CHAPTER 12

DIRECTORS' PERSONAL LIABILITY FOR ACTS OF THE COMPANY

12.1 In the preceding chapter, shareholders' remedies against directors were considered. In this chapter, directors' liability is considered in so far as directors are the mind and will of the company and, in that sense, have duties and responsibilities on behalf of the company to the wider community. Ways in which directors can prevent harm or breaches of legislation occurring are also discussed.

12.2 Directors' personal liability can arise under both company law and under a range of laws which affect the conduct of corporations. The 'corporate veil' does not shield them from personal liablity in all circumstances.

Corporate personality

12.3 The concept of a corporation having a legal personality, distinct from the personality of each of its members, was affirmed in 1897 by the House of Lords in the case of Salomon v Salomon & Co Ltd.[1] A corporation is liable as a separate entity for its own actions. For example, a company can be liable in tort if it negligently supplies a product which causes damage,[2] it can be vicariously liable for negligent acts by its servants[3] and it can be sued for breach of contract.[4]

12.4 Traditionally, the law has concerned itself with natural

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1. *[1897] AC 22.*
2. *Eg Grant v Australian Knitting Mills Ltd [1932] AC 562.*
3. *Eg Lloyd v Grace, Smith & Co [1912] AC 716.*
4. *Eg Lee v Lee's Air Farming Ltd [1961] AC 12. See also Companies Code, s80 (Corporations Act, s182), and generally, Ford, HAJ, Principles of Company Law (4th ed), Butterworths, Sydney, 1986, chapter 5.*

persons and there were some difficulties in accepting into the criminal law the concept of corporate personality and corporate responsibility for criminal acts. A major problem stemmed from the fact that, despite a legal personality, a corporation is unable to think and act for itself and so it was difficult to attribute to a corporation the mental element necessary to establish certain offences. As well, as a matter of public policy, criminal behaviour must be considered to be beyond the powers of a corporation. Beyond these conceptual difficulties, certain procedural rules, though apposite when applied to natural persons, required adaptation before they were appropriate to corporations.[5]

12.5 Notwithstanding these difficulties, it is now accepted that a corporation can be liable for a wide range of offences. However, differences in the treatment at law of natural persons and companies have been inevitable due to the artificiality of the corporate personality. As was said to the Committee,

> the certificate of incorporation cannot get behind the wheel of a car.[6]

12.6 Because a company must act through a natural person, the distinction between what are to be taken as the acts of the company and the acts of the individual can be a nice point.

12.7 Where fault must be proved, it is attributed to a corporation by imputing to the corporation the actions or behaviour of an individual within the corporation:

> A living person has a mind which can have knowledge or intention or be negligent and he has hands to carry out his intentions. A corporation has none of these: it must act through living persons, though not always one

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5. *See Welsh, RS, 'The Criminal Liability of Corporations' (1946) 62 Law Quarterly Review 345; also see Law Reform Commission of Canada, Working Paper 16, Criminal Responsibility for Group Action.*
6. *Evidence, p 139 (Mr Harper).*

> or the same person. Then the person who acts is not speaking or acting for the company. He is acting as the company and his mind which directs his acts is the mind of the company.[7]

12.8 Identification of the corporation with the individual is made on the basis that the individual whose actions are imputed to the corporation is in a position which allows a degree of control over the relevant corporate behaviour:

> A company may in many ways be likened to a human body. It has a brain and nerve centre which controls what it does. It also has hands which hold the tools and act in accordance with directions from the centre. Some of the people in the company are mere servants and agents who are nothing more than hands to do the work and cannot be said to represent the mind or will. Others are directors and managers who represent the directing mind and will of the company, and control what it does. The state of mind of these managers is the state of mind of the company and is treated by the law as such.[8]

12.9 It is a question to be decided in each case whether, in doing certain acts, a particular person is to be regarded as the company itself or as its servant or agent. In the latter situation, the liability of the company can only be statutory or vicarious. In the former situation, the person

> is not acting as a servant, representative, agent or delegate. He is an embodiment of the company or, one could say, he hears and speaks through the persona of the company, within his appropriate sphere, and his mind is the mind of the company. If it is a guilty mind then that guilt is the guilt of the company.[9]

