



**CHARTERED SECRETARIES  
AUSTRALIA**

*Leaders in governance*

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Mr John Kluver  
Executive Director  
CAMAC  
Level 16  
60 Margaret Street  
SYDNEY NSW 2000

By mail  
and by email: [john.kluver@camac.gov.au](mailto:john.kluver@camac.gov.au)

Dear Mr Kluver

**Corporate Duties Below Board Level  
Discussion Paper**

Chartered Secretaries Australia (CSA) welcomes the opportunity to comment on the discussion paper *Corporate Duties Below Board Level*.

CSA is Australia's peak professional body delivering accredited education and the most practical and authoritative training and information on governance, as well as thought leadership in the field. In Australia, CSA has over 8,000 members and affiliates working as company secretaries, governance professionals and other officers in corporations, who advise their boards on matters of governance.

Members of CSA have a thorough working knowledge of directors' and officers' duties and the *Corporations Act 2001*.

General comments

In respect of the discussion paper, CSA comments that, in principle, it supports extending the personal duties and liabilities under the *Corporations Act* beyond directors and other officers. CSA believes there is a gap in liability below board level. The current law on the liability of senior managers not classified as officers is unclear. Any legal regime for the enforcement of corporate governance standards that does not include the acts or omissions of at least some categories of senior managers not classified as officers will not be as effective as it should be.

CSA recognises that extending these duties could bring about a better delegation of authority from the board to management. An exposure to liability based on a functional model, rather than on an employment relationship model, which extends the category of persons facing the liability into the senior management range, must produce an enhanced sense of responsibility and accountability in corporate decision making.

An extension of liability, by one method or another, along the lines proposed in the discussion paper, will enhance applied corporate governance. Risk management and compliance systems introduced by companies are likely to be more meaningfully implemented if some degree of direct liability accompanies those persons responsible for the implementation and ongoing management of them. It will also give more meaning to the law's move towards effective protection for whistleblowers.

While CSA strongly believes that directors should be responsible for the oversight of corporations, that is, they are responsible for the strategy and vision of a corporation, the HIH Insurance example illustrates the desirability of extending formal liability so that it attaches, at appropriate levels, to internal corporate functional responsibility. This is the essence of good governance, with responsibility and accountability aligned.

At the same time, it will not eliminate the other responsibility of the board to set appropriate policies and to review these regularly. Indeed, it is important that a proper delegation of authority needs to be in place so that individuals will not be liable simply because they are carrying out functions nominated by senior managers. If individuals are carrying out functions that are not authorised, however, then they should be held liable.

#### *The issue of consent*

CSA has considered the issue of consent, which was not highlighted in the discussion paper. CSA does not believe that the introduction of a consent model is necessary to achieve an extension of liability in a company. The person in whatever function they perform, by accepting a position with the company, consents to carry out that function. Therefore, it is recommended that the relevant current sections in the *Corporations Act* on consent for directors and the company secretary not be amended and that the responsibility be left to corporations to ensure that, as for other areas of legal obligations, management identifies those persons who have legal obligations and communicate to and train them to ensure that they have adequate knowledge of the law. Obtaining written acknowledgement from the person carrying out the function that they have been made aware of their obligations should be part of that process.

The concept of a senior manager possibly avoiding liability only because they have failed to sign a consent to act is unacceptable and would lead to inappropriate behaviour. The need for more stringent delegation and updating of the employee's functionality when they change jobs within the company would, rather, be a useful addition to a governance framework.

#### *The issue of insurance*

If amendments are made to the legislation extending liability in a company and to non-employees carrying out functions in the company, it is crucial that both the indemnification sections in the *Corporations Act* and perhaps other legislation, and directors' and officers' (D&O) insurance policies are reviewed to ensure these issues are aligned. For example, some D&O policies only cover officers and few, if any, would cover non-employees unless they also hold the role of director or secretary.

#### Recommendation 1

In principle, CSA supports extending the personal duties and liabilities under the *Corporations Act* beyond directors and other officers. CSA believes there is a gap in liability below board level. The current law on the liability of senior managers not classified as officers is unclear.

