

AUSTRALIAN INSTITUTE
of COMPANY DIRECTORS

Impact of Legislation on Directors

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AUSTRALIAN INSTITUTE of COMPANY DIRECTORS

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Executive Summary

Directors are subject to a wide range of responsibilities and potential personal liability under Federal and State legislation and regulations. In addition to the *Corporations Act 2001* and other Commonwealth statutes, there are more than 750 state laws affecting the director community. In many cases, directors can be found liable simply by virtue of their position, regardless of their actions, which is known as ‘derivative liability’. In some areas of legislation, there is a reverse onus of proof for directors (despite the fundamental legal and human rights principle is to be innocent until proven guilty).

Reform of corporate regulation, and especially laws which have a direct impact on directors and the way they operate, is a significant issue for the business community, for the economy and, ultimately, for Australian society as a whole.

To this end, the Council of Australian Governments (COAG) and the Ministerial Council for Corporations have a review of legislation imposing personal liability on company directors for corporate misconduct underway. This review is one of COAG’s 27 deregulation priorities¹.

The Australian Institute of Company Directors conducted a survey regarding the impact of legislation on directors in early 2010.

Key Findings

- **Awareness:** More than 82 per cent were aware of legislation that automatically imposes personal liability on directors for corporate breaches.
- **Personal Risk:** More than 73 per cent of respondents believe there is a medium to high risk of directors being found personally liable for decisions they have made in good faith (Figure 3.1).
- **Available defences:** 54 per cent do not believe there are reasonable defences available for directors (Figure 3.2).
- **Overly cautious decision-making:** 65 per cent said they felt the risk of personal liability had caused them or a board on which they sit to take an overly cautious approach to business decision-making frequently or occasionally (Figure 4.1).
- **Impact on optimal decision-making:** More than 90 per cent of respondents said that the personal liability of directors has an impact on optimal business decision-making or outcomes – ranging from marginal – 42.4 per cent to severe – 6.7 per cent (Figure 4.3).
- **Impact on contribution to the economy:** More than 59 per cent of respondents that indicated their primary organisation was headquartered / registered in Western Australia said the impact of personal liability had inhibited their organisation’s contribution to the broader economy (Figure 4.6).
- **Impact on director recruitment:** 56.8 per cent of respondents knew of other directors who had declined the offer of a directorship primarily due to the risk of personal liability (Figure 5.3), while 32.2 per cent personally declined an offer for this reason (Figure 5.1). 52.2 per cent said they knew of someone who had resigned from a board due to liability concerns (Figure 5.4); 22.2 per cent said they had resigned from a position themselves (Figure 5.2).
- **Concern for organisational impact:** More than 90 per cent of respondents were moderately to seriously concerned about the lost time and opportunity costs for companies defending actions brought as a result of automatic personal liability for directors, and corporate legal expenses that would be incurred (Figure 6.1).
- **Concern regarding personal impact:** More than 64 per cent of respondents said they were “seriously concerned” about the prospect of being subject to criminal and civil penalties as a director (Figure 6.2).

¹ www.coag.gov.au

- **Time spent on compliance duties:** Seventy-nine percent of respondents said they are moderately or seriously concerned that the time their board invests in overlooking compliance is detracting from time which could be better spent focusing on enhancing organisational performance / productivity.
- **Harmonisation of OH&S:** More than 87 per cent of respondents said the harmonisation of OH&S legislation would positively impact their organisations.
- **Impact on consideration of directorship as a future career:** Seventy-four per cent of those who identified themselves in the survey as “aspiring directors” (when asked to nominate their primary role or interest in directorship) said the risk of personal liability had made them reconsider directorship as a career.

Qualitative commentary

The following quotes from qualitative commentary in the survey demonstrate a range of concerns regarding director liability. The various themes raised within these quotes are considered throughout this report.

When "derivative liability" is the default mode, then one is automatically in the situation of having to prove innocence (the reverse of the normal construct). It is both inappropriate and, I imagine, extremely difficult, costly and time consuming to achieve. It will doubtless lower the quality of directors serving public companies as many will opt out because the risk is too high and NOT within the directors' control. Companies will suffer from this loss of quality and experience.

"It [director liability] is an issue that affects all decision making, sometimes expressly and at other times sub-consciously."

"I think it is getting worse and will increase risk averse decisions & reduce availability of volunteer directors."

"In my case, I now sit on one board only, a small non profit. I do not need the hassle in my life. As an alternative, I sit on "advisory panels" of several SMEs where you can get something done, not as worried about the compliance is an issue, and liability is less likely to be an issue, as the organisations are smaller, family, and the culture & environment is far less adversarial."