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7. *Tesco Supermarkets Ltd v Nattrass [1972] AC 153 at 170 per Lord Reid.*
8. *HL Bolton (Engineering) Co Ltd v TJ Graham & Sons Ltd [1957] 1 QB 159 at 172 per Denning LJ.*
9. *Tesco Supermarkets Ltd v Nattrass [1972] AC 153 at 170 per Lord Reid.*

12.10 Clearly directors will often be in a position where their actions will be taken as those of the corporation. Actions of delegates of the board and other superior officers will also often be identified in that way. Those of subordinate officers, carrying out orders from above, will seldom be of that kind. For the corporation to be liable for the actions of the officer, the officer must be acting within the scope of his or her authority.[10]

Individual liability

12.11 Individuals may be made liable for corporate misconduct under statute or doctrines which impose such liability. This is referred to as lifting or piercing the corporate veil.[11] For example, individual liability may be imposed by statutory provisions such as sections 82, 229A and 556 of the Companies Code (Corporations Act, ss186, 233 and 592 respectively), or provisions in other legislation such as section 53 of the Environmentally Hazardous Chemicals Act 1985 (NSW).

12.12 In relation to cases in which the corporate veil may be lifted, Gower has said:

> [T]hey reveal no consistent principle beyond a refusal by the legislature and the judiciary to apply the logic of the principle laid down in Salomon's case where it is too flagrantly opposed to justice, convenience or the interests of the Revenue.[12]

Hamilton v Whitehead

12.13 An example of a statutory provision in the companies

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10. *Moore v I Bresler Ltd [1944] 2 All ER 515.*
11. *See Redmond, Paul, Companies and Securities Law - Commentary and Materials, Law Book Co Ltd, Sydney, 1988, pp 137-51, for discussion of the kinds of cases in which the corporate veil has been lifted.*
12. *Gower, LCB, Gower's Principles of Modern Company Law (4th ed), Stevens & Sons, London, 1979, p 112.*

legislation which imposes personal liability on a director, in addition to the liability on a company, is section 38(1) of the Companies and Securities (Interpretation and Miscellaneous Provisions) (Western Australia) Code:[13]

> A person who aids, abets, counsels or procures, or by act or omission is in any way directly or indirectly knowingly concerned in or party to, the commission of an offence against any relevant Code shall be deemed to have committed that offence and is punishable accordingly.

This section has the same effect as the general accessory provision in the Crimes Act 1914 (Cth).[14]

12.14 In Hamilton v Whitehead[15] the High Court found that a (managing) director was personally liable for acts of the company. The director had been 'knowingly concerned' in the commission of offences by the company because he had committed the wrong and knew of all the relevant circumstances.

12.15 The company itself had been found liable under section 169 of the Companies Code (Corporations Act, s1064).[16] Section 38(1) of the Companies and Securities (Interpretation and Miscellaneous Provisions) (Western Australia) Code made the director liable in addition to the company.

12.16 The High Court said:

> [T]he fundamental purpose of the companies and securities legislation - to ensure the

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13. *This code, and similar codes in each of the States and the Northern Territory, adopted the substantive provisions of the Companies and Securities (Interpretation and Miscellaneous Provisions) Act 1980 (Cth), incorporating minor variations relevant to each particular jurisdiction.*
14. *Section 5.*
15. *(1989) 7 ACLC 34.*
16. *Pursuant to s169, the company was liable in so far as, being unauthorised, it had offered or issued to the public a prescribed interest in a syndicate trust.*

> protection of the public - would be seriously undermined if the hands and brains of a company were not answerable personally for breaches of the Code which they themselves have perpetrated.[17]

Allocation of individual and corporate liability

12.17 Making individuals liable for misdeeds of a company is not a novel concept. However, even today it seems to be the exception rather than the rule.[18] One study of the enforcement of corporate law in Australia shows that liability is usually directed at the corporate entity:

