

# CULPABLE CORPORATE MINDS

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*Many common law, equitable and statutory doctrines and rules concerned to regulate serious commercial misconduct require proof of the defendant's state of mind. This presents a significant hurdle where the defendant is a complex corporation, due to the current unsatisfactory state of the law's attribution rules. Building on the work of corporate theorists and legal philosophers, as well as criminal law reforms, this article proposes a novel model of corporate culpability, which conceptualises the corporate state of mind as manifested in its systems, policies and patterns of behaviour. It illustrates the value of the model by reference to the concept of dishonesty and examples of corporate misbehaviour the subject of examination by the Financial Services Royal Commission.*

## I INTRODUCTION

The private law boasts a wide array of doctrines that regulate, prohibit and remedy serious commercial wrongdoing. Often gathered under the general epithet of common law and equitable 'fraud', specific doctrines such as fraudulent misrepresentation, deceit and unconscionable dealing address a wide range of harmful behaviours. However, they all share a common demand for proof of a relevantly 'culpable mind' on the part of the perpetrator as a condition of liability. Typically, more expansive remedies are available at common law and

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in equity in response to this element of culpability, as opposed to circumstances where the defendant was merely careless or indeed entirely innocent.<sup>1</sup>

Beyond common law and equitable doctrines, commercial dealings are now also comprehensively regulated by statute. The degree to which these regimes require conscious wrongdoing varies. Many provisions do not require a state of mind but attach strict liability to the prohibited conduct.<sup>2</sup> Some statutory prohibitions invoke a mental state, targeting, for example, conduct that is 'unconscionable'<sup>3</sup> or 'dishonest'.<sup>4</sup> While, as we shall see, there are different views about what must be shown to establish dishonesty or unconscionability in a corporate setting, some baseline element of general intentionality is implicit in the prohibitions.<sup>5</sup> Other provisions, although invoking a norm of conduct, sanction the consequence of the conduct rather than the intention to engage in that conduct. In particular, the many iterations<sup>6</sup> of the core prohibition of misleading conduct<sup>7</sup> do not require proof of a mental component: the statutory norm may be contravened by defendants who neither know nor intend that their conduct is misleading.<sup>8</sup> But, as we will see, even under these statutory prohibitions, defendant culpability remains a pertinent consideration, with more onerous remedial options attaching to misleading conduct that was deliberate, dishonest or reckless, as opposed to accidental or innocent. Consistently, Commissioner Hayne in the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (the 'FSRC') described

<sup>1</sup> Eg the more generous remoteness rules for deceit, as compared to negligence: see *Palmer Bruyn & Parker Pty Limited v Parsons* (2001) 208 CLR 388, 413 [78] (Gummow J); *Doyle v Olby (Ironmongers) Ltd* [1969] 2 QB 158 (CA), 167 (Lord Denning MR); *Smith New Court Securities Ltd v Citibank NA* [1997] AC 254 (HL), 264–7 (Lord Browne Wilkinson), 283 (Lord Steyn). For examples in rescission, see Elise Bant, 'Rights and Value in Rescission: Some Implications for Unjust Enrichment' in Donal Nolan and Andrew Robertson (eds), *Rights and Private Law* (Hart Publishing, 2012) 609, 628–33.

<sup>2</sup> For example, under the *National Consumer Credit Protection Act 2009* (Cth) ('NCCP') a person is prohibited from providing credit services without a licence: NCCP s 24.

<sup>3</sup> Eg *Competition and Consumer Act 2010* (Cth) sch 2, ss 20–1 ('ACL').

<sup>4</sup> Eg *Corporations Act 2001* (Cth) s 1041G ('Corporations Act'), discussed at text to n 70.

<sup>5</sup> See below at text to n 140.

<sup>6</sup> See, eg, *Corporations Act* (n 5) s 1041H; *Australian Securities and Investment Commission Act 2001* (Cth) s 12DA; *Retail Leases Act 1994* (NSW) s 62D; *Commercial Tenancy (Retail Shops) Agreements Act 1985* (WA) s 16C.

<sup>7</sup> The core prohibition is found in s 18 of the *ACL* (n 3), previously s 52 of the *Trade Practices Act 1974* (Cth) ('TPA').

<sup>8</sup> *Parkdale Customer Built Furniture Pty Ltd v Puxu Pty Ltd* (1982) 149 CLR 191, 197 (Gibbs CJ).

egregious commercial misconduct in these serious terms where warranted, and drew attention to the expressive and deterrent value of that characterisation.<sup>9</sup>

As a matter of legal doctrine, establishing the requisite culpability against the typical modern commercial actor – the corporation – is fraught with difficulty. Traditionally, assessments of culpability are dependent upon ascertaining and characterising the defendant's state of mind. Typically, this will require an enquiry into the defendant's knowledge of the misconduct, or at least reckless indifference to it, the defendant's intention to engage in the prohibited conduct, dishonesty in undertaking the conduct, or the defendant's intention to take advantage of the plaintiff's known vulnerability. Such requirements mandate scrutiny of the defendant's internal mental state. Thus, the High Court has recently explained that, in its ordinary meaning, 'a person intends a result when they have the result in question as their purpose' and that this is a matter of 'that person's actual, subjective, state of mind'.<sup>10</sup> As we will see, this focus on individuals' states of mind likely reflects the ancient origins of the doctrines.<sup>11</sup> Courts were rightly concerned to ensure that the stigma and punitive consequences that historically attached to findings of civil fraud against natural persons were merited as a matter of individualised personal culpability.<sup>12</sup> However, this human-centric model stumbles when dealing with the complexities of modern corporate defendants, where the corporation has no natural 'mind' and the knowledge of its human agents is often dissipated through complex structures and reporting lines.

The article accordingly posits that it is time to bring a fresh perspective to private law conceptions of corporate culpability. Focusing on the challenges of proving corporate dishonesty,<sup>13</sup> it proposes a model of 'systems intentionality',

<sup>9</sup> Discussed below at text to n 59.

<sup>10</sup> *SZTAL v Minister for Immigration and Border Protection* (2017) 262 CLR 362, 372 [26]–[27] (Kiefel CJ, Nettle and Gordon JJ) 383 [67] (Edelman J) but cf 378 [47], 381 [57] (Gageler J) ('*SZTAL*') preferring an expanded conception consistent with s 5.6(1) of the *Criminal Code Act 1995* (Cth) ('*Criminal Code*'). See also *Zaburoni v The Queen* (2016) 256 CLR 482, 488 [7]–[9], 501 [55].

<sup>11</sup> See generally Peter MacDonald Eggers, *Deceit: The Lie of the Law* (Informa Law, London 2009).

<sup>12</sup> Cf 'just desert' as a theory of punishment, discussed in the context of civil penalties in Jeannie Marie Paterson and Elise Bant, 'Intuitive Synthesis and Fidelity to Purpose? Judicial Interpretation of the Discretionary Power to Award Civil Penalties under the Australian Consumer Law' in Prue Vines and M Scott Donald, (eds) *Statutory Interpretation in Private Law* (Federation Press, 2019) 154.

<sup>13</sup> Related standards that also require consideration of defendants' mental states, such as unconscionability and recklessness, must be examined separately in the interests of space. On unconscionability, see E Bant and JM Paterson, 'Systems of Misconduct: Corporate Culpability and Statutory Unconscionability' (2021) 15 *J Eq* (forthcoming).

in which the corporate mind is manifested through its corporate systems, policies and patterns of behaviour. As conceived, this model would stand alongside and supplement existing general law and statutory attribution rules.<sup>14</sup> Importantly, the proposed model aims to meet the demands of our existing general law and statutory principles, without requiring radical development of stand-alone and corporate-specific doctrines and statutory prohibitions. The model draws on insights from the criminal law context, including the work of leading scholars and philosophers, the Criminal Code's 'corporate culture' attribution provisions, as well as the recent report of the Australian Law Reform Commission (ALRC) into Corporate Criminal Responsibility.<sup>15</sup> This expansive review appears both helpful and warranted. As the ALRC has observed, it is nigh impossible to achieve any form of effective regulation of serious corporate misconduct without considering both civil and criminal law spheres.<sup>16</sup> This is particularly so given that Australia's complex regulatory system currently does not delineate between civil and criminal corporate misconduct on a principled basis, and the consequences of misconduct also fall on a spectrum and sometimes overlap.<sup>17</sup> It may be hoped that a more holistic analysis will contribute to more coherent and principled regulation of corporate misconduct generally. Finally, while the article has an Australian focus, it is clear that similar challenges face all jurisdictions sharing a common law heritage.<sup>18</sup> It is accordingly anticipated that the proposed model may be of interest in these broader reform debates.

Part 2 sets the scene for the analysis by briefly placing the current, deficient private law attribution rules in broader context. After tracing the pervasive role of state of mind requirements relevant to civil forms of commercial misconduct, it explains how existing attribution rules fail to grapple with modern corporate actors and, in particular, the phenomenon of 'diffused responsibility'. Their shortcomings are illustrated by reference to the 'fees for no service' cases and the

<sup>14</sup> The relationship between it and general law attribution models is further explored in Bant and Paterson, *ibid*.

<sup>15</sup> Australian Law Reform Commission, Parliament of Australia, *Corporate Criminal Responsibility* (Final Report No 136, April 2020) ('Final Report').

<sup>16</sup> Australian Law Reform Commission, Australian Government, *Corporate Criminal Responsibility* (Discussion Paper No 87, November 2019) [1.21] ('Discussion Paper'); *Final Report* (n 15) [1.15], [1.25].

<sup>17</sup> Most obviously in the widespread use of civil penalties, but see generally *Final Report* (n 15) Chapter 5.

<sup>18</sup> As revealed by the recent referral of the issue to the Law Commission of England and Wales: <https://www.lawcom.gov.uk/project/corporate-criminal-liability/>

challenges of providing corporate dishonesty, both the subject of extended consideration by the FSRC. Part 3 then critically explores criminal law insights on, and reforms to, corporate attribution rules. Part 4 draws on these lessons to develop a novel model of systems intentionality, returning to the 'fees for no services' cases to outline the model's operation and advantages. Part 5 concludes.

## II THE PROBLEM IN CONTEXT

### A *The Pervasive Reach and Origins of State of Mind Requirements*

Assessment of the defendant's state of mind is a critical component of both general law and statutory doctrines that regulate serious commercial misconduct. Examples, which can be broadly gathered under the umbrella of common law and equitable fraud, include deceit, fraudulent misrepresentation, injurious falsehood, knowing receipt and assistance, and unconscionability. Thus the tort of deceit requires that the defendant has made a misrepresentation knowingly or recklessly, intending to induce reliance on the part of the victim.<sup>19</sup>

In Australia, statutory schemes often attach strict liability to prohibited conduct.<sup>20</sup> Nonetheless, as under the common law, state of mind is invoked directly or indirectly in a number of prohibitions<sup>21</sup> and enforcement responses.<sup>22</sup> It also remains a central element of a number of statutory prohibitions, particularly those subject to criminal sanction. A prime example is s1041G of the *Corporations Act 2001* (Cth) ('*Corporations Act*') which prohibits conduct that is dishonest and imposes criminal and civil sanctions for contravention. The elements, operation and reform of this provision are the subject of extended consideration below.<sup>23</sup> For current purposes, it suffices to note that, under the original statutory approach, the defendant's subjective conception of dishonesty was a key element of the provision. Yet even as recently amended, it will remain necessary to assess the quality of the defendant's conduct in light of the defendant's subjective intention and knowledge. Indeed, even when a statutory prohibition is strict, state of mind may play a role in remedial relief and in the enforcement strategies available to the regulator. Thus, a defendant's state of

<sup>19</sup> *Magill v Magill* (2006) 226 CLR 551.

