Directors and Officers Liability for Corporate Fault - Update

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Introduction

A concern over recent years has been the overwhelming number of laws that hold directors and officers personally responsible for the wrongdoing of a company through the operation of derivative liability provisions.

Guided by the Council of Australian Government’s (COAG) Principles, the Commonwealth government passed the Personal Liability for Corporate Fault Reform Act 2012 (Commonwealth Act) which commenced on 11 December 2012. Following suit, the NSW government passed the Miscellaneous Acts Amendment (Directors’ Liability) Act 2012 (NSW Act) which commenced on 11 January 2013.

Broadly speaking, the Commonwealth and NSW Acts reduce the complexity and number of director and officer derivative liability provisions for corporate fault. Previously, over 700 laws contained derivative liability provisions and applied inconsistent standards of personal responsibility, many reversing the evidentiary onus of proof requiring directors and officers to demonstrate that reasonable steps had been taken to avoid the commission of the offence. The new legislation is intended to clarify the compliance regime to which directors and officers are subject.

COAG Principles

In December 2009, COAG agreed on a set of principles proposed by the Ministerial Council for Corporations for national adoption as the basis on which personal liability for corporate fault should be imposed.

The COAG Principles do not concern direct and accessorial liability provisions and focus only on provisions that hold directors and other corporate officers liable because an offence has been committed by the corporation.

The principles are as follows:

1. Where a corporation contravenes a statutory requirement, the corporation should be held liable in the first instance.
2. Directors should not be liable for corporate fault as a matter of course or by blanket imposition of liability across an entire Act.
3. A “designated officer” approach to liability is not suitable for general application.
4. The imposition of personal criminal liability on a director for the misconduct of a corporation should be confined to situations where:
   a) there are compelling public policy reasons for doing so (for example, in terms of the potential for significant public harm that might be caused by the particular corporate offending);
   b) liability of the corporation is not likely on its own to sufficiently promote compliance; and
   c) it is reasonable in all the circumstances for the director to be liable having regard to factors including where:
      i) the obligation on the corporation, and in turn the director, is clear;
      ii) the director has the capacity to influence the conduct of the corporation in relation to the offending; and
      iii) there are steps that a reasonable director might take to ensure a corporation's compliance with the legislative obligation.
5. Where principle 4 is satisfied and directors’ liability is appropriate, directors could be liable where they:
   a) have encouraged or assisted in the commission of the offence; or
   b) have been negligent or reckless in relation to the corporation's offending.
6. In addition, in some circumstances, it may be appropriate to put directors to proof that they have taken reasonable steps to prevent the corporation's offending if they are not to be personally liable.

The purpose of the principles is to ensure a measure of consistency across laws that impose derivative liability.

COAG categorised derivative liability offences as either Type 1, Type 2 or Type 3 offences. Depending on the offence, either the prosecution or the defence has to establish guilt or innocence respectively, and according to different standards of proof. Of the offences, Type 3 offences place the greatest pressure on defendant directors and officers. It is hoped by COAG that many type 3 provisions would be amended to a Type 2 or Type 1 provision, or removed altogether. Where Type 3 provisions remain, they have to be justified.

To highlight the effect of the differences in the types of offences, a summary of the onus and standard of proof for each offence is provided in the below table.
### Implementation across Australia

The Commonwealth Act amends 15 statutes, including the *Corporations Act 2001* and *Insurance Contracts Act 1984*.

The NSW Act amends over 40 statutes, reducing the number of offences to which derivative liability provisions apply from over 1000 to about 150.

Other states and territories have now followed with:

- the Australian Capital Territory *Directors Liability Legislation Amendment Act 2013*, commenced on 21 February 2013, amending 13 statutes containing derivative liability provisions;
- the Victorian *Statute Law Amendment (Directors’ Liability) Act 2013*, commenced on 14 March 2013, amending 18 statutes containing derivative liability provisions;
- the South Australian *Statutes Amendment (Directors’ Liability) Bill 2012* passed through both houses of Parliament and soon expected to receive assent which, in its current form, seeks to amend 50 statutes containing derivative liability provisions;
- the Tasmanian *Directors’ Liability (Miscellaneous Amendments) Bill 2012* and the Queensland *Directors’ Liability Reform Amendment Bill 2012* which have not progressed further since they were introduced into the Tasmanian House of Assembly on 20 November 2012 and the Queensland Legislative Assembly on 28 November 2012, respectively. In its current form, the Tasmanian Bill seeks to amend 36 statutes containing derivative liability provisions while the Queensland Bill seeks to amend 80 statutes containing derivative liability provisions.
- in relation to the Western Australian and Northern Territory, no Bill has yet been introduced into the respective Houses of Parliament.

### Implications

It remains to be seen whether the refinement of the existing laws through the incorporation of the COAG principles ultimately streamlines directors’ and officers’ personal liability for corporate fault.

It will also be interesting to observe whether the reform will have any practical effect on the number of regulator prosecutions or shareholder class actions initiated against directors and officers.

Directors and officers should become familiar with this legislation and check that appropriate risk management procedures have been implemented to ensure compliance with their obligations.