> Prosecutions are overwhelmingly directed at companies rather than at individuals who acted on behalf of the company. Only twenty [of the 96 regulatory agencies surveyed] ... had a policy or preference for prosecuting individuals rather than companies, mostly in the mining and marine areas ... Mine safety regulation is notable for fostering individual accountability through statutes which nominate in some detail the responsibilities of individuals who fulfil various roles in the organization.[19]

12.18 Individual and corporate liability are not mutually exclusive. The problem is to find the appropriate balance.[20]

Examples from other jurisdictions

12.19 A common theme running through submissions to the Committee was that the duties and obligations (and consequent liability) imposed on company directors in Australia were already sufficient, if not over-burdensome. Anecdotal examples of

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17. *Hamilton v Whitehead (1989) 7 ACLC 34 at 38-9.*
18. *See submission from Professor Fisse, p 24.*
19. *Grabosky, Peter and Braithwaite, John, Of Manners Gentle - Enforcement Strategies of Australian Business Regulatory Agencies, Oxford University Press in association with Australian Institute of Criminology, Melbourne, 1986, p 189.*
20. *See submission from Professor Fisse, pp 17-18.*

individual liability for corporate misconduct in the United States were cited with disapproval.[21]

12.20 The Committee notes reports of one of the first successful prosecutions of a corporate executive for negligent homicide in the United States.[22] When two employees died in Austin, Texas in 1986 as a result of the collapse of a 30 foot trench in which they were working, charges were laid against the company and its president. Neither contested the charges. The company was fined $10 000. The president was sentenced to a six month gaol term, with probation in lieu, together with an additional six months probation and a $2000 fine. Occupational Safety and Health Administration officials found the trench had not met the required standards.[23]

12.21 Recent research supported by the Institute for Civil Justice in the United States shows

> a surge of suits against the directors and officers of corporations alleging personal responsibility for such torts as defective products or losses arising from merger rejections.[24]

12.22 It quotes an annual survey of US directors' and officers' liability which showed that the percentage of companies with a director against whom a liability claim was brought rose from 7% in 1974 to 18% in 1984. The average cost for a successful claim (excluding legal fees) rose from less than $US900 000 in

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21. *Eg Evidence, pp 105-6 (Mr Peters), 430 (Mr Webber).*
22. *Corporate Crime Reporter, vol 1, no 2, Monday April 20 1987, p 4.*
23. *According to the report, this case was to have been appealed on a technical point regarding the inter-relationship of state and federal legislation - Corporate Crime Reporter, vol 1, no 2, Monday April 20, 1987, p 5.*
24. *Reuter, Peter, The Economic Consequences of Expanded Corporate Liability: An Exploratory Study, RAND Corporation, USA, November 1988, p 28.*

1980 to almost $US2 million in 1986.[25]

12.23 Individual liability for corporate misconduct appears to be a strong tradition in Japan.[26] For example, the Japanese Supreme Court upheld a ruling that the president and a plant director of a company were responsible for deaths caused by contaminated water discharged from the company's plant in the 1950s. The two were sentenced to two years imprisonment and placed on three years probation. It has been estimated that as many as 10 000 people may have been affected, some fatally, by the discharge of methylene chloride mercury-contaminated water. By 1975, the company had paid out an estimated $80 million to 785 victims of mercury poisoning.[27]

12.24 In the USSR, three directors were sentenced to ten years hard labour following the Chernobyl nuclear plant disaster.[28]

12.25 In the United Kingdom, it is reported that three former directors of the P&O shipping group are to be prosecuted for manslaughter following the Zeebrugge ferry disaster in March 1987.[29] In that accident, 193 lives were lost when a ferry sank as it left the port. The bow doors had been left open. Summonses were issued against various officers who were on the ferry at the time and against the ferry company itself. This will be the first time in the United Kingdom that a company has been prosecuted for manslaughter.

12.26 The directors and seamen face a maximum penalty of life

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25. *Reuter, Peter, The Economic Consequences of Expanded Corporate Liability: An Exploratory Study, RAND Corporation, USA, November 1988, p 28.*
26. *See, eg, Braithwaite, John and Fisse, Brent, 'Varieties of Responsibility and Organizational Crime' (1985) 7 Law & Policy 315 at 317.*
27. *Corporate Crime Reporter, vol 2, no 20, Monday May 23 1988, p 3.*
28. *Wells, Celia, 'The Decline and Rise of English Murder: Corporate Crime and Individual Responsibility' [1988] Crim L Rev 788 at 799.*
29. *The Guardian Weekly, 2 July 1989, p 4.*

imprisonment. The ferry company faces an unlimited fine. If the cases against the individuals are successful, there will be ramifications elsewhere, for example, for those involved in the Kings Cross underground disaster where no prosecution has yet been brought against any individual.