<sup>20</sup> Considered further below at text to n 55.

<sup>21</sup> See, eg, *ACL* (n 3) s 21.

<sup>22</sup> See, eg, *ibid* s 224, discussed immediately below.

<sup>23</sup> See text to nn 70 and 140.

mind may become highly relevant at a range of points when assessing private rights of redress or remedy,<sup>24</sup> for example, when determining the defendant's scope of liability,<sup>25</sup> or through defensive or mitigating considerations such as good faith change of position,<sup>26</sup> honest and reasonable mistake,<sup>27</sup> or apportionment of loss.<sup>28</sup> Perhaps most importantly as a matter of regulatory practice, the defendant's state of mind influences the enforcement strategies deployed by the regulator.<sup>29</sup> This concern with culpability is particularly apparent where civil pecuniary penalties are in play.<sup>30</sup> Here, courts commonly look for indicia of the defendant's blameworthiness through (amongst other factors) state of mind criteria, such as the defendant's knowledge, intention, regret or contrition.<sup>31</sup> Culpability determined by reference to the defendant's internal mental state accordingly assumes considerable significance both as a matter of general law principle and in the interpretation and enforcement of statutory regimes.

This pervasive role for state of mind requirements arguably reflects the roots of the common law and equitable doctrines that regulate commercial fraud. These go back to the 14<sup>th</sup>-18<sup>th</sup> centuries in England.<sup>32</sup> While these laws aimed or operated to regulate serious commercial wrongdoing, courts were also concerned to protect natural individuals from unmerited and overly crushing personal

<sup>24</sup> For example, through remoteness considerations, above (n 1).

<sup>25</sup> Elise Bant and Jeannie Paterson, 'Limitations on Defendant Liability for Misleading or Deceptive Conduct under Statute: Some Insights from Negligent Misstatement' in Kit Barker, Ross Grantham and Warren Swain (eds), *The Law of Misstatements: 50 Years on from Hedley Byrne v Heller* (Hart, 2015) 159.

<sup>26</sup> See, eg, the range of statutory claims considered in Elise Bant and Michael Bryan, 'Outflanking *Barnes v Addy*? The Revival of Recipient Strict Liability' (2017) 3 *J Eq* 271.

<sup>27</sup> Eg *Criminal Code* (n 10) ss 6(1) and (9); *Corporations Act* (n 4) s 1317QC. This form of defence and its relationship to strict liability is usefully discussed in: Australian Law Reform Commission, Australian Government, *Traditional Rights and Freedoms – Encroachments by Commonwealth Laws* (Final Report No 129, March 2016) ch 10 <[https://www.alrc.gov.au/wp-content/uploads/2019/08/fr\\_129ch\\_10.\\_strict\\_or\\_absolute\\_liability.pdf](https://www.alrc.gov.au/wp-content/uploads/2019/08/fr_129ch_10._strict_or_absolute_liability.pdf)>.

<sup>28</sup> Eg *Competition and Consumer Act 2010* (Cth) s 137B(d) ('CCA'), which excludes cases of fraudulently or intentionally-caused loss or damage.

<sup>29</sup> Australian Securities and Investments Commission, 'ASIC's Corporate Plan 2019-2023' (Media Release 19-229MR, 29 August 2019) <<https://asic.gov.au/about-asic/news-centre/find-a-media-release/2019-releases/19-229mr-asic-s-corporate-plan-2019-2023/>>.

<sup>30</sup> Paterson and Bant (n 13).

<sup>31</sup> See the 'French factors' developed in *Trade Practices Commission v CSR* [1991] ATPR 41-076 and now authoritative: see eg *ACCC v Singtel Optus Pty Ltd* (No 4) [2011] FCA 761, [11]; *Singtel Optus Pty Ltd v ACCC* [2012] FCAFC 20, [37] (Keane CJ, Pinn and Gilmour JJ); *ACCC v Woolworths Ltd* [2016] FCA 44. Compare *Final Report* (n 16) recommendations 9-11.

<sup>32</sup> See Eggers (n 11) ch 1.

liability. This was particularly apposite given the real potential for incarceration, and the profound and often irreparable damage to commercial and personal reputation, consequent on a finding of fraud.<sup>33</sup> Thus, courts demanded clear evidence of high levels of personal culpability on the part of defendants accused of fraud, sometimes compendiously expressed as a 'fraudulent state of mind'.<sup>34</sup> The law's development was, it seems, heavily premised on the paradigm of the individual rogue.<sup>35</sup> Yet modern, commercial miscreants are far more likely to be massive, massively complex, multi- and trans-national corporate institutions that sit within a web of related entities. This poses a range of challenges to the law's effective regulation of commercial misconduct, to which we now turn.

### B Attribution Rules, Diffused Responsibility and the Corporate State of Mind

The law's traditional focus on individuals' states of mind may have been relatively well-adapted for the particular policy concerns of former times.<sup>36</sup> However, this human-centric model fails to address the complexities of dealing with modern corporate defendants, where the corporation has no natural 'mind' and the knowledge of its human agents is often dissipated through complex, decentralised structures and reporting lines.<sup>37</sup> Moreover, there is good reason to think that group decision-making is not the sum of its individual parts, individuals within the group being motivated by collective aims and coordinated through group rules of recognition.<sup>38</sup> As the Review Committee of the Singapore Penal Code observed:

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<sup>33</sup> The most compelling accounts are Dickens': see, for example, Charles Dickens, *The Pickwick Papers* (1836) for examples of the (in)civil incarceration of small-time rogues. The wonder of it is that the law was so concerned to protect commercial entrepreneurs from the same incarceration meted out to simpler unfortunates, often wholly unaware of the reasons for their position: the subject of extended reflections in Charles Dickens, *Bleak House* (1853).

<sup>34</sup> For some modern examples, see *Dutton v O'Shane* [2003] FCAFC 195; *Ag-Exports (Australia) Pty Ltd v Export Finance and Insurance Group* [2006] NSWSC 467; *Macquarie Bank Ltd v Sixty-Fourth Throne* [1998] 3 VR 133, 144–5 (Tadgell JA).

<sup>35</sup> See generally Eggers (n 11). This is not to say that enormous corporate entities that emulated (or, indeed, rivalled) states in their financial and military powers and ambitions did not exist: see William Dalrymple, *The Anarchy: the Relentless Rise of the East India Company* (Bloomsbury, 2019).

<sup>36</sup> However, see below at text to n 83.

<sup>37</sup> See Cristina de Maglie, 'Models of Corporate Criminal Liability in Comparative Law' (2005) *Washington University Global Studies Review* 547, 559–60. See also, *Final Report* (n 15) [1.19].

<sup>38</sup> See, eg, James Gobert, 'Corporate Criminality: Four Models of Fault' (1994) 14 *Legal Studies* 393, 408; Amy MacArthur, 'Kantian Group Agency' (2019) 154 *Journal of Business Ethics* 917, 923; James Gobert and Maurice Punch, *Rethinking Corporate Crime* (LexisNexis Butterworths, 2003) 17–8, cited

Individuals in the company are part of a greater enterprise – their acts both contribute to the corporate effect and are consequences of the corporate effect. As a result, corporate decision making is often the product of organisational policies and collective procedures, not individual decisions.<sup>39</sup>

Notwithstanding this group context, private law doctrines, which are concerned to address corporate (rather than natural) responsibility for wrongdoing, tend to look for (and be derivative upon) a single human repository of fault, responsible both for the impugned conduct and carrying the requisite state of mind.<sup>40</sup> Thus, traditional attribution rules look for authorisation or approval of the impugned act in the corporation's 'directing mind and will', generally found in the board and senior managers of the company.<sup>41</sup> The broader *Meridian* gloss<sup>42</sup> examines and interprets the relevant rule of responsibility, liability or proscription to be applied to the corporate entity, to identify the specific human actor whose conduct or state of mind counts for the purposes of the attribution enquiry.<sup>43</sup> Statutory reforms tend to apply combinations of these models to promote a more expansive liability rule, which aims to extend the

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in the *Final Report* (n 15) 33. For a damning assessment of 'group think', see Mats Alvesson and André Spicer, 'A Stupidity-Based Theory of Organizations' (2012) *Journal of Management Studies* 1194.

<sup>39</sup> Penal Code Review Committee, Singapore Government, *Penal Code Review Committee Report* (Report, August 2018) [10] ('PCRC Report'), citing Richard Mays, 'Towards Corporate Fault as the Basis of Criminal Liability of Corporations' (1982) 2 *Mountbatten Journal of Legal Studies* 31, 40, 54. For the definitive critique of methodological individualism, in the context of corporate crime, see Brent Fisse and John Braithwaite, *Corporations, Crime and Accountability* (1993) ch 2.

<sup>40</sup> See Gobert (n 38). Vicarious liability is not the focus of this article, as it holds the corporation liable for the acts or wrongdoing of its employees, rather than asserting clear and independent, organisational fault: see also below at text to n 86 To the extent that it focusses on individual misconduct, it also struggles to address the problem of diffused responsibility (as reflected in proposals for 'aggregation' principles, addressed immediately below).

<sup>41</sup> *Lennard's Carrying Co v Asiatic Petroleum Co Ltd* [1915] AC 705, 713; *HL Boulton (Engineering) Co Ltd v TJ Graham and Sons Ltd* [1957] 1 QB 159, 172 (Lord Denning); *Tesco Supermarkets Ltd v Nattrass* [1972] AC 153, 170 (Lord Reid) ('Tesco').

<sup>42</sup> Named after *Meridian Global Funds Management Asia Ltd v The Securities Commission Co* [1995] 2 AC 500, see especially at 91 (Lord Hoffmann). *Meridian* has been endorsed in Australia in *Director of Public Prosecutions Reference No 1 of 1996* [1998] 3 VR 352, 355 (Callaway JA, with whom Phillips CJ and Tadgell JA agreed), cited with approval in *Commonwealth Bank of Australia v Kojic* (2016) 249 FCR 421, 445–6 [99] (Edelman J) ('Kojic'). See also *Jin v Knox Property Investment Limited* [2016] NZCA 565, [26]; *Ho Kang Peng v Scintronix Corp Ltd* [2014] 3 SLR 329, [47]–[50]; *Moulin Global Eyecare Trading Limited v Commissioner of Inland Revenue* (2014) 17 HKCFAR 218, [40]. The approach is closely critiqued in Rachel Leow, *Corporate Attribution in Private Law* (Hart Publishing, 2022) (forthcoming) and Rachel Leow, 'Equity's Attribution Rules' (2021) 15 *J Eq* (forthcoming).

<sup>43</sup> *ASIC v Westpac Banking Corp (No 2)* (2018) 357 ALR 240, [1660] (Beach J).

operation of traditional attribution principles.<sup>44</sup> The broader difficulties and limitations of this hodgepodge of rules are well-examined elsewhere, including most recently by the ALRC.<sup>45</sup> For present purposes, it suffices to note, that in most cases, corporate responsibility depends upon the identification of an individual human repository of fault.<sup>46</sup> This unity is often elusive in large, complex corporations, where activities will typically be shared between multiple departments, employees and agents (including corporate agents), and where those who hold pertinent knowledge or intention may be significantly separated from that conduct by corporate structures and time. In this respect, derivative models of liability create the conditions for diffusion and evasion of responsibility for corporate acts (the 'diffused responsibility' problem).<sup>47</sup>

The use of automated processes to carry out core activities, such as payment and accounting systems, only adds to the challenges of attribution.<sup>48</sup> In this context, there is a high degree of uncertainty as to who to look to in finding the requisite intent. Is it the programmer<sup>49</sup> – who may be a very small and uninformed cog in the corporate wheel? Or is it the manager who oversaw the implementation of the automated process? Or the person managing the process inputs, such as key customer data, decisions about pricing, or the management of risk associated with individual customers?