CSA recommends that the relevant current sections in the *Corporations Act* on consent for directors and the company secretary not be amended and that the responsibility be left to corporations to ensure that, as for other areas of legal obligations, management identifies those persons who have legal obligations and communicate to and train them to ensure that they have adequate knowledge of the law.

Proposals in discussion paper

*Proposals 1 and 2*

**Should s 181 (the duty of good faith) (and its criminal consequences under s 184(1)) and s 180(1) (the duty of care and diligence) be extended beyond directors and other officers of a corporation to a wider category of persons?**

Recommendation 2

CSA supports the extension of s 181 (the duty of good faith) and s 180(1) (the duty of care and diligence) to senior manager level (if those managers are not currently classified as officers), but only to those managers charged with particular responsibility (for example, mine managers, ship captains, treasury managers, a head of a significant division, or even the head of a functional department, such as a Director of Marketing) or taking part in significant decisions. It is not feasible to try to extend these liabilities to every person who “takes part in” management.

CSA believes the objective of the proposals can best be achieved by clarifying the definition of “officer”.

Provisions could be inserted into the *Corporations Act* that:

- (1) Combine sub-paragraphs(b)(i)&(ii) of the definition of “officer” and slightly amend it to say:
  - (b) *a person:*
    - (i) *who makes, or substantially participates in making, decisions that significantly affect the business affairs or financial standing of the corporation;*

This is essentially the same as the proposed definition of “management” (page 24 of the discussion paper). It retains the notion of a functional test and obviates the introduction of another category of person and the need for an additional definition.

- (2) For the avoidance of doubt, confirm that the officer is an officer of any corporation which is affected by the decision.

This addresses the corporate group issue (see later for further comments).

- (3) Confirm that the definition of “officer” is not limited by the existence of the definition of “senior manager” (see page 12 of the discussion paper).

It is noted that the definition applies to “a person” and is not limited to employees. The definition would apply to a consultant who is engaged to perform services of the type mentioned in the definition.

*Proposal 3*

**As a corollary of Proposal 2, should s 180(2) (the business judgment rule) be extended beyond directors and officers of a corporation to any other person who takes part, or is concerned, in the management of that corporation?**

Recommendation 3

The use of CSA's suggested solution to Proposals 1 and 2 (expanded definition of "officer") means that the business judgment rule will automatically apply without further amendment.

However, if another solution is chosen, CSA supports the concept that the business judgment rule should be available to any person who is subject to the duty under s 180.

*Proposals 4 and 5*

**Should ss 182 and 184(2) (improper use of corporate position) and ss 183 and 184(3) (improper use of corporate information) be extended beyond directors, other officers and employees of a corporation to any other person who performs functions, or otherwise acts, for or on behalf of that corporation?**

CSA supports the concept of extending ss 182 and 183 beyond directors, officers and employees in the manner proposed.

Contracts of engagement of consultants or contractors usually specify that the consultant is an independent contractor, not an employee, and is not authorised to bind the company to contracts, and usually excludes or limits the consultant's liability to the company.

There is a distinction between two types of contract in relation to this matter:

- 1 One type of contract is entered into for an individual or company to provide a service as an adviser, and such an individual or company makes recommendations only. Company officers consider that advice and, after taking into account all the factors, make a decision.
- 2 The second type of contract consists of an individual contracting (sometimes through their company) but acting or performing functions as if they were an employee, even though their contract says they are not an employee.

CSA is comfortable that the proposed words "performs a function, or otherwise acts, for or on behalf of the corporation" captures both groups. Whatever definition is used there will be some grey situations.

CSA does not believe that ss 182 and 184 should extend only to those persons who comprise the second group, as it is important that those individuals who make improper use of corporate information be held liable.

CSA notes that there are difficulties attached to the proposal as follows:

- There will need to be a provision that consultants/contractors cannot contract out of their statutory liability and cannot be indemnified by the company in this respect.
- There may be an impact on the market for professional indemnity insurance to cover this additional area of liability for contractors.