Submissions

12.27 BHP Limited expressed concern at '[t]he nature of some of the liabilities imposed upon directors, and the trend to extend them'.[30] It said:

> In some instances liabilities appear to be imposed indiscriminately, without regard to principle. The singling out of directors (and in some cases other officers of companies) for this treatment, as compared with the treatment of those who carry responsibility for the affairs of other organisations in the public and private sectors, cannot be justified. While directors cannot avoid bearing responsibilities, and the law must seek to deal with dishonest and fraudulent conduct, there is no good to be gained by subjecting directors as a group to unrealistic personal liability.[31]

12.28 The Company Directors' Association referred to personal responsibility imposed on company directors by State and Commonwealth legislation and said:

> As a matter of principle the [Company Directors'] Association believes that imposing such responsibilities has gone beyond bounds. The corporation is the body responsible and the corporate veil should not be lifted just to ensure compliance [with] a statute.[32]

12.29 Professor Fisse saw no reason for changing the law in so

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30. *Submission, para 19 (Evidence, p 608).*
31. *Submission, para 19 (Evidence, p 608).*
32. *Submission, p 13 (Evidence, p 92).*

far as it allowed for a mix of personal and corporate criminal liability. He cautioned, however, that proposals to extend strict liability for company acts which violated statutory requirements to corporate officers were 'highly problematical' because to do so would violate the traditional precept that criminal liability requires blameworthiness on the part of an accused.[33]

12.30 He recommended 'a much less drastic change'. As the law now stands, a director is liable for complicity, or for being knowingly concerned in an offence, where he or she intentionally gives assistance or encouragement to the commission of that offence. Professor Fisse said that a director's liability for complicity should be extended to cover the situation where he or she recklessly assists or encourages the commission of an offence by another. This would be consistent with the English position at common law.[34]

12.31 The Committee recommends that **the law be amended to make a director personally liable for complicity where he or she intentionally or recklessly assists in or encourages an act which constitutes an offence by a company.**

Indemnification

12.32 Many submissions said the indemnification of directors was a difficult issue.[35] It was suggested that an increase in directors' personal liability would reduce the pool of those prepared to take on a directorship.[36] This would be so

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33. *Submission, p 16.*
34. *Submission, p 17.*
35. *See, eg, submissions from Peat Marwick Hungerfords, p 4 (Evidence, p 6); Company Directors' Association of Australia, p 10 (Evidence, p 89); Institute of Directors in Australia, pp 8-12 (Evidence, pp 126-30); Mayne Nickless Ltd, p 2 (Evidence, p 374); BHP Ltd, para 22 (Evidence, p 609); Desane Group Holdings Ltd, p 1; Attorney-General's Department, paras 5.8-11; Evidence, pp 64-5 (Mr Middleton, Mr Prosser); 99-100 (Mr Peters); 635 (Mr Loton).*
36. *Eg, submissions from BHP Ltd, para 19 (Evidence, p 608); NCSC, pp 5-6 (Evidence, pp 564-5).*

particularly if there were difficulties obtaining indemnification. It has been reported that increases in the personal liability of directors in the United States have made it more difficult to obtain outside directors. This means that US boards now face less than the desired ratio of outside to inside directors.[37]

12.33 As the Companies and Securities Law Review Committee has investigated the question of indemnification,[38] the Committee has not pursued this matter.