A consequence of this collision of human models of liability and the realities of modern commerce is that large corporations may be disproportionately protected from the full legal consequences of their misconduct.<sup>50</sup>

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<sup>44</sup> *TPC v Tubemakers of Australia Ltd* (1983) 47 ALR 791, 737–8 (Toohey J) ('Tubemakers'); *Final Report* (n 15) ch 3. For a Canadian example, see the attribution rules laid out in s 22 of the *Criminal Code*, RSC 1985, in particular s 22.2 ('Canadian Criminal Code').

<sup>45</sup> *Final Report* (n 15) ch 7.

<sup>46</sup> Eric Colvin, 'Corporate Personality and Criminal Liability' (1995) 6 *Criminal Law Forum* 1, 1–2; Meaghan Wilkinson, 'Corporate Criminal Liability. The Move Towards Recognising Genuine Corporate Fault' (2003) 9 *Canterbury Law Review* 142.

<sup>47</sup> Brent Fisse, 'Reconstructing Corporate Criminal Law: Deterrence, Retribution, Fault, and Sanctions' (1983) 56 *Southern California Law Review* 1141, 1189.

<sup>48</sup> These systems are determinative in the sense of performing an action on preprogrammed situations. Attribution problems may only compound as algorithmic decision making systems are introduced into corporate processes. For important discussions on this developing challenge, see Mihailis Diamantis, 'The Extended Corporate Mind: When Corporations Use AI to Break the Law' (2020) 98 *North Carolina Law Review* 893; Brent Fisse, 'Algorithmic Market Coordination' (2018) 46 *ABLR* 210, and below at text to n 161.

<sup>49</sup> Cf *Quoine Pte Ltd v B2C2 Ltd* [2020] SGCA (I) 02 ('Quoine').

<sup>50</sup> *PCRC Report* (n 39) [12]; *Final Report* (n 15) [6.38].

In completing this brief survey, it is worth noting that, in theory, it would be possible for the law to 'aggregate', for the purposes of attribution, the acts and knowledge of associates who, for example, individually know of some act or practice but fail to appreciate that it forms part of broader misconduct. Some US courts have adopted this route as a way of overcoming the diffused responsibility problem.<sup>51</sup> In general, however, aggregation has failed to take root in the US and has been treated with caution in other jurisdictions.<sup>52</sup> A key concern has been well-expressed by Edelman J:

[A]n aggregation principle could undermine the fundamental question to be asked .... "is the conduct unconscionable"? It is not easy to see how a corporation, which can only act through natural persons, can engage in unconscionable conduct when none of those natural persons acts unconscionably. Similar reasoning has led courts to reject submissions that a corporation has acted fraudulently where no individual has done so (in instances of deceit) and that a corporation has acted contumeliously where no individual has done so (in cases of exemplary damages).<sup>53</sup>

### C Ramifications: Fees For No Services and Charging Dead People

It is helpful here to pause, to observe the practical ramifications of the current, unwieldy combination of the mental elements of fraud and the deficient operation of our current rules of attribution. In Australia, one of the most striking consequences is apparent from the enforcement practices adopted by regulators. The FSRC provided salient examples, prominently including in the so-called 'fees for no service' cases.<sup>54</sup> In these scenarios, financial service providers (FSPs) charged clients fees over extended periods for financial advice

<sup>51</sup> *United States v Bank of New England*, NA, 821 F 2d 844 (1st Cir 1987). See further Gobert (n 38) 405.

<sup>52</sup> See in particular *Kojic* (n 42) 446 [101], 448–56 [110]–[143] (Edelman J, with whom Allsop CJ generally concurred); *R v H M Coroner for East Kent, ex parte* (1989) 88 Cr App R 10. For some limited, statutory examples, see *Criminal Code* (n 10) 12.3, noted in *Final Report* (n 15) [6.70]–[6.71]; *Canadian Criminal Code* (n 44) s 22.1.

<sup>53</sup> *Kojic* (n 42) 449 [112] (Edelman J, with whom Allsop J generally agreed at [31], but see also 438 [66] (Allsop P) and [81]–[84] (Besanko J)). Edelman J has additionally suggested that some statutory attribution rules (such as TPA (n 8) s 84 and its equivalents), may on their terms additionally impede judicial development of any theory of aggregation: *Kojic* (n 42) 448–9 [110]–[111] (Edelman J) but cf 438 [65] (Allsop CJ) and 441 [81] (Besanko J). See further *Australian Competition and Consumer Commission v Radio Rentals Ltd* (2005) 146 FCR 292, 325–6 [177]–[181] (Finn J); *Fisse* (n 47) 1189–90; *Final Report* (n 15) [4.83]–[4.87].

<sup>54</sup> *Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* (Final Report, February 2019) vol 1, 150–1 ('FSRC Final Report').

in circumstances where no advisor had been allocated to the client. In another, FSPs charged service fees to clients notwithstanding having received notice of their death ('charging dead people').

There are a number of ways potentially to characterise the wrong occasioned by such conduct: it may involve a breach of contract, misrepresentation, mistake or deceit and may engage a range of analogous statutory claims. Each avenue of claim has strengths and weaknesses, particularly (for current purposes) in terms of state of mind requirements on the part of the defendant and corresponding remedial consequences. Breach of contract, for example, typically does not require a mental element, while misrepresentation may be 'innocent',<sup>55</sup> and deceit looks to a culpable state of mind. In terms of private rights of redress, the core, desired remedy is likely to be compensation for the deducted fees. This may well make strict liability claims such as contract and the statutory prohibition against misleading conduct attractive from the perspective of individual claimants.

By contrast, faced with protracted and egregious conduct of this kind, the regulatory goal may be to impose a sanction that acts as an effective deterrent against further misconduct.<sup>56</sup> This may even involve punishing the corporation for its transgressions. Here, there are a number of statutory contraventions that may be applicable: including the prohibitions identified earlier on conduct that is dishonest<sup>57</sup> or the licensing requirement to provide financial services 'efficiently, honestly and fairly'.<sup>58</sup>

<sup>55</sup> *Tanwar Enterprises Pty Ltd v Cauchi* (2003) 217 CLR 315, 325 [25] (Gleeson CJ, McHugh, Gummow, Hayne and Heydon JJ).

<sup>56</sup> Noting that ASIC has used its enforcement powers also to seek compensation for injured customers: see, eg, Australian Securities and Investments Commission, 'ASIC Secures over 160 million in remediation for junk consumer credit insurance' (Media Release 20-115MR, 13 May 2020) <<https://asic.gov.au/about-asic/news-centre/find-a-media-release/2020-releases/20-115mr-asic-secures-over-160-million-in-remediation-for-junk-consumer-credit-insurance/>>.

<sup>57</sup> *Corporations Act* (n 4) s 1401G.

<sup>58</sup> *Ibid* s 912A. In *Australian Securities and Investments Commission v MLC Nominees Pty Ltd* [2020] FCA 1306 ('MLC Nominees'), contravention of s912A was admitted, but penalties awarded in respect of misleading conduct. Here, 'deliberateness' was recognised as a primary consideration, but was not alleged by ASIC and was accepted by Yates J to be unsupported by the stated facts: see [180], [197], [217], [243], [270], [306]. See also Australian Securities and Investments Commission, 'ASIC Commences Civil Penalty Proceedings against StatePlus Super for Charging fees for no Service' (Media Release 220-189MR, 20 August 2020) <<https://asic.gov.au/about-asic/news-centre/find-a-media-release/2020-releases/20-189mr-asic-commences-civil-penalty-proceedings-against-stateplus-super-for-charging-fees-for-no-service/>>; Australian Securities and Investments Commission, 'ASIC Commences Civil Penalty Proceedings Against BT Funds Management and Asgard Capital Management for Charging Fees for no Service and Misleading Statements' (Media Release 20-190MR,

However, regulators have faced a significant hurdle in satisfying the mental aspect of dishonesty-based claims. Factually, a striking issue in these cases is that, in many instances, the impugned fees were deducted by FSPs through automated payment systems, with the result that there were, potentially, no humans engaged with each impugned 'taking' of fees. Further, while natural individuals may have appreciated, at some point, that a client had received no advice, or had died, it is another matter to connect that person's knowledge to the automated 'conduct', or bring the knowledge home to a member of the corporation's senior management team. The employee who receives the phone call advising of the client's death may well reasonably assume that, by recording that call on the corporate database, the information will be shared with the relevant corporate department and may have little, personal understanding of its potential legal significance.

Given these features, it is perhaps unsurprising that FSPs sought to characterise these kinds of cases to the FSRC as involving merely 'poor systems and carelessness'<sup>59</sup> and that regulators initially focused on remediation, rather than denunciation and penalty.<sup>60</sup> While the latter may appear to be a pragmatic and sensible response, the danger is that it undermines effective, public denunciation of the misconduct and both specific and general deterrence. For example, studies into corporate responsibility indicate that corporations' perceptions of the reputational risks of misconduct will often be influential in deterring corporate misconduct.<sup>61</sup> Where conduct is characterised as involving mistake or systems errors, this expresses a wholly distinct and significantly lower level of blameworthiness. Consistently, in its Final Report, the FSRC roundly criticised this 'narrative':

The amounts of money that just 'fell into the pocket' of so many large and sophisticated financial entities, the number of times it happened, and the many

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<sup>58</sup> 20 August 2020) <<https://asic.gov.au/about-asic/news-centre/find-a-media-release/2020-releases/20190mr-asic-commences-civil-penalty-proceedings-against-bt-funds-management-and-asgard-capital-management-for-charging-fees-for-no-service-and-misleading-statements/>>.

<sup>59</sup> FSRC Final Report (n 54) 139. See, eg, Megan Neil, 'NAB Says Fees for no Service not Dishonest', *Guardian News* (online, 26 November 2018)

<<https://www.nambuccaguardian.com.au/story/5778688/nab-says-fees-for-no-service-not-dishonest/>>.

<sup>60</sup> FSRC Final Report (n 54) 145–50.

<sup>61</sup> See, eg, Christine Parker and Vibeke Lehmann Nielsen, 'How Much Does It Hurt? How Australian Business Think About the Costs and Gains of Compliance and Noncompliance with the *Trade Practices Act*' (2008) 32 *Melbourne University Law Review* 554.

years over which it happened, show that it cannot be swept aside as no more than bumbling incompetence or the product of poor computer systems.<sup>62</sup>

The Final Report highlighted, by way of example of this evasive strategy, the case of one senior executive of a leading final institution,<sup>63</sup> who accepted that deducting fees for no service was dishonest conduct, but asserted that no-one knew this was happening. The money just kept ‘falling into NAB’s pocket’.<sup>64</sup> Even when this conduct, widespread in the industry, began to be called to account, the focus of both regulator and perpetrators were on remediation, or compensation for the misconduct. Here, again, the characterisation of the conduct was all-important in shaping their approach: ‘the conduct was treated as if it was no more than a series of inadvertent slips brought about by some want of care in record keeping’.<sup>65</sup> Remediation efforts were typically slow, sporadic and inefficient. Again, this is unsurprising, given this classification of the conduct in terms of mere carelessness or error. Where the reputational risk is low, corporations will continue profitable patterns of misconduct<sup>66</sup> and, one might add, show contempt for regulators and the rule of law.<sup>67</sup>

Arguably, then, a more effective deterrent strategy, and some would say accurate characterisation of the conduct, would be to focus on its egregious nature. One possibility is the general licensing obligation in s 912A of the *Corporations Act*, which requires those holding financial services licences ‘to do all things necessary to ensure that the financial services covered by the licence are provided efficiently, honestly and fairly’. This route may be particularly attractive now that these elements have been interpreted to be disaggregated, rather than cumulative, requirements.<sup>68</sup> Thus it may be enough to show that the conduct was not honest, or efficient, or fair, to contravene the section.

