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The Committee Secretary
Parliamentary Joint Committee on Corporations and Financial Services
Department of the Senate
Parliament House
Canberra ACT 2600

Dear Secretary

Inquiry into Corporate Responsibility: Questions on Notice

We refer to the inquiry into Corporate Responsibility and two questions on notice directed to the Task Force members at the hearing on 23 November 2005.

First Questions

At page CFS 10 of the committee *Hansard*, the Chairman stated and asked:

> "You would be aware, I assume, of the recent decision on the ASIC case against Rich where it was held that the standard of care expected from a chairman be determined by community expectations. How do you see this within the context of the terms of degree of care and diligence expected under section 181 of the Corporations Act and principle 10 of the Stock Exchange's corporate governance principles, which requires directors to 'recognise legal and other obligations to all legitimate stakeholders'? Do you think there is any significance in that particular judgment?"

These questions were taken on notice (CFS 11).

The decision of Austin J in *ASIC v Rich* (2003) FLR 128, [2003] NSWSC 85 concerned a motion by Mr Greaves, the former chairman of One.Tel Ltd, to strike out ASIC's statement of claim as disclosing no reasonable cause of action. Relevantly, the decision deals with the construction of s 180(1) of the *Corporations Law*, which was in identical terms to s 180(1) of the *Corporations Act*. That subsection provided:

> "180(1) A director or other officer of a corporation must exercise their powers and discharge their duties with the degree of care and diligence that a reasonable person would exercise if they:
> (a) were a director or officer of a corporation in the corporation's circumstances; and
> (b) occupied the office held by, and had the same responsibilities within the corporation as, the director or officer."

The wording in paragraph 180(1)(b) was the result of amendments which took effect on 13 March 2000, apparently in response to concerns in the business community arising from the decision of the New South Wales Court of Appeal in *Daniels v Anderson* (1995) 37 NSWLR 438.

In *ASIC v Rich* the central issue was the meaning of "responsibilities" in that provision. Austin J held that the word "responsibilities" is not concerned only with specific tasks delegated to the relevant director through the articles or by resolution or otherwise. Rather,

> "It is a wider concept, referring to the acquisition of responsibilities not only through specific delegation but also through the way in which work is distributed within the corporation in fact, and the expectations placed by those arrangements on the shoulders of the individual director."[1]

ASIC asserted in its pleading that Mr Greaves had various responsibilities in relation to the company by reason of, inter alia, his position as chairman. ASIC adduced evidence in support of its assertions by way of reports of two experts as to the usual responsibilities of the chairman of a listed company in Australia, as well as further material including reports and codes of conduct, which His Honour referred to generically as corporate governance literature. His Honour concluded that this evidence appeared to provide a reasonably arguable case that Mr Greaves had the responsibilities pleaded by ASIC.

It was in that context that His Honour referred to community expectations, as follows:

> "It may appear, at first blush, to be unduly harsh on a person in Mr Greaves' position that evidence of this kind might be relied upon to establish that in 2001 he was subject to responsibilities and, ultimately, legal duties never before set out in a statute or by judicial decision. It should be remembered, however, that the Court's role, in determining the liability of a defendant for his conduct as company chairman, is to articulate and apply a standard of care that reflects contemporary community expectations. It is now commonplace to observe that the standard of care expected of company directors, both by the common law (including equity: see *Australian Securities and Investments Commission v Adler* (2002) 168 FLR 253 at 347-349) and under statutory provisions, has been raised over the last century or so. One might correspondingly expect that the standard for company chairmen has also been raised. In *Commonwealth Bank of Australia v Friedrich* (1991) 5 ACSR 115, Tadgell J said (at 126):
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> > "As the complexity of commerce has gradually intensified (for better or for worse) the community has of necessity come to expect more than formerly from directors whose task is to govern the affairs of companies in which large sums of money are committed by way of equity capital or loan. In response, the parliaments and the courts have found it necessary in legislation and litigation to refer to the demands made on directors in more exacting terms than formerly . .."
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> Over the dozen years since Tadgell J wrote those words, there has been an enormous outpouring of literature concerning corporate governance, and there has been much debate in the Australian commercial community as to the effects the new thinking should have in practice. The Court must perform

[1] (2003) 174 FLR 128 at 140, para [50]

> the difficult task of articulating a standard of care by reference to community expectations, in an area not frequently traversed in litigation. It seems to me preferable for the Court to embark upon this task with a measure of assistance from the kind of evidence ASIC proposes to advance, than to choose the only other alternative, namely to rely on unassisted armchair reflection."[2]

His Honour's comments in the above passage relate to the evidence which might be used by a court in determining the standard of care and diligence against which a director's conduct is to be judged.

His Honour's comments do not address the issue of the extent to which, and on what basis, directors may consider "stakeholder" interests, and nor do they address the interaction between directors' duties and Principle 10 of the Stock Exchange's Corporate Governance Principles.

Nevertheless, *ASIC v Rich* could arguably be called in aid of the proposition that material such as the Corporate Governance Principles and various statements and codes relating to corporate social responsibility, as well as expert evidence relating to community expectations in relation to corporate social responsibility ought to be admissible in proceedings against a director for breach of duty, where the director's defence involves some element of corporate social responsibility.

Second Question

At pages CFS 12 to 15 of the committee *Hansard*, discussion ensued on the breadth of application of any corporate social responsibility reporting obligations that may be applied to companies and corporate groups.

The Task Force was requested to make further submissions on this question.

Section 292 of the *Corporations Act* is the principal provision that specifies who must annually prepare and release a financial report and a director's report[3]. Under that section these reports must be prepared by:

- all disclosing entities
- all public companies
- all large proprietary companies
- all registered schemes, and
- all small proprietary companies controlled by foreign companies that are not consolidated for the relevant period in accounts lodged by the foreign company or a company, registered scheme or disclosing entity.

Sections 293 and 294 specify additional situations where a small proprietary company may be directed to prepare such reports, either by their shareholders or by the ASIC.

The content requirements for those reports are specified in sections 299, 299A, 300 and 300A. In those sections, different requirements are specified for ASX listed entities and the other entities referred to above, with generally more onerous reporting obligations placed on ASX listed entities.

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[2] (2003) 174 FLR 128 at 147, para [71-72]
[3] Additional provision is made in sections 302 to 306 of the *Corporations Act* for half-yearly reports.

We submit that any corporate social responsibility reporting regime that is introduced be applied to all the companies and other entities that are required to prepare reports under sections 292, 293 and 294. Particularly, we submit that the corporate social responsibility reporting regime not only apply to listed public companies and listed public company groups.

We further submit that in respect of the corporate social responsibility reporting, the exemption that applies to small proprietary companies that are controlled by a foreign company not apply on a wholesale basis, but rather only to the extent that any reports lodged by the controlling foreign entity do not cover such reporting requirements as are legislated in Australia in this regard. The Task Force does not see why such Australian companies should be exempted from these requirements by what may be inadequate reporting obligations in a foreign jurisdiction for a controlling foreign company. As an Australian corporate citizen, the laws of another jurisdiction should not determine what standards of corporate behaviour are reported on in Australia.

We hope that our further response will assist the committee in its deliberations.

Yours faithfully

Daren Armstrong
Secretary
Legislative Review Task Force