Currently, professional indemnity or even D&O insurance in their basic form will not cover penalties. There are some D&O policies that do, but these are fairly limited. The difficulty is that the company cannot indemnify for actions taken in bad faith or not in the interests of the company, and it is reasonable to assume that in most cases a breach invoking the law in this area would prevent the company from indemnification. However, the ability of the insurance to pay in advance for legal advice and assistance for the employee/contractor needs to be retained.

#### Recommendation 4

CSA supports the concept of extending ss 182 and 183 beyond directors, officers and employees in the manner proposed.

#### *Proposals 6 and 7*

**Should s 1309(1) (knowingly providing false or misleading information), s 1309(2) (veracity of information) and s 1307(1) (misconduct concerning corporate books) be extended beyond officers and employees of a corporation to any other person who performs, or has performed, functions, or otherwise acts or has acted, for or on behalf of that corporation?**

#### Recommendation 5

CSA supports the amendments in these two proposals, including the amendment to s 1309(2).

Officers and employees are already covered by these sections. Extending the liability to consultants or contractors acting on behalf of the company should ensure that such persons act with due care and this in turn assists the implementation of governance frameworks within companies by those charged with such responsibilities.

#### *Other proposals*

#### Recommendation 6

##### ***Item 2.2.4: General dishonesty prohibition***

CSA recommends that any such provision apply to the *Corporations Act* only. The discussion paper sets out the difficulties of applying any other approach.

#### Recommendation 7

##### ***Item 2.3: Definition of “employee”***

CSA is not in favour of defining the term “employee”.

The proposals for extending the various liabilities (either via a revised definition of “officer” as CSA proposes, or via the introduction of another category of person as in CAMAC's proposals) reduce the need to try to bring people within the category of “employee”.

CSA notes that “employee” is currently defined in s 596AA of the *Corporations Act* in the context of employee entitlements as “a person who is or has been an employee of the company...”. Attempting to define it further, or define it for other purposes, runs the risk of excluding some persons who might otherwise have been caught. What amounts to an “employee” has been the subject of many court decisions and any statutory definition will still be subject to interpretation by the courts in the circumstances of the particular case.

Recommendation 8

***Item 2.4: Corporate groups: What, if any, amendments are necessary to ensure that corporate group executives are properly subject to the duties in ss 180-184?***

CSA does not believe that an additional definition of the type on page 37 of the discussion paper is necessary.

CSA believes that the imposition of duties in ss 180-184 based on the performance of functions should be sufficient to cater for corporate groups.

Under the existing definition of “officer”, the “person” referred to in paragraph (b) is not required to be an employee of the corporation being affected by his/her decision. The person is an officer of the corporation merely because he/she makes or participates in a decision which affects the business or financial standing of the corporation.

This would appear to cover corporate groups because under paragraph (b) of the definition, the person will be an “officer” of the corporation which is affected by the decision. Paragraph (b) of the definition does not require any closer nexus than the fact that the corporation is affected by the decision.

Even though the existing definition of “officer” appears to be adequate in relation to corporate groups, the position would be improved by the adoption of CSA's suggested solution to Proposals 1 and 2, which involves three suggested actions to improve the definition of “officer”, including a clarifying provision, for the avoidance of doubt, that the officer is an officer of any corporation which is affected by the decision.

***Item 2.5: Other behaviour***

CSA has no recommendations in relation to this item.

Additional comment  
Recommendation 9

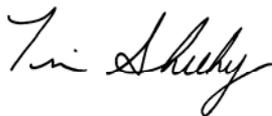
Section 189 of the *Corporations Act*: “Reliance on information or advice provided by others” provides a certain level of defence for directors in the limited circumstances set out in s 189(c) involving a duty under Part 2D.1 or an equivalent general law duty.

CSA is of the view that the benefit of this section should be extended to “officers” and any other persons who are exposed to the same duties as directors under Part 2D.1 or an equivalent general law duty.

Conclusion

In preparing this submission, CSA has drawn on the expertise of the members of its two internal national policy committees. We would welcome the opportunity to meet with you to discuss any of our views in greater detail. Please call me if you would like to set up a meeting. I can also arrange a meeting with our members.

Yours faithfully



Tim Sheehy  
CHIEF EXECUTIVE