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<sup>62</sup> FSRC Final Report (n 54) 139.

<sup>63</sup> Mr Thorburn of National Australia Bank.

<sup>64</sup> FSRC Final Report (n 54) 139.

<sup>65</sup> *Ibid* 150.

<sup>66</sup> *Discussion Paper* (n 16) [4.47], [9.60], [10.53], for this reason also exploring non-monetary penalty options and [2.30], [2.39]–[2.43], noting the particular expressive stigma associated with criminal conviction.

<sup>67</sup> See the examples collated in Elise Bant, ‘Misleading Conduct? So What?’, *Pursuit* (online, 25 September 2018) <<https://pursuit.unimelb.edu.au/articles/misleading-conduct-so-what>>.

<sup>68</sup> ASIC v Westpac [2019] FCAFC 187. Cf *MLC Nominees* (n 58) [50].

It may be questioned whether findings of endemic failures to attain efficiency and even fairness have the same expressive power as findings of dishonesty.<sup>69</sup> However, if a finding of dishonesty is the goal, there remains the hurdle of attributing dishonesty to a corporation in these factual scenarios. Consistently with its expressed concern that the longstanding 'fees for no service' and 'charging dead people' scenarios have been inappropriately characterised, with deleterious remedial and regulatory consequences, the FSRC Final Report closely considered whether and how FSPs engaging in this conduct could be considered to have engaged in contraventions of s 1041G of the *Corporations Act*.<sup>70</sup> Section 1311(1) of the *Corporations Act* makes that contravention an offence. At the relevant time, s 1041G stated:

(1) A person must not, in the course of carrying on a financial services business in this jurisdiction, engage in dishonest conduct in relation to a financial product or financial service.

(2) In this section:

Dishonest means:

(a) dishonest according to the standards of ordinary people; and

(b) known by the person to be dishonest according to the standards of ordinary people.

The second limb of the statutory definition of dishonesty, which presents a significant state of mind attribution hurdle, has since been removed.<sup>71</sup> However, the original definition will continue to apply to claims that relate to events prior to the reforms, such as the fees for no services scenarios. Moreover, the *Ghosh* test of dishonesty,<sup>72</sup> from which it derives, continues to find sporadic statutory and judicial expression in a range of other contexts, including under the *Criminal Code*.<sup>73</sup> Whether this will be rectified through wholesale legislative revision, as currently proposed under the *Crimes Legislation Amendment (Combatting*

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<sup>69</sup> The same follows if there is a distinction, as has been suggested, between dishonesty and a failure to act honestly: *Australian Securities and Investments Commission v Australia and New Zealand Banking Group Ltd (No 3)* [2020] FCA 1421 [62] (Allsop CJ).

<sup>70</sup> FSRC Final Report (n 54) 151–7.

<sup>71</sup> See *Corporations Act* (n 4) s 9.

<sup>72</sup> Named after *R v Ghosh* [1982] QB 1053 ('Ghosh').

<sup>73</sup> See, eg. *Criminal Code* (n 10) s 130.3, s 270.2, s 474.1, s 480.2.

*Corporate Crime) Bill 2019* (Cth), remains to be seen.<sup>74</sup> The acute challenges of establishing corporate dishonesty in these terms therefore merits close examination.

On the issue of knowledge, s 769B of the *Corporations Act* uses a model, also adopted under the *Trade Practices Act/Competition and Consumer Act*,<sup>75</sup> which deems conduct of certain employees agents or officers to be that of the company and attributes 'any state of mind' of certain employees, agents or officers to the company.<sup>76</sup> It is generally understood that such statutory attribution models are designed to extend the narrow application of the traditional common law rules.<sup>77</sup>

However, notwithstanding its ameliorative aims, the statutory provision, like its general law counterparts, generally requires that conduct and state of mind elements be united in one identified specific employee or agent. Assuming that the fee deductions (in Commissioner Hayne's potent language, the 'takings') could successfully be attributed to the FSP, the second limb of s 1041G(2), as it applied at the time of the misconduct, required identification of a human individual involved in that conduct, who was aware of the taking and, furthermore, that the individual realised that the taking was dishonest according to community standards. Commissioner Hayne's analysis sought to address the challenge of this second limb by emphasising the truism, articulated in *Ghosh*, that '[i]n most cases, where the actions are obviously dishonest by ordinary standards, there will be no doubt about it. It will be obvious that the defendant himself knew that he was acting dishonestly.'<sup>78</sup> But this approach appears to assume that it will be possible to identify a single human aware of, and carrying out the conduct. In reality, this responsibility is likely to be dispersed across a number of different divisions in a corporate structure – with those managing

<sup>74</sup> For the range of arguments, see David Lusty, 'The Meaning of Dishonesty in Australia' (2012) 36 *Criminal Law Journal* 282, favouring wholesale reform; *Ivey v Genting Casinos (UK) Ltd* [2018] AC 391 [63] (Lord Hughes, with whom Lord Neuberger, Lady Hale, Lord Kerr and Lord Thomas agreed) ('Ivey') arguing that there can be 'no logical or principled basis for the meaning of dishonesty... to differ according to whether it arises in a civil action or a criminal prosecution' and *Final Report* (n 15) [6.66]; and, recommending caution, Jeremy Gans, Submission to Legal and Constitutional Affairs Legislation Committee, *Inquiry into the Crimes Legislation Amendment (Combatting Corporate Crime) Bill 2019* (12 December 2019).

<sup>75</sup> The variations of what the ALRC terms the 'TPA Model' are mapped in *Final Report* (n 15) ch 3, see also 121.

<sup>76</sup> *Tubemakers* (n 44) 737–8. The more novel 'corporate culture' provisions found in the *Criminal Code* (n 10), to which we return below, are excluded.

<sup>77</sup> *Kojic* (n 42); *Discussion Paper* (n 16) [5.80].

<sup>78</sup> *FSRC Final Report* (n 55) 157, citing *Ghosh* (n 72), 1064 (Lord Lane CJ).

payments separated from those dealing with individual clients and record keeping - and, moreover, the payments will often have been effected by automated systems. Clearly, as Commission Hayne also observed, establishing that impugned payments were made in conformity with established systems precludes any claim of accident.<sup>79</sup> But unless the deficiencies of the payment or business system in question were a deliberate part of its design,<sup>80</sup> the requisite state of mind on the part of individual employees is likely to come in the form of an understanding of the deficiencies of the system coupled with a failure to act. Again, as described earlier, this combination may be spread across different actors at very different levels in the managerial hierarchy. One officer of the company may realise that payments for services rendered should no longer be deducted from a client's account. Another may understand that the payment system does not adjust to changes in the circumstances of individual clients without human intervention. But those two pieces of information may not at any time be actually combined.

Commissioner Hayne also rightly emphasised the shift in evidential burden that flows from the usual inference of knowledge:

As Toohey and Gaudron JJ said in *Peters v The Queen* (1998) 192 CLR 493, 509 [31]: 'As a matter of ordinary experience, it will generally be inferred from an agreement to use dishonest means to deprive another of his or her property or to imperil his or her rights or interests that the parties to that agreement knew that they had no right to that property or to prejudice those rights or interests. And as with the defence of honest claim of legal right, it will be taken there is no issue in that regard unless the absence of knowledge or, which is the same thing, belief as to legal right is specifically raised and there is some evidence to that effect'<sup>81</sup>

While, again, this is no doubt true, it may be doubted whether only a countervailing 'claim of right' will displace the usual inference. Rather, claims of mistake, systems error and negligence are precisely the sort of claims that, if accepted on their face,<sup>82</sup> may be made in order to raise serious doubt about the subjective dishonesty of the corporation's employees and, through them, the corporation itself. The risk that they may succeed is important when criminal charges are under consideration, particularly given the requirements of

<sup>79</sup> *Ibid* 157.

<sup>80</sup> *Quoine* (n 49).

<sup>81</sup> *FSRC Final Report* (n 54) 156, n 147.

<sup>82</sup> We return to the cogency of claims of 'systems errors' below, at text following n 169.

regulators and prosecutors as ‘model litigants’. All in all, it seems, it will be very challenging to establish corporate dishonesty on these facts, without some significant reform to our existing attribution rules.

### III INSIGHTS FROM CRIMINAL LAW DEVELOPMENTS AND REFORMS

#### A Early Moves

In considering options for reform, the criminal law offers some valuable attribution models, and deep academic insight, which are well worth considering. While civil law was late in attributing culpable states of mind to companies, courts took even longer to consider it possible for corporations to commit crimes.<sup>83</sup> Eventually, the clear need to hold corporations responsible for the egregious harms they were capable of causing necessitated the shift.<sup>84</sup> In general, this was managed simply by wholesale adoption of the attribution and liability rules used in the law of torts.<sup>85</sup> This led, in the US, to the use of vicarious liability rules to establish corporate criminal liability,<sup>86</sup> an approach that has been criticised on the ground that liability is not grounded in the corporation’s own wrongdoing.<sup>87</sup> Rather, courts in most common law jurisdictions (including some in the US, following the Model Penal Code)<sup>88</sup> now prefer the ‘direct’ or organic model of attribution outlined earlier,<sup>89</sup> or a statutory model designed to expand

<sup>83</sup> See, eg, Blackstone, *Commentaries on the Law of England* (1769) vol 1, 464–5; LH Leigh, *The Criminal Liability of Corporations in English Law* (Weidenfeld and Nicolson, 1969) 3–14.

<sup>84</sup> *New York Central & Hudson River Railroad Co v United States*, 212 US 481 (1909) (‘New York Central’). In England, see *Director of Public Prosecutions v Kent and Sussex Contractors Ltd* [1944] KB 146; *R v ICR Haulage Co Ltd* [1944] KB 551; *Moore v I Bresler Ltd* [1944] 2 All ER 515, examined in Wilkinson (n 46).

<sup>85</sup> Judge Learned Hand in *United States v Nearing* 252 F 223, 231 (SD NY, 1918) stated that there is ‘no distinction in essence between the civil and criminal liability of corporations ... [e]ach is merely an imputation to the corporation of the mental condition of its agents’.

<sup>86</sup> *New York Central* (n 84). See also *Mousell Bros v London and North-Western Railway Co* [1917] 2 KB 836. In Australia, vicarious liability was applied by the High Court in *R v Australasian Films Ltd* (1921) 29 CLR 195, 217 and *Morgan v Babcock & Wilcox* (1929) 43 CLR 163.

<sup>87</sup> *Final Report* (n 15) [4.50]–[4.57]. It remains contentious in Australia whether vicarious liability entails that the corporation is responsible for the act of another, or the wrong of another: see *Pioneer Mortgage Services Pty Ltd v Columbus Capital Pty Ltd* [2016] FCAFC 78, (2016) 250 FCR 136 [48]–[58] (Davies, Gleeson and Edelman JJ).

<sup>88</sup> The American Law Institute, *US Model Penal Code* (1985), discussed in *Discussion Paper* (n 17) 114–5; Gerhard OW Mueller, ‘Mens Rea and the Corporation: A Study of the Model Penal Code Position on Corporate Criminal Liability’ (1957) 19 *University of Pittsburgh Law Review* 21; Peter A French, *Collective and Corporate Responsibility* (Columbia University Press, 1984) ch 13.