"Personal liability for independent non-executive directors of limited liability companies who have not committed a criminal offence is anathema to the principle of a limited liability company and equity capital and its importance in the creation of wealth and enterprise. It is also anathema to the ancient golden thread woven throughout common law since the Magna Carta of being innocent until proved guilty and represents a disturbing trajectory towards authoritarian government exploiting populism. Finally it suggests a gross lack of understanding of the role of the independent non-executive director and the protection of shareholder rights relative to that of executive directors and management and seriously threatens the existence of the independent role and the very desirable differentiation between independent and executive directors and officers. This is not to suggest in any way that penalties for companies should not exist for breaches of the law or for individuals for criminal offences. The dead hand of the law however does have a demonstrable significant negative impact on the economic and social well-being of the nation."

Part 1: Background

The Australian Institute of Company Directors has long advocated for reform of legislation where we believe it hinders directors carrying out their duties.

Our objectives in advocating for such reform are to:

- better allow directors to act in the best interests of the companies they serve;
- support the capacity of directors and their organisations to influence job retention and creation; and
- reduce unnecessary compliance burdens or red-tape.

Of particular concern are provisions in legislation that impose automatic personal liability on directors for corporate fault – ‘derivative liability’ (i.e. directors can be found liable simply by virtue of their position, regardless of their actions).

We are also advocating for streamlined duties, offences and defences for directors (including for an expanded business judgement rule and greater ‘safe harbours’).

To gather quantitative evidence regarding our members’ concerns of in this area, we invited 600 directors of ASX 200 companies to participate in a Federal Treasury Survey in 2008. The results of this survey enabled us to quantify the impact (on ASX 200 directors) of personal liability on board recruitment, retention and decision-making.

The risks of personal liability and the burden of legislative compliance are applicable to all directors, however, not just those of large, publicly listed companies.

As the Australian Institute of Company Directors represents more than 27,000 current and emerging directors, we are committed to understanding the concerns of our individual members – right across the spectrum of organisation sizes and types – regarding the negative impact of legislation.

1.1 Methodology

This report has been prepared following analysis of the results of an online survey of our membership, through phone conversations with individual directors, as well as a review of our policy materials addressing these issues. It includes quotes received from the online survey.

Director Liability Survey

The Australian Institute of Company Directors expanded on questions asked in the 2008 Federal Treasury *Survey of Company Directors*, and invited members subscribed to our email distribution list to complete the survey. The survey was open from 29 March to 9 April 2010.



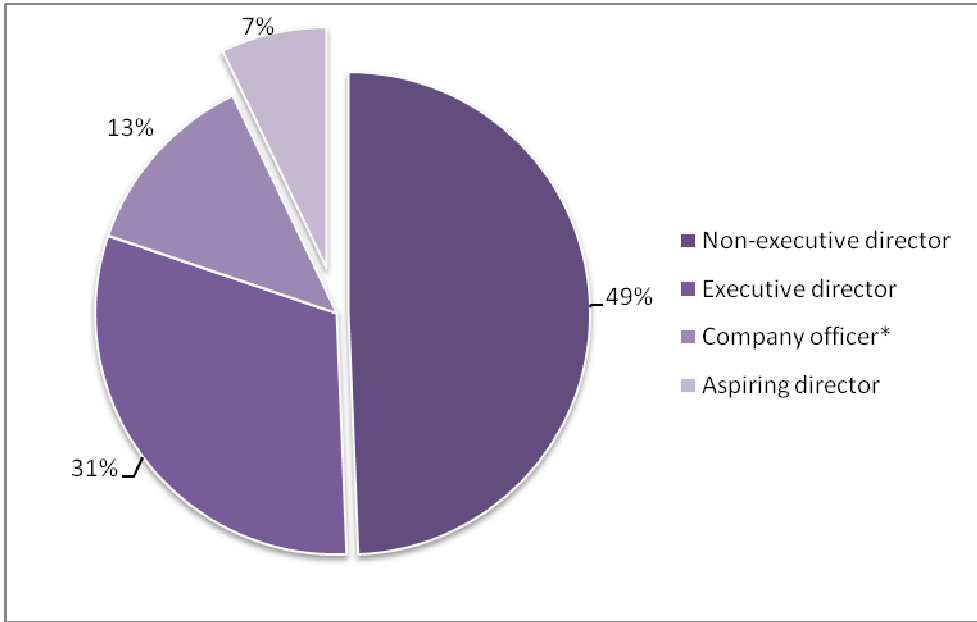
The survey was completed in its entirety by 623 members, a response rate of 10 per cent (of the number of members who opened the email containing the survey invite).

There were two different paths which respondents were taken on according to the selection of their primary role. Those who selected the option “Aspiring Director” instead of one of the director / officer roles, completed a fewer number of the total possible questions.