Individual liability may be appropriate

12.34 Many submissions recognised that there were circumstances where directors should bear personal liability for acts done in the company's name. For example, Dr Pascoe, speaking for the Business Council of Australia, said if directors of a company knew that polluting substances were being dumped in a sensitive area by the company and condoned the action, they should be held responsible for that action.[39]

12.35 Mr Harper, Federal President of the Institute of Directors in Australia, said:

> The fact that an anti-social act is committed requires that some action be taken by the community to put that anti-social act right or to prevent it happening again. The fact that a company is responsible for doing an anti-social act means that some officer of the company is responsible for the action being taken. If it is quite clear that any ordinary person with decent feelings would realise that he was committing an anti-social act then

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37. *Reuter, Peter, The Economic Consequences of Expanded Corporate Liability: An Explanatory Study, RAND Corporation, USA, November 1988, p 29.*
38. *Companies and Securities Law Review Committee, Discussion Paper No 9, Company Directors and Officers: Indemnification, Relief and Insurance (April 1989).*
39. *Evidence, pp 492-3.*

> clearly that person is responsible. That person may or may not be a director of the company. ... The directors as such are paid their modest fees for the purpose of taking responsibility for the actions of the officers of the company, and therefore ultimately in an anti-social act because of the way our system is structured, the directors are responsible.[40]

12.36 Mr Harper emphasised that, in his view, personal liability of a director should depend on the nature of the 'anti-social act' and on whether the director had been criminal or negligent in what he or she did.[41]

Development of policy

12.37 The Company Director's Association, and others, spoke of the trend towards imposing personal liability on directors.[42] It appears that legislators are thinking more and more in these terms.[43] Mr Loton spoke of 'the rather piecemeal approach in legislation to the imposition of specific legal liabilities on directors and the way in which those liabilities are sometimes extended'.[44]

12.38 Professor Fisse wrote that

> [t]he present law provides for both individual and corporate liability but makes no attempt to achieve a well-balanced mix; the balance in fact achieved depends on the vicissitudes of

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40. *Evidence, pp 139-40.*
41. *Evidence, p 140.*
42. *Eg, submissions from Company Directors' Association of Australia, p 13 (Evidence, p 92); BHP Ltd, para 19 (Evidence, p 608); Evidence, pp 576 (Mr Bosch, Senator Hill), 614-15 (Mr Loton).*
43. *See, eg, The Sydney Morning Herald, 11 March 1989, p 4, quoting the NSW Minister for the Environment, the Hon Tim Moore MLA, proposing substantial personal liability for company directors for acts of companies in relation to environmental matters. See also submission from Mr Sumner, SA Attorney-General and Minister of Corporate Affairs and chairman of the Ministerial Council for Companies and Securities.*
44. *Evidence, p 614.*

prosecutorial discretion.[45]

12.39 Where there is a practice of prosecuting corporations rather than individuals, no matter what the circumstances, there is a risk that people within the company who ought be held liable will never be called to account for their actions. This practice is often followed as a matter of convenience and has no policy underpinning it.[46] No proper thought is given to the best means of preventing future misconduct.

12.40 The way corporations are prosecuted and punished provides little incentive for them to use 'their internal disciplinary systems to sheet home individual accountability'.[47] It is often far less disruptive and embarrassing, and indeed cheaper, for the corporation to pay the fine and let the matter rest.[48]

12.41 Whether a company or an individual should be held liable for corporate misconduct in any given circumstances, or whether liability should be apportioned between the two, is an issue properly decided according to principle. It should not be determined according to the 'vicissitudes of prosecutorial discretion'.[49] Regulators should act according to a policy which vindicates the rights of people vulnerable to ill conduct of companies.

Relevant factors

12.42 Factors which ought to be taken into account when formulating such a policy include:

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45. *Submission, pp 18-19.*
46. *See submission from Professor Fisse, p 19.*
47. *Submission from Professor Fisse, p 19. See also Fisse, Brent and Braithwaite, John, 'Accountability and the Social Control of Corporate Crime: Making the Buck Stop' 20(1) Australian Journal of Forensic Sciences, September 1987, p 166.*
48. *Submission from Professor Fisse, pp 19, 22-3.*
49. *Submission from Professor Fisse, p 19.*

- cost - to prosecute a corporation could be more convenient and cheaper than prosecuting a number of individuals;

- establishing liability - it will be easier to establish the requisite mental element in the case of an individual than in that of a corporation. It may be open to prosecute the company in any case where the mental element of the individual can be imputed to the company;