<sup>89</sup> *Tesco* (n 41), approved in Australia by the High Court in *Hamilton v Whitehead* (1988) 166 CLR 121.

the reach of traditional attribution rules. Countries have experimented with combinations of the two. A common statutory model adopted in Australia combines a modified vicarious liability limb for attribution of conduct with a liberal organic attribution rule for state of mind requirements, in an effort to expand the reach of statutory prohibitions and requirements to corporate defendants.<sup>90</sup> An example, mentioned earlier, is s 769B of the *Corporations Act*. All these share the same deficiencies, identified previously, in addressing the problem of diffused responsibility as their civil law counterparts.

### B *The Concept of a Culpable Corporate Culture*

Faced with the unsatisfactory state of corporate criminal responsibility, Part 2.5 of the *Criminal Code* introduced a strikingly different approach. It modestly expanded the range of humans whose state of mind could be attributed to the company beyond the traditional 'directing mind and will'. But more radically, it also developed a conception of organisational fault, through what have commonly become known as the 'corporate culture' provisions. Section 12.3 of the *Criminal Code* contains the key provisions:<sup>91</sup>

#### 12.3 Fault elements other than negligence

(1) If intention, knowledge or recklessness is a fault element in relation to a physical element of an offence, that fault element must be attributed to a body corporate that expressly, tacitly or impliedly authorised or permitted the commission of the offence.

(2) The means by which such an authorisation or permission may be established include:

...

(c) proving that a corporate culture existed within the body corporate that directed, encouraged, tolerated or led to non-compliance with the relevant provision; or

(d) proving that the body corporate failed to create and maintain a corporate culture that required compliance with the relevant provision.

...

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<sup>90</sup> *Final Report* (n 15) ch 3.

<sup>91</sup> See generally S Odgers, *Principles of Federal Criminal Law* (4<sup>th</sup> ed, Thomson Reuters, Pyrmont 2019) Ch 12.

(4) Factors relevant to the application of paragraph (2)(c) or (d) include:

- (a) whether authority to commit an offence of the same or a similar character had been given by a high managerial agent of the body corporate; and
- (b) whether the employee, agent or officer of the body corporate who committed the offence believed on reasonable grounds, or entertained a reasonable expectation, that a high managerial agent of the body corporate would have authorised or permitted the commission of the offence.

...

(6) In this section:

**"corporate culture"** means an attitude, policy, rule, course of conduct or practice existing within the body corporate generally or in the part of the body corporate in which the relevant activities takes place.

**"high managerial agent"** means an employee, agent or officer of the body corporate with duties of such responsibility that his or her conduct may fairly be assumed to represent the body corporate's policy.

As a matter of theory, and building on the ground-breaking work of leading scholars such as Bucy, French and Fisse, the Model Criminal Code Officers Committee considered that corporate culture was 'analogous to intention'.<sup>92</sup> Its revolutionary approach takes seriously Bucy's insight that corporations develop their own character and values and should be treated as actors in our society in their own right.<sup>93</sup> As Peter A French argued, corporate intentions may be identified from decisions and choices that are communicated through corporate policy.<sup>94</sup> The reform also reflects Fisse's powerful concept of 'reactive corporate fault'.<sup>95</sup> This recognises organisational blameworthiness where a corporation fails to undertake reasonable corrective or remedial measures in relation to

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<sup>92</sup> Criminal Law Officers Committee of the Standing Committee of Attorneys-General, Australian Government, *Model Criminal Code* (Final Report, December 1992) chs 1 and 2, 21, 107 ('CLAC Report'). See also Olivia Dixon, 'Corporate Criminal Liability: The Influence of Corporate Culture' (Sydney Law School Legal Studies Research Paper No 17/14, University of Sydney, February 2017), 7 <<http://ssrn.com/abstract=2921698>>.

<sup>93</sup> Pamela H Bucy, 'Corporate Ethos: A Standard for Imposing Corporate Criminal Liability' (1991) 75 *Minnesota Law Review* 1095.

<sup>94</sup> French (n 88); Peter A French, 'Integrity, Intentions and Corporations' (1996) 34(2) *American Business Law Journal* 141, 152.

<sup>95</sup> Fisse (n 47) 1195-2013.

harmful conduct undertaken by personnel on its behalf.<sup>96</sup> On this approach, where there is an express or implied corporate policy to fail to take preventive or corrective reactive measures, this may reflect deliberate or reckless organisational intentionality.<sup>97</sup> These organisational theories both substantiate and reflect our lived reality of the power and impact of corporate citizens.

And, as a matter of practice, this approach makes considerable sense, given that looking for a natural person on which to pin egregious misconduct overlooks the fact that in a corporation of any size, staff routinely leave, are transferred to other roles, are fired, promoted or resign. What remains constant are the company's structures, policies and processes that dictate how the next round of employees should act when engaged in the corporation's activities. And, consistently with this observation, in many cases, the real problem is not what any one person did, knew or intended, but that the corporation's overall or localised systems, policies and procedures were highly flawed and inherently likely to encourage or result in misconduct. The concept also recognises the problem of complex, dispersed and decentralised corporate structures discussed earlier.<sup>98</sup>

Notwithstanding their attractions, the corporate culture provisions have very rarely been used and never been fully considered by courts.<sup>99</sup> As a result, there is significant uncertainty over how they will operate in practice. There are likely a number of reasons for this. The provisions have been largely excised or excluded (without explanation) from operation in relation to key statutory schemes, and, in any event, only apply to commonwealth crimes. They have not been enacted at state and territory levels. One reason for prosecutorial caution where they do apply may well be that the references to 'offence' throughout the provisions indicate that it is still necessary to find that the relevant offence has been

<sup>96</sup> See further, Brent Fisse, 'The Attribution of Criminal Liability to Corporations: A Statutory Model' (1991) 13 *Sydney Law Review* 277; Brent Fisse, 'Recent Developments in Corporate Criminal Law and Corporate Liability to Monetary Penalties' (1990) 13 *University of New South Wales Law Journal* 1; Fisse and Braithwaite (n 39) 47–9. Arguably, the concept of corporate negligence underpins the idea of corporate culture: see B Fisse, 'The Social Policy of Corporate Criminal Responsibility' (1978) 8 *Adelaide LR* 361, 373–376; Fisse and Braithwaite (n 39) 29–30. How this translates to active intentionality required for many offences and doctrines has been a major hurdle to its implementation, discussed immediately below.

<sup>97</sup> Fisse (n 47) 1141, 1202.

<sup>98</sup> CLAC Report (n 92) ch 1, 105.

<sup>99</sup> See further Caron Beaton-Wells and Brent Fisse, *Australian Cartel Regulation* (Cambridge University Press, 2011) 232; John HC Colvin and James Argent, 'Corporate and Personal Liability for "Culture" in Corporations?' (2016) 34(1) *Companies and Securities Law Journal* 30.

committed by some natural person before that wrongdoing may be ascribed to the corporation, through the corporate culture provisions. There has also been uncertainty over the 'states of mind' that can be captured by the provisions: they do not expressly refer to 'dishonesty', for example, and one judge has suggested that the use of the indefinite article in the definition of 'corporate culture' requires identification of a single 'policy, attitude...'.<sup>100</sup> The real issue here may be that the concept of a delinquent 'corporate culture' speaks to general culpability (on Fisse's analysis, corporate negligence or a failure to take reasonable corporate precautions),<sup>101</sup> rather than to specific states of mind. How does a delinquent corporate culture relate to knowledge, intention or a predatory mindset? Thus, Skupski has argued that the concept fails to clarify the appropriate threshold beyond which it may be said that the variables that reveal a corporate culture actually encourage specific criminal violations, nor how this threshold correlates with the specific mens rea in issue. He concludes that it is 'merely a smell test'.<sup>102</sup>

Another serious challenge is the significant uncertainty over what 'culture' entails<sup>103</sup> and, hence, how to go about proving it.<sup>104</sup> These uncertainties are particularly troublesome given that the onus of establishing a culpable corporate culture rests with the prosecution. Relevant evidence may be objective and relatively easy to find:<sup>105</sup> corporate policy, for example, may be found in documents, including minutes, memoranda, training manuals, policy documents and so on. But, of course, official policy may be a world away from the reality of what occurs on the ground, in the day to day working of the corporation. How does a prosecutor get to the evidence of the reality of the inner workings of the corporation?<sup>106</sup> The provision, after all, directs attention to

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<sup>100</sup> Transcript of Proceedings, *R v Potter & Mures Fishing Pty Ltd* (Supreme Court of Tasmania, Blow CJ, 14 September 2015) 464, 465.

<sup>101</sup> Above n 96.

<sup>102</sup> George R Skupski, 'The Senior Management Mens Rea: Another Stab at a Workable Integration of Organizational Culpability into Corporate Criminal Liability' (2011) 62 *Case Western Reserve Law Review* 267, 304; see also William S Laufer, *Corporate Bodies and Guilty Minds* (The University of Chicago Press, 2006) 59.

<sup>103</sup> Colvin and Argent (n 99) 33.

<sup>104</sup> Vicky Comino, "'Corporate Culture' is the 'New Black' – Its Possibilities and Limits as a Regulatory Mechanism for Corporations and Financial Institutions?" (2020) 44(1) *University of New South Wales Law Journal* 295.

<sup>105</sup> Comino, for example, emphasises this workable aspect of the concept: *ibid*.

<sup>106</sup> This is particularly challenging where discovery processes do not exist, the prosecution being left to unearth relevant evidence through search warrants.

culture 'within the body corporate' and whether the 'employee, agent or officer of the body corporate who committed the offence believed on reasonable grounds, or entertained a reasonable expectation, that a high managerial agent of the body corporate would have authorised or permitted the commission of the offence'. If, as Commissioner Hayne, suggested, corporate culture is about 'what people do when no one is watching',<sup>107</sup> how can that be shown? The danger is that the enquiry might require subjective evidence from a range of individuals as to their understanding of the corporate ethos.<sup>108</sup> Some commentators, including Fisse, have suggested that this may require expert sociological evidence.<sup>109</sup> It has even been suggested that the model may be 'unworkable' as a matter of practice.<sup>110</sup> Given that Commonwealth prosecutors are 'model litigants' who must only proceed when there is clear foundation to do so, it is unsurprising that the corporate culture provisions have failed to have the degree of regulatory impact that they appeared to promise.

Notwithstanding these difficulties, corporate culture has become a powerful idea in the regulation of corporations in Australia, both within the criminal and civil spheres. For example, courts commonly take corporate culture into account when fixing civil pecuniary penalties for misconduct, looking for evidence of training and compliance programs as signs of the existence of a culture of compliance and, conversely, their absence as an indicator of corporate culpability.<sup>111</sup> Commentators<sup>112</sup> have argued that it is possible to identify objective cultural indicators, such as remuneration, training and compliance practices, the degree of divergence between formal policies and day-to-day practices, the presence of audits, the nature and application of corrective mechanisms and, one might add, the presence of whistleblower protections and

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<sup>107</sup> FSRC Final Report (n 54) 334, citing Group of Thirty, *Banking Conduct and Culture: A Call for Sustained and Comprehensive Reform*, (Group of Thirty, 2015) 17.

<sup>108</sup> Jonathan Clough and Carmel Mulhern, *The Prosecution of Corporations* (Oxford University Press, 2002) 142; see also Dixon (n 92) 15.

<sup>109</sup> Beaton-Wells and Fisse (n 99) 232, reiterated in Brent Fisse, 'Penal Designs and Corporate Conduct: Test Results from Fault and Sanctions in Australian Cartel Law' (2019) 40 *Adelaide Law Review* 285, 290.

<sup>110</sup> Ibid, favouring a combined 'failure to prevent' and 'reactive corporate fault' model. For very helpful discussions of the difficulties, see Dixon (n 92).

<sup>111</sup> Paterson and Bant (n 12). Notably, this does not demand the sort of particularised findings of state of mind required for most doctrines and provisions.