The majority of the figures cited throughout this report are based on the responses of the directors and officers (more than 90 per cent of the total sample size). Many questions invited directors to contribute comments to support their multiple choice response. These have been used and collated throughout the report according to similarity of themes raised.

The responses of those who identified their primary role, or interest in directorship as being that of a “non-executive director” have been analysed in isolation of other responses in some sections of this report – reflecting the very different nature of this role to that of an executive director or company officer. Nearly 50 per cent of the total sample was comprised of non-executive directors (see Figure 1.1).

Figure 1.1
Primary role or interest in directorship



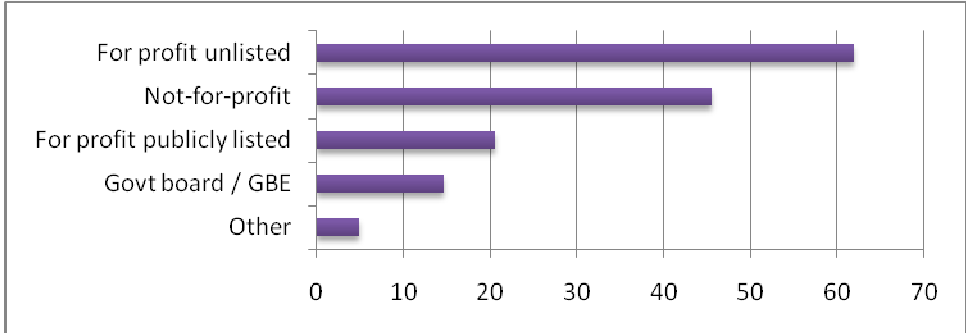
Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked to nominate their primary role or interest in directorship. N=693

Figure 1.2 shows the type of organisational structure(s) which respondents indicated that they were directors / officers of. Respondents were able to select from multiple categories, enabling them to show multiple directorships.

Sixty-two (62) per cent were directors / officers of for-profit unlisted companies, while more than 45 per cent had a role in not-for-profit organisations (NFPs).

Examples of organisation types given in the ‘other’ category include subsidiary boards and committees, co-operatives, superannuation trustee boards, credit unions and mutual organisations.

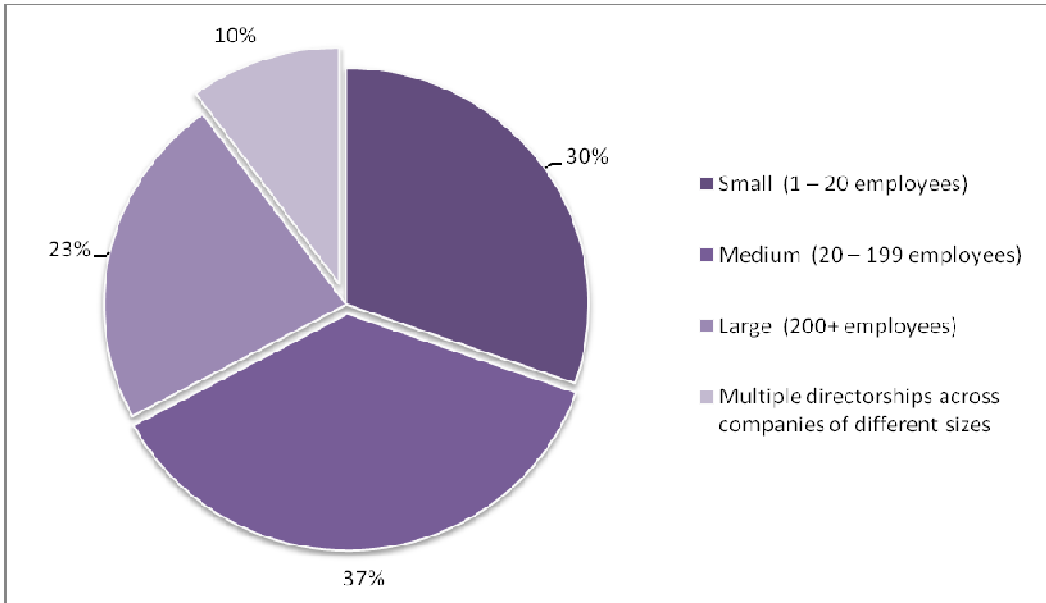
Figure 1.2
Organisation Type



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked to nominate the type of organisations they are currently a director of. More than one category could be selected. N=631 (director / officer responses only).

The size of the organisations represented ranged in similar portions from small (defined in this Survey as less than 20 employees) to large (more than 200 employees) – as shown in Figure 1.3. Directors / officers were also invited to select that they had multiple directorships across companies of different sizes (yet considered them of equal