a criminal liability is void at common law as being contrary to public policy: criminal law imposes penalties which, at least in part, are intended to be a deterrent, and the deterrent effect would be lessened or even eliminated if a penalty can be passed on to an insurer. In addition, many D & O policies have express exclusions in relation to criminal liability.

On the other hand, some D & O policies extend cover to the costs of defending criminal proceedings. That is not thought to be void against public policy, on the basis that everyone is presumed to be innocent until proved guilty and is entitled to a fair trial.

### **Concluding comments**

The decision of the High Court in *Spies* seems, at least for the most part, to have decided in the negative the vexed question whether directors in that capacity owe independent fiduciary or other duties to, and enforceable by, persons other than their companies. Had the Court decided otherwise directors would have been placed in a position of inherent potential, if not actual, conflict between their duties to their company and duties to an indefinite number of third parties.

Developments in statute law, however, in its ever-burgeoning quantity, are of increasing concern, not only company directors but also to the community at large. The imposition on directors of strict statutory liability for the acts or omissions of others is both inherently unfair and demonstrates a misapprehension of the role of directors in relation to the business operations of their companies. It will also inevitably make people of ability, achievement, integrity and wisdom all the less willing to assume the risks now inherent in the office of director, some of which are not insurable. It must also be remembered that the general level of fees paid by

listed Australian companies to their non-executive directors is, to say the least, by no means extravagant.

Recent tendencies in statute law in relation to company directors, involving as they do the imposition of strict liability, reversed onus of proof, imputed knowledge and other forms of what one could call legislative amorality, can perhaps be seen as reflecting the distinction between the process of the common law and the process of legislation in laying down duties and standards of conduct.<sup>34</sup>

The process of the common law is an evolutionary one, developments occurring by the decisions of judges on the basis of applying accepted principles of law to known facts in the light of forensic argument. Law, as the product of legislation, can be - and has been - seen as the attempt to design rules to govern conduct in an infinite variety of future, and hence unknowable, circumstances. It tends to be the product of prejudice, as opposed to knowledge and experience. It can thus be seen as being more revolutionary than evolutionary. At a philosophical level, the distinction reflects the distinction between the rationalism of the thinkers of the Scottish Enlightenment of the 18th century - for example David Hume, Adam Smith, Adam Ferguson - epitomized in Ferguson's observation that:

"Nations stumble upon establishments, which are indeed the result of human action, but not the execution of any human design".

and that of thinkers of the French Enlightenment - for example, Diderot, Voltaire, Rousseau, Condorcet - informed as it was by Descartes' contention that all useful institutions are and ought to be the deliberate creation of conscious reason.<sup>35</sup>

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<sup>34</sup> For an extended discussion of this widely overlooked distinction, see eg Leoni *Freedom and the Law* (Liberty Press 1991) and Hayek *Law, Legislation and Liberty* Vol. 1 (Routledge Kegan Paul (1973).

<sup>35</sup> See, e.g. Hayek "*Kinds of Rationalism*" and "*The Results of Human Action but not of Human Design*" in *Studies in Philosophy, Politics and Economics* (Routledge & Kegan Paul 1967).

## DIRECTORS' LIABILITY FOR CORPORATE CRIMINAL CONDUCT

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