<sup>112</sup> See in particular the work of Clough and Mulhern (n 108), Bucy (n 93) and Comino (n 104). See also *Final Report* (n 15), [6.50]

compensatory schemes.<sup>113</sup> And again, the idea of corporate culture speaks directly to the concept of organisational fault and responsibility, which is very important when it is the corporation itself which is the wrongdoer and which the law is trying to deter. The concept has arguably captured an important understanding about the way in which corporations work that is closer to the actuality of their practices than the anthropomorphised 'corporate mind'. It now finds expression throughout commercial law rules and practices as a key means by which corporations can and should be judged.<sup>114</sup> The question remains, though, how its limitations, identified above, can be overcome: most particularly, how can the concept of 'corporate culture' be operationalised?

### C Failure to Prevent Offences

Another model of corporate criminal responsibility, which has emerged in response to serious and transnational wrongdoing, such as bribery, is the 'failure to prevent' model of liability.<sup>115</sup> In the UK, the *Bribery Act 2010* (UK) introduced the corporate offence of failure to prevent bribery and this has now been copied both within the UK for tax evasion offences<sup>116</sup> and in other jurisdictions, such as Australia.<sup>117</sup> It requires that a natural person be identified, who is 'associated' with the company, has committed the offence and then makes the corporation responsible for that offence. A process-driven defence is available: provided that the company has 'adequate'<sup>118</sup> or 'reasonable'<sup>119</sup> procedures in place to prevent the offence from taking place (such as risk assessment processes, due diligence training, monitoring and review), the company is protected, even if an employee or agent does engage in that misconduct.

It appears, therefore, that this model combines an expansive vicarious liability framework with placing the onus on the corporation to show that it lacked

<sup>113</sup> See discussion in *Final Report* (n 15) ch 11.

<sup>114</sup> Justice Robert French, 'The Culture of Compliance - a Judicial Perspective' (FCA) [2003] *Federal Judicial Scholarship* 16: an idea whose 'time had come'. For evidence of its permeation internationally, see Jennifer G Hill 'Legal Personhood and Liability for Flawed Corporate Cultures' (Research Paper No 19/03, Faculty of Law, The University of Sydney, February 2019) <[https://ecgi.global/sites/default/files/working\\_papers/documents/finalhill3.pdf](https://ecgi.global/sites/default/files/working_papers/documents/finalhill3.pdf)>.

<sup>115</sup> For an excellent discussion, see Liz Campbell, 'Corporate Liability and the Criminalisation of Failure' (2018) *Law and Financial Markets Review* 57.

<sup>116</sup> *Criminal Finances Act 2017* (UK).

<sup>117</sup> See, eg, *Crimes Legislation Amendment (Combatting Corporate Crime) Bill 2019* (Cth) s 8.

<sup>118</sup> *Bribery Act 2010* (UK).

<sup>119</sup> *Criminal Finances Act* (n 111).

culpability in terms of its processes. The model is deliberately instrumental, designed to ‘influence behaviour and encourage bribery prevention as part of corporate good governance’.<sup>120</sup> Wells has proposed that this model should be extended to all economic crimes.<sup>121</sup> Although this model may seem a world away from the corporate culture concept, as Campbell observes, ‘indirect omissions liability and the associated defences aim to ensure that corporate management fosters a culture of compliance and communicates commitment to the prevention of bribery and tax evasion throughout the organisation’.<sup>122</sup>

This model avoids some of the aspects of ‘unworkability’ that have been levelled against the corporate culture provisions, while still enabling identification and deterrence of organisational blameworthiness.<sup>123</sup> However, it is a very distinctive, corporate-specific strategy. We have seen that issues of corporate state of mind are endemic to commercial regulation. It would be possible to introduce specific failure to prevent reforms applicable to key commercial doctrines, or introduce a generalised principle of corporate culpability that applies to specific states of mind, relevant to both statutory and general law doctrines.<sup>124</sup> But implementing these options would require a level of coordinated reform and agreement that, as will see immediately below, have been in short supply. They could also be anticipated to attract serious rule of law concerns.<sup>125</sup> Is a less seismic option available, which can adapt and respond to existing doctrines and principles?

#### *D ALRC Recommendations for Reform of Corporate Criminal Responsibility*

In its Final Report, the ALRC has made a number of recommendations for reform that would, if adopted, assist in the application of the corporate culture

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<sup>120</sup> Ministry of Justice and Department for Business, Innovation & Skills, *Insight into awareness and impact of the Bribery Act 2010 Among small and medium sized enterprises (SMEs)* (2015) 3: [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/440661/insight-into-awareness-and-impact-of-the-bribery-act-2010.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/440661/insight-into-awareness-and-impact-of-the-bribery-act-2010.pdf)

<sup>121</sup> Celia Wells, ‘Corporate Failure to Prevent Economic Crime – A proposal’ [2017] *Criminal Law Review* 426, 427.

<sup>122</sup> Campbell (n 115) 61.

<sup>123</sup> Fisse (n 109); *Discussion Paper* (n 16) discussed immediately below.

<sup>124</sup> My thanks to one of the anonymous reviewers for this observation.

<sup>125</sup> A common complaint in response to the ALRC’s original discussion paper proposals: see immediately below at text to n 131.

provisions.<sup>126</sup> These included changing the reference to ‘offence’ to ‘the physical element’, so that it clearly is unnecessary to find a single human offender whose wrongdoing can be attributed to the corporation.<sup>127</sup> The recommendations also propose amending the definition of corporate culture to include the plural, as well as the singular and, for the avoidance of any possible confusion, to replace the idea of ‘due diligence’ with ‘reasonable precautions’.<sup>128</sup> The Final Report further recommends that s 12.3(2)(d) be repealed on the ground that ‘it is inappropriate to require proof beyond reasonable doubt of the non-existence of a particular culture in order to attribute liability to a corporation’.<sup>129</sup>

However, while valuable, these recommendations arguably do not surmount the main hurdles to effective deployment of the corporate culture concept. These are the combination of the onus lying on the prosecutor or regulator, the potentially subjective and uncertain nature of the evidence required to prove the culpable corporate culture and, last but not least, how the concept of a culpable corporate culture relates to the sort of specific mental states that underpin many forms of claim for serious misconduct. On this last point, ALRC considered that ‘[a]lthough there may be an argument that s 12.3(2) erases the distinction between intention, knowledge, and recklessness, the ALRC considers that the provision retains relevant gradients of fault. That is, the prosecution must prove that the authorisation or permission amounted to intention, knowledge or recklessness.<sup>130</sup> However, its examples of how that is achieved arguably revert back to a human-dependent model: ‘Intention may be proved through the approval of the board of directors, and recklessness by reference to the state of mind of a high managerial agent.<sup>131</sup>

In earlier discussions papers,<sup>132</sup> the ALRC had gone further, contemplating combining a broad organic attribution model, through which the state of mind

<sup>126</sup> *Final Report* (n 15) recommendation 7 option 1. The Report recommends that government elect between two options, the other being a modified TPA Model of liability, to which a defence of reasonable precautions would apply. As it notes, the latter option (while familiar and well-tested) does not address the diffused responsibility problem: at [6.126].

<sup>127</sup> *Ibid* [6.56]–[6.60].

<sup>128</sup> There is no significant difference in substance between the two phrases: see the explanation for the switch at [6.168]–[6.168].

<sup>129</sup> *Ibid* [6.69].

<sup>130</sup> *Ibid* [6.73].

<sup>131</sup> *Ibid* [6.75].

<sup>132</sup> See, eg, ‘Corporate Attribution – Principled Simplicity’, Australian Law Reform Commission (Web Page, 27 November 2019) <[www.alrc.gov.au/news/corporate-attribution-principled-simplicity](http://www.alrc.gov.au/news/corporate-attribution-principled-simplicity)>; *Discussion Paper* (n 16) proposals 8 and 9, described and discussed in chapter 6.

of 'associates' of the company were treated as that of the company, combined with a due diligence defence. This drew from the English 'failure to prevent' model by adopting the broader concept of 'associates,' albeit as part of an attribution rather than vicarious liability framework, coupled with a due diligence defence. The combination would operate in many cases to shift the burden of proving a blameworthy organisational state of mind to the defendant company which, as we have seen, is generally in the best position to bring evidence of its internal policies, systems and processes. Additionally, the early recommendations contemplated that corporate fault could continue to be established by prosecutors proving that a corporation had 'authorised or permitted' misconduct through a culpable corporate culture. The combination of methods sought to capture the most effective elements of existing attribution and corporate culture models, while including safeguards to protect corporations with appropriate compliance processes and conscientious corporate cultures from unmerited liability. Notwithstanding, these suggestions were criticised<sup>133</sup> as rash and unprincipled proposals that, if adopted, would convict innocent corporations for the acts of 'rogue employees' and impermissibly alter the basis of criminal liability.<sup>134</sup>

#### IV A MODEL OF SYSTEMS INTENTIONALITY

##### A *Guiding Principles for Any Reform*

Faced with the current, uncertain and arguably unsatisfactory state of affairs, this Part proposes a new model of 'systems intentionality' that would sit alongside and support other general law and statutory attribution and liability

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<sup>133</sup> For the tenor of some submissions, see 'Review into Australia's Corporate Criminal Responsibility Regime/Submissions', *Australian Law Reform Commission* (Web Page, 29 August 2019) <<https://www.alrc.gov.au/inquiry/corporate-crime/submissions/>>; TA Game and Justice David Hammerschlag, Joint Comment on ALRC Discussion paper 87 on Corporate Criminal Responsibility of November 2019 (20 December 2019) <<https://www.alrc.gov.au/wp-content/uploads/2019/08/17-Public-T-Game-and-Justice-D-Hammerschlag.pdf>>. For how this was viewed in some media, see Michael Pelly, 'Judges Take Aim at Corporate Crime Reform Plan', *Australian Financial Review* (online, 10 February 2020) <<https://www.afr.com/companies/professional-services/judges-take-aim-at-corporate-crime-reform-plan-20200207-p53yvc>>; on the 'back-down', see Michael Pelly, 'Law reform Backdown on Corporate Crime', *Australian Financial Review* (online, 9 March 2020) <<https://www.afr.com/companies/financial-services/law-reform-backdown-on-corporate-crime-20200308-p547wb>>.

<sup>134</sup> Even senior judges made powerful submissions along these lines: see Game and Hammerschlag (n 133).

approaches.<sup>135</sup> This model seeks to build on and ‘operationalise’ some of the valuable insights that underpin the concept of corporate culture, in a way that meets doctrinal demands for specific states of mind. It inherently protects compliant corporations against the spectre of liability arising from rogue employees and, moreover, requires no major overhaul of existing laws that regulate misconduct. It therefore merits further consideration in the current reform debates.

The starting premise for this model is the truism that corporations do not possess natural or innate states of mind. Second, taking that reality seriously enables us to appreciate that corporate liability should not necessarily be human liability transferred, but rather liability developed for the reality of the corporation. Third, however, is that entirely jettisoning fictional concepts of corporate state of mind would be very difficult and highly disruptive. Such ideas underpin or inform a huge range of areas across corporate and commercial law. Fourthly, and relatedly, it is no doubt desirable that the law should develop in a rational and coherent manner. It follows that, any proposed reforms to introduce distinctions in treatment between corporate and natural persons must be justified and, moreover, fit with (or at least not undermine) their broader statutory and general law principles and contexts.

Finally, a key challenge is to map and distinguish the different kinds and contents of rules that may be potentially engaged by this enquiry. This article has already noted the various liability rules, defences and remedial contexts. But even within these, the various ‘state of mind’ enquiries vary widely. Dishonesty is a different concept than being ‘predatory’, knowledge is different to intention,<sup>136</sup> mistake is distinguishable from doubt and recklessness.<sup>137</sup> Within the confines of this paper, it is only possible to note the nature of this challenge and to identify within the following discussion, the sorts of circumstances in which they arise.