- securing an effective remedy - where it is cheaper for a company to remedy internal controls which may have failed than to pay a fine, potential prosecution of a corporation might be a more effective remedy;

- admissions of guilt - proof of guilt is often based on admissions, and it may be unclear who would have the authority to make admissions on behalf of a company;

- the law as it is - traditionally, the criminal law has dealt with individual rather than corporate offenders. There is much common sense in this because it is actually individuals who commit crimes, rather than corporations. This approach denies, however, the separate legal personality of the corporation. As a legal entity, it should be subject to legal sanctions;

- the nature of sanctions - an individual may have to pay a fine from his or her personal resources; a fine levied against a corporation must be borne by the shareholders and perhaps by the consumers. Individuals or corporations may be injuncted, either to prevent or to force action. A director can be disqualified or sent to gaol. A corporation can be wound up.

12.43 Professor Fisse submitted that one way of achieving accountability for corporate misconduct, and of achieving a better mix of individual and corporate liability,

> would be to structure enforcement so as to activate and monitor the private justice systems of corporate defendants.[50]

12.44 In other words, he said it may be more efficient to devise some means of forcing a corporation which has transgressed to conduct its own inquiry as to who was responsible within the organisation. The corporation could be required to apportion blame and to discipline those responsible, and to design a means of avoiding such transgressions in the future, to the satisfaction of the court. A further advantage of this approach is that taxpayers would not have to bear the burden of costs associated with investigation.[51] Professor Fisse has said this idea requires further development if it is to be implemented successfully.[52] It was not developed in the evidence before the Committee.

12.45 The Committee has elsewhere commented on the need for adequate enforcement of the law (see chapter 10). Enforcement action must be targeted in a principled way. The development of a policy to direct enforcement is a detailed and technical matter which should be addressed urgently. It is not desirable that development continue in its present ad hoc manner. It should take into account corporate organisational culture. All relevant regulatory agencies should play a part in its development. The economic advantages which have flowed to the community as a result of corporate endeavour are great, but the corporate form should not be used as a mask.

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50. *Submission, p 25.*
51. *Submission from Professor Fisse, pp 26-9.*
52. *Submission, p 29.*

12.46 The Committee recommends that

(i) the appropriate mix of individual and corporate liability for corporate misconduct be referred to a body such as the Australian Law Reform Commission for detailed investigation and report;

(ii) the matter be investigated and researched in close consultation with all persons and community groups who are willing and able to contribute; and

(iii) the aim of such a review be to develop a theoretical basis to guide the future drafting of legislation and prosecution guidelines.

Legal risk management

12.47 The imposition of legal obligations on corporate activities generates the need for compliance systems in all but the smallest companies. A 'compliance system' is an institutionalised method of preventing illegal or unsatisfactory conduct or outcomes.[53]

12.48 A compliance system could involve drawing up guidelines or statements of policy, implementation of certain procedures (eg designed to ensure safety or quality), clear allocation of responsibility, monitoring compliance with statutory requirements, or general educative programs for company personnel.[54] The system required will depend on the circumstances but

> in companies of any size, compliance with legal duties is typically not a matter simply of individual choice but depends upon organisational policies and operating

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53. *Fisse, Brent, 'Legal Risk Management and Corporate Strategy', unpublished paper, Sydney, November 1987, p 6.*
54. *Ibid, pp 8-10.*

procedures.[55]

12.49 Professor Fisse said:

> It is entirely conceivable that a company director may be held civilly or criminally liable under s.229(2) of the Companies Code [Corporations Act, s232(4)] if a suitable compliance system is not in place in his or her company. There is also the possibility of civil liability for the tort of negligence. Furthermore, criminal or civil liability can arise under a wide variety of statutory provisions requiring the taking of reasonable care.[56]

12.50 Professor Fisse acknowledged

> a vast proliferation of rules governing particular facets of company operations (e.g., accounting requirements, occupational health and safety regulations),[57]

but pointed out that generally companies are given the freedom to regulate their own internal affairs. This did not mean, however, that the adequacy or otherwise of compliance systems would be immune from legal scrutiny.[58]

12.51 He gave the following example:

> Assume that the board of directors of a merchant bank delegates all tasks of fraud prevention to a compliance manager and then exercises no supervisory role over his or her compliance activities. Assume further that the compliance manager takes an unduly optimistic or casual view of the compliance function delegated and that the company's financial health is jeopardised by a number of middle managers who have engaged in manipulation of

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55. *Fisse, Brent, 'Legal Risk Management and Corporate Strategy', unpublished paper, Sydney, November 1987, p 5.*
56. *Submission, p 1.*
57. *Submission, p 1.*
58. *Submission, pp 1-2.*

> share prices, trading ahead of customers on the futures exchange, and money-laundering. In supposing that the compliance officer would prepare adequate compliance procedures, and in refraining from demanding any assurances of adequacy, have the members of the board violated s. 229(2) of the Companies Code by failing to use reasonable care and diligence in monitoring the company's compliance efforts? Should they have insisted on at least quarterly or half-yearly reports by the product safety officer as to the nature and extent of the company's compliance system?[59]

12.52 Professor Fisse submitted:

> It may be argued that, in the absence of any reason to suspect that the compliance officer would not properly discharge the function delegated, there is no liability. Certainly there is some support in the case law for this position [see, eg, Re City and Equitable Fire Insurance Co Ltd [1925] Ch 407 at 429 per Romer J; Graham v Allis Chalmers 188 A 2d 125 (1963)]. On the other hand, it may be argued that prevention of fraud is a matter of such significance for a merchant bank that failure to monitor compliance by requiring periodic reports and assurances may amount to lack of reasonable care by the directors in exercising their power to manage the business of the company. Losses associated with non-compliance may easily be more significant than some of the traditional items of financial business on the agenda of board meetings, and hence it would be unwise to assume that the duty under s.229(2) is confined only to the traditional areas of fiscal command expected of directors in the past.[60]

12.53 Companies' boards should consider legal risk management as it applies to their particular circumstances:

> Unsatisfactory compliance policies and procedures can be directly in issue in a

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59. *Submission, p 2.*
60. *Submission, p 3.*

> variety of contexts, including the tort of negligence and statutory offences of failing to exercise due diligence to prevent a contravention [eg under s229(2) of the Companies Code].[61]

12.54 Precedents set under the Trade Practices Act indicate that the existence of compliance measures are taken into account in the assessment of penalty.[62] For example, in a recent resale price maintenance case under the Trade Practices Act, Judge Fisher, in assessing penalty, regarded seriously the fact that an officer of the defendant corporation

> had not been made aware or fully aware of the company's obligations under the [Trade Practices] Act and its policy of compliance therewith.[63]

This was notwithstanding evidence that the board of directors itself took its obligations seriously. The judge said

> its failure to impress upon its employees and its senior management these obligations is particularly culpable.[64]

12.55 In <u>Henderson v Australasian Conference Association Limited</u>,[65] 'informal and slipshod' product recall procedures sounded in penalties although there was 'no moral turpitude, no dishonesty and no profit making involved'.[66] In <u>Trade Practices</u>

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61. *Submission from Professor Fisse, pp 1-2.*
62. *See Frieberg, Arie, 'Monetary Penalties Under the Trade Practices Act 1974 (Cth)' (1983) 11 <u>Australian Business Law Review</u> 4.*
63. *<u>Trade Practices Commission v General Corporation Japan (Aust) Pty Ltd</u> (1989) ATPR 40-922 at p 49,977.*
64. *Ibid.*
65. *(1987) ATPR 40-801.*
66. *Ibid at p 48,710.*

Commission v Annand and Thompson Pty Ltd,[67] the penalty was assessed 'towards the lower end of the scale' because it was 'a "one-off" instance, which occurred despite attempts ... to inform ... employees of the requirements of the [Trade Practices] Act'.[68] In Dawson v World Travel Headquarters Pty Ltd,[69] the failure of a fail-safe system, in the absence of dishonest or deliberate conduct, was considered a mitigating factor.

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67. *(1987) ATPR 40-772.*
68. *Ibid at p 48,394.*
69. *(1981) ATPR 40-193.*