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<sup>135</sup> See Bant and Paterson (n 13).

<sup>136</sup> The relationship between knowledge, intention and foresight is notoriously close and difficult: see eg the expansive and ‘controversial’ definition in s 5.2(3) of the *Criminal Code* (n 10) which provides: “[a] person has intention with respect to a result if he or she means to bring it about or is aware that it will occur in the ordinary course of events”, examined in SZTAL (n 10). See in particular the discussion of ‘oblique intention’ by Edelman J at 381–2 [60]–[62], 392–8 [93]–[103], concluding that foresight of consequence is only evidence from which intention may be inferred. On the spectrum of mental states relevant to ‘knowledge’, see also *Group Seven Ltd v Notable Services LLP* [2019] EWCA Civ 614, [2020] Ch 129 [33]–[61] (the Court) (‘Group Seven’).

<sup>137</sup> Here, unjust enrichment analysis offers insights: see, eg, the discussion in James Edelman and Elise Bant, *Unjust Enrichment* (Hart Publishing, 2016) 174–9.

An initial, important step in that direction is to separate out normative standards and state of mind enquiries, to which we now turn.

### B Separating Out Standards and States of Mind

Given the difficulties around corporate attribution, it is important to appreciate when the necessary focus of an enquiry is on the objective quality of the conduct of corporations, as opposed to its state of mind. This may be a particularly cogent strategy for regulating corporations where the law's focus is on contravention of some community norm or standard of behaviour, like misleading conduct or, potentially, dishonesty or unconscionable conduct. On a wholly objective approach, it might be possible to avoid the state of mind enquiry, at least at the liability stage.<sup>138</sup> However, this is not yet the position in the case of dishonesty, on the state of current authorities.<sup>139</sup>

We saw earlier that the *Ghosh* test of dishonesty was incorporated into statutory prohibitions such as s 1041G(2) of the *Corporations Act*.<sup>140</sup> According to its dual approach, the acts in question must be dishonest according to current standards of ordinary decent people and the accused must have realised that they were dishonest by those standards. The latter subjective mental component has been widely criticised, not least for unhelpfully promoting (if not endorsing)<sup>141</sup> a 'Robin Hood' mentality.<sup>142</sup> It was rejected by the High Court of Australia *Peters v R*,<sup>143</sup> a position that it has repeatedly affirmed.<sup>144</sup> The test has also now been authoritatively abandoned in England as a wrong turn in the law.<sup>145</sup>

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<sup>138</sup> Arguably state of mind enquiries still become relevant at remedial and penalty phases, see above at text to n 24.

<sup>139</sup> For unconscionability, see Bant and Paterson (n 13).

<sup>140</sup> *Ghosh* (n 72).

<sup>141</sup> *Ibid* 1057–64.

<sup>142</sup> See, eg, Law Commission for England and Wales, *Legislating the Criminal Code: Fraud and Deception* (Consultation Paper No 155, April 1999) [5.7]–[5.8]; *R v Theroux* [1993] 2 SCR 5, [18]–[21].

<sup>143</sup> *Peters v R* (1998) 192 CLR 493.

<sup>144</sup> *Spies v R* (2000) 201 CLR 603, 630–1; *McCann v Switzerland Insurance* (2000) 203 CLR 579, 596, 608, 617–8; *Macleod v The Queen* (2003) 214 CLR 230, 241–3 [35]–[39], 245 [46], 256 [99]–[101], 264–5 [130]; *Polyaire Pty Ltd v K-Aire Pty Ltd* (2005) 221 CLR 287, 295–6; *Farah Constructions Pty Ltd v Say-Dee Pty Ltd* (2007) 230 CLR 89, 126 [73] ('Farah'); *Marcolongo v Chen* (2011) 242 CLR 546, 559 [33]. This has been welcomed by commentators: see eg Murray Gleeson, 'Australia's Contribution to the Common Law' (2008) 82 *Australian Law Journal* 247, 249; Lusty (n 74).

<sup>145</sup> *Ivey* (n 74) 416–7 [74]–[75]; *Barton v R* [2020] EWCA Crim 575, [1] ('Barton'). See also *Group Seven* (n 136) [52]–[58] (the Court).

Consistently, courts applying civil law doctrines in which dishonesty forms a component have followed a similar trajectory away from the *Ghosh* dual test.<sup>146</sup> As the New South Wales Court of Appeal stated in *Hasler v Singtel Optus Pty Ltd*: 'Dishonesty amounts to a transgression of ordinary standards of honest behaviour. It is not necessary to say anything else by way of elaboration, save to confirm that it is not necessary to demonstrate that the person thought about what those standards were.'<sup>147</sup> Likewise in *Ancient Order of Foresters in Victoria Friendly Society Limited v Lifeplan Australia Friendly Society Limited*, Kiefel CJ, Keane and Edelman JJ stated (in the context of an equitable claim of knowing assistance in a breach of fiduciary duty):

[P]articipation in a dishonest and fraudulent breach of fiduciary duty includes knowingly assisting the fiduciary in the execution of a "dishonest and fraudulent design" on the part of the fiduciary to engage in the conduct that is in breach of fiduciary duty. The requisite element of dishonesty and fraud on the part of the fiduciary is met where the conduct which constitutes the breach transgresses ordinary standards of honest behaviour [citing *Hasler*.]<sup>148</sup>

This shift to a more objective standpoint is reflected in the recent amendment to the definition of 'dishonest' in s 9 of the *Corporations Act*, by which 'dishonest means dishonest according to the standards of ordinary people'.

While this trend might suggest that dishonesty is a wholly objective standard of conduct, that conclusion overstates the position. On the current state of authorities, it remains necessary to assess objectively the quality of the defendant's conduct *in light of the defendant's* actual intention and knowledge.<sup>149</sup> For example, the conduct in question must have been intentional<sup>150</sup> rather than produced as a result of some psychotic episode or while sleepwalking. As the High Court explained in *Peters*, 'ordinary, honest persons determine whether a

<sup>146</sup> For a stark example in the context of the English doctrine of 'dishonest assistance', see *Royal Brunei Airlines v Tan* [1995] 2 AC 378, 389 (Lord Nicholls), re-interpreted in *Twinsectra v Yardley* [2002] 2 AC 164, [35]–[36]; rectified in *Barlow Clowes v Eurotrust* [2006] 1 WLR 1476, [10] and then endorsed in *Ivey* (n 74) 416–7 [74]–[75], and reiterated in *Group Seven* (n 136) [58]. In Australia, see *Farah* (n 144) 126 [73] (the Court).

<sup>147</sup> (2014) 87 NSWLR 609, 636 [124] (Leeming JA, Barrett and Gleeson JJA concurring).

<sup>148</sup> (2018) 265 CLR 1, 31 [71].

<sup>149</sup> *Ivey* (n 74) 416–7 [74]; *Barton* (n 146) [84], [107]–[108]; *Group Seven* (n 135). This notably contradicts the recent statement in *MLC Nominees* (n 58) [51] that dishonesty 'does not rely on any proof or finding of intent' and is wholly determined by reference to objective circumstances.

<sup>150</sup> A matter of 'general' rather than specific intention: see *He Kaw The v R* (1985) 157 CLR 523, 569–70 (Brennan J).

person's act is dishonest by reference to that person's knowledge or belief as to some fact relevant to the act in question or the intention with which the act was done.<sup>151</sup> This requires us to understand the defendant's state of mind, to which we now turn.

### C Systems Intentionality

We have seen that the Australian corporate culture provisions identify the significance of corporate policies, practices and processes to ascertaining the corporate state of mind. However, they do so in a way that invites consideration of an internal perspective – the subjective understandings of employees, for example, of what their obligations both to the corporation as an employee, and to wider society, entail. Moreover, it is unclear how the concept of a corporate culture bears on specific forms of state of mind, such as knowledge or intention, without reverting to a derivative model of liability.

Here, it is possible to develop a more rigorous and objective framework that sees the corporate state of mind manifested in its systems, policies and patterns of behaviour.<sup>152</sup> Peter A French, in his seminal study on Collective and Corporate Responsibility,<sup>153</sup> examines at length the interaction between concepts of intentionality and corporations. He explains that 'saying 'someone did y intentionally' is to describe an event as the upshot of that person's having had a reason for doing y which was the cause of his or her doing it.'<sup>154</sup> When it comes to corporations, these reasons for decisions are found not just with the directors, but in the broader 'Corporate Internal Decision' structure. This structure includes (1) the corporate lines of responsibility (the corporate 'flowchart') and (2) corporate decision 'recognition rules' (usually found in corporate procedural rules and policies). Individual understandings of natural persons must be understood within this framework: 'When operative and properly activated, the CID structure accomplishes a subordination and synthesis of the intentions and acts of various biological persons into a corporate decision.' As he concludes:

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<sup>151</sup> Peters (n 143) 503-503 (Toohey and Gummow JJ).

<sup>152</sup> Gobert (n 38) 408. For other seminal studies, on which this models draws, see Celia Wells, *Corporations and Criminal Responsibility*, 2<sup>nd</sup> edn (Oxford University Press, 2001), in particular chapter 8 and Christian List and Philip Pettit, *Group Agency: The Possibility, Design and Status of Corporate Agents* (Oxford University Press, 2011) Chapter 7.

<sup>153</sup> French (n 88).

<sup>154</sup> Ibid 40.

when the corporate act is consistent with an instantiation or an implementation of established corporate policy, then it is proper to describe it as having been done for corporate reasons, as having been caused by a corporate desire coupled with a corporate belief and so, in other words, as corporate intentional.<sup>155</sup>

Consistently with this approach, it may be argued that a corporation's state of mind is manifested,<sup>156</sup> for example, where it adopts a system of conduct or pattern of behaviour that results in a contravention, or is apt to (calculated to, designed to, of a nature to) contravene, the conduct element of some civil law prohibition. Here, the purpose or design of a system is not dependent on foreseeability viewed from the perspective of human participants in the process, but rather involves an assessment of its inherent features. Laufer has suggested a similar model but with a more challenging, two-stage process.<sup>157</sup> On his model, the first stage similarly asks about the inherent tendency of a corporation's policies and practices. But it then asks whether it would be open to conclude that, given that evidence, a reasonable corporation 'of like size, complexity, structure' purposely engaged in that illegal conduct. This second step seems difficult and unnecessary, not least because of its circularity.<sup>158</sup> Further, on the preferred approach, the knowledge necessary for the operation of, or implicit in, the adopted process/system may safely be assumed, leaving the corporation to bring evidence of mistake or ignorance. Likewise, with recklessness, it is possible and appropriate to assess the objective risks implicit in a process (for example, failures to put in place obvious safeguards) to determine whether the level of corporate culpability extends beyond corporate negligence to embrace a reckless mental state.<sup>159</sup>

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<sup>155</sup> *Ibid* 44.

<sup>156</sup> Sheley plausibly criticises arguments that corporate intention may be *inferred* from these factors for assuming that corporate and human intention can usefully be analogised: see Erin L Sheley, 'Tort Answers to the Problem of Corporate Criminal Mens Rea' (2019) 97 *North Carolina Law Review* 773, 793.

<sup>157</sup> Laufer (n 102). See also William S Laufer and Alan Strudler, 'Corporate Intentionality, Desert and Variants of Vicarious Liability' (2000) 37 *American Criminal Law Review* 1285, 1309–10.

<sup>158</sup> See also Mihailis Diamantis, 'Corporate Criminal Minds' (2016) 91 *Notre Dame Law Review* 2049, 2075–6.

<sup>159</sup> This article cannot hope to map the spectrum of mental states, but recklessness is generally treated as more culpable than mere negligence, although not equivalent to intention: see SZTAL (n 10). On recklessness manifested in systems, see *Australian Competition and Consumer Commission v Cornerstone Investment Aust Pty Ltd (in liq) (No 4)* [2018] FCA 1408 ('Cornerstone'), analysed in Bant and Paterson (n 13).

On this approach, we look to what a corporation routinely and systematically does, and what its systems are objectively apt to produce, to ascertain what it knows, intends or is reckless towards.<sup>160</sup>

This analysis is supported by Mihailis E Diamantis' novel application of the 'extended mind thesis,' developed by cognitive scientists and philosophers, to explain how corporations may be responsible for acts carried out through AI systems.<sup>161</sup> This thesis explores how humans utilise external systems to facilitate recall and decision-making. Everyday examples are the use of maps, recipes or records. Diamantis argues that, just as the use of these mental extensions does not undermine the fact that the act remains that of the human, so acts carried out through AI systems remain those of the corporation.

Taking this idea further, just as we might say that a human can reasonably be understood to 'know' how, and 'intend to' get to her destination, make the cake, or remember the recorded information, through application of the relevant system, so too corporations must be said to know and intend the systems they generate, or adopt and apply. Indeed, corporations necessarily employ systems to coordinate and manage their human personnel, over time. In some cases (as with automated and algorithmic processes) those humans are entirely replaced by self-executing systems. From the perspective of the 'extended mind' analysis, it seems strongly plausible that corporations manifest their intentionality through the systems they adopt and implement. Moreover, the analysis is applicable to both legal and natural persons,<sup>162</sup> meeting the concern mentioned earlier about equal treatment of the law's subjects. The proposed model of systems intentionality simply makes explicit for corporations what also holds true for humans: when we draw on (internal or external) systems to facilitate our decisions and recall, those systems become an extension of our mental state. Indeed, on one view, corporate systems, policies and processes as instantiated are not a mere extension of the corporate mind but where that corporate mind

<sup>160</sup> Cf estoppel, where the question whether a statement is 'calculated' to induce reliance points to its objective aptitude or nature, eg, *Redgrave v Hurd* (1881) 20 Ch D 1 (Sir Jessel MR), explained in *Seton, Laing & Co v Lafone* (1887) 19 QBD 68, 72, 73 (Lord Esher MR). See also *Freeman v Cooke* (1848) 2 Ex 654, 653; 154 AR 652, 656 (Parke B); *Craine v Colonial Mutual Fire Insurance Co Ltd* (1920) 28 CLR 305, 327. As in estoppel and other cases of 'decision causation', the test of causation would be the 'a factor' test of contribution: E Bant and JM Paterson, 'Statutory Causation in Cases of Misleading Conduct: Lessons from and for the Common Law' (2017) *Torts Law Journal* 1.

<sup>161</sup> Diamantis (n 48). For his approach to attribution more generally, see Diamantis (n 158).

<sup>162</sup> Such as the book-up system in *Australian Securities Investment Commission v Kobelt* [2019] HCA 18, (2019) 368 ALR 1.

naturally and necessarily resides. The systems *manifest* the corporate states of mind.

Finally, although it falls outside the scope of this paper, the model is also supported by the developing jurisprudence concerning statutory unconscionability, in the context of exploitative business models and practices. Building on judicial insights,<sup>163</sup> provisions such as s21 ACL expressly capture unconscionable ‘systems of conduct and patterns of behaviour’.<sup>164</sup> Courts applying these provisions have started to develop clear conceptions of corporate unconscionability in organisational terms consistent with the proposed model.<sup>165</sup> These include detailed consideration of what constitutes a system of conduct and pattern of behaviour, how a system or pattern may be proven, and their connections to intentionality. The decisions suggest, for example, that a system is inherently purposive in nature: an internal method or organised connection of elements operating to produce the conduct. By contrast, a pattern is an externally manifested sequence or repetition of behaviour from which a system may be inferred. Such understandings strongly corroborate the proposed model of systems intentionality. Indeed, it is arguable that the ALRC’s recommendation 8, which proposes the creation of a criminal offence where corporations engage in ‘systems of conduct or patterns of behaviour’ that repeatedly breach the law,<sup>166</sup> is itself consistent with the proposed model. The crucial insight this model offers, however, is that such misconduct is more culpable not merely because it is repeated, but because it manifests or evidences intentionality.

These considerations, taken together, suggest that, far from being a revolutionary concept, the idea of systems intentionality is both a principled one and is already implicit in our law.<sup>167</sup> It remains to make it explicit and work through its detailed operation. A full account cannot be attempted here. But,

<sup>163</sup> *Australian Securities Investments Commission v National Exchange Pty Ltd* [2005] FCAFC 226, (2005) 148 FCR 132 [33] (Tamberlin, Finn and Conti JJ).

<sup>164</sup> The subject of detailed examination in Bant and Paterson (n 13).

<sup>165</sup> Key authorities include *Australian Competition and Consumer Commission v EDirect Pty Ltd* [2012] FCA 1045; *Australian Competition and Consumer Commission v Get Qualified Australia Pty Ltd (in liquidation) (No 2)* [2017] FCA 709; *Cornerstone* (n 159); *Unique International College Pty Ltd v Australian Competition and Consumer Commission* (2018) 362 ALR 66; *Australian Competition and Consumer Commission v Australian Institute of Professional Education Pty Ltd (in liq) (No 3)* [2019] FCA 1982; *Australian Securities and Investments Commission v AGM Markets Pty Ltd (in liquidation) (No 3)* (2020) 275 FCR 57.

<sup>166</sup> *Final Report* (n 15) [7.12].

<sup>167</sup> See also *Kojic* (n 42) 457 [153].

returning to the concept of 'dishonesty' and the fees for no service scenarios discussed earlier, we may start to explore the application of the model of systems intentionality in practice.

#### *D Fees For No Service From the Perspective of Systems Intentionality*

We have seen that dishonesty requires assessment of the objective quality of the defendant's conduct in light of the defendant's actual intention and knowledge. Turning to the state of mind question first, in the context of corporate liability, the analysis suggests that this enquiry must take place against the reality of corporate systems, policies and practices. Where a corporation's conduct is carried out in accordance with its instantiated (rather than purely formal or authorised) systems, policies or practices,<sup>168</sup> it may be understood as corporate intentional and based on the knowledge required for that system, policy or practice to be adopted and function. The quality of the corporation's behaviour, assessed against this manifested state of mind, must then be assessed objectively, as explained above.

A defendant may argue that there was a relevant 'systems error' or mistake, so that the systems intentionality was vitiated or impaired, in such a way that should operate as an excuse or mitigating factor. How this may be done must be left for another day. However, on the current analysis, mistake cannot be established simply by identifying the system or practice that resulted in the impugned outcome, as was attempted in the FSRC with executives blaming 'systems errors'. Rather, adopted systems demonstrate intentionality. The 'systems error' argument has, through this analysis, been turned on its head. Nor will it be sufficient to demonstrate that, for example, directors were oblivious to or 'ignorant of' the inherent tendency of the system. As is well-established in the law of unjust enrichment in Australia, in order for ignorance to give rise to a mistake, it must have informed a positive but incorrect assumption on which a decision was based. A mere failure to advert to a matter (or 'mere ignorance') does not count.<sup>169</sup>

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<sup>168</sup> The question of how systems are proven is addressed briefly in Jeannie Marie Paterson and Elise Bant, 'Should Australia Introduce a Prohibition on Unfair Trading? Responding to Exploitative Business Systems in Person and Online' (2020) *Journal of Consumer Policy* <<https://doi.org/10.1007/s10603-020-09467-9>>.

<sup>169</sup> Edelman and Bant (n 137) 173-174.

Focussing on the inherent features of the payment systems, we saw that, in one scenario, deductions were automatically made for the provision of services pursuant to a system in which no advisor had been allocated to the client. In another, FSPs charged service fees to clients notwithstanding having received notice of their death. In both cases, there was a failure of the records of the status of clients to be calibrated against the payments deducted from their accounts. In other words, the record systems and payment systems which should have been closely linked were operating in isolation. This cannot be dismissed as mere error or the result of an unfortunate oversight. The systems were designed to remain in place over extended periods and in respect of human clients whose circumstances would inevitably change (a feature implicit in the very idea of intermittent, renewed financial advice). Here, one starts from the position that the systems as instantiated were intended and were predicated on the knowledge necessary for the system to function (eg details of client accounts, the necessity for continuing authorisation for deductions, the basis or reasons for the deductions and so on). The question then becomes whether (absent countervailing evidence by the defendant on these issues, for example going to mistake) the conduct was dishonest assessed against objective community standards, viewed in light of that assumed intentionality and knowledge.

Here, it is plausible that the requisite standard of dishonesty is revealed in the period of time over which the conduct extended, which may indicate a reckless disregard for the ongoing, lawful basis for the deductions and a blind eye being turned to the need for regular review of the payment system itself. This assessment is supported by French's insights (and consistent with Fisse's concept of reactive corporate fault)<sup>170</sup> of the need for corporate operating systems or processes, whether manual or automated, to be informed by a 'principle of responsive adjustment': the capacity to review and adjust the processes to ensure they are performing in the way that is required and expected.<sup>171</sup> French regards this principle as an important component or foundation for the corporation as a moral person. 'Simply, to be a moral person is to be both an intentional actor and an entity with the capacity or ability to intentionally modify its behavioural patterns, habits or modus operandi' to respond to revealed harmful behaviours or fault. We may accept that where a corporation has the capacity to review and

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<sup>170</sup> See above nn 95 and 96.

<sup>171</sup> French (n 88) 164–9.

correct processes that cause harm, repeated contraventions of the law through those processes on this view become intentional in character. However, it is also arguable that, where a process is introduced that is (objectively) intended to operate over a long period of time, and which necessarily entails repeated acts (here, deductions from client accounts) that require ongoing justification, yet omits any appropriate adjustment mechanisms, the corporation is directly responsible for that operation, and may be open to being adjudged dishonest in the failure to ensure appropriate mechanisms or adjustments. To adopt and maintain a 'set and forget' system of this nature may be regarded as objectively dishonest, particularly where the defendant is a sophisticated commercial entity with considerable experience (indeed, expertise) in this form of activity.

Finally, it should be noted that, where it applies in respect of misconduct that occurred prior to the definitional reforms discussed earlier, the second limb of the former statutory test for dishonesty under s 1401G continues to present a significant hurdle to regulator enforcement. That hurdle will require assertive judicial treatment, of the kind advocated by Commissioner Hayne, in order to be overcome. However, the fact that corporate pleas of accident, want of knowledge and error can readily be challenged through the proposed model provides additional principled support for a robust approach.

## V CONCLUSION

This article outlines a fresh approach to the elusive concept of the culpable corporate mind. It takes first steps to articulating a coherent doctrinal conception of corporate intention, building on the work of law reformers and theorists working in the field. It illustrates the way in which the model might apply in the context of misconduct involving 'dishonesty', both as that concept is defined under the *Ghosh* test and related statutory provisions, and on a reformed basis. In so doing, it suggests how required elements of knowledge and recklessness might also be demonstrated.

Throughout, the paper focuses on the challenges posed by the reality of complex corporate systems and processes and shows how that reality may yet provide a way forward for efficient and just regulation. In concluding, it is worth reiterating that, as the operational and decision-making systems within corporations become increasingly reliant on automation, there will be an ever more pressing need to supplement our anthropomorphic and human-focussed

attribution rules with doctrines that are ‘fit for purpose’ in the digital age. From that perspective, as well as due appraisal of current need, the proposed model merits further investigation as part of ongoing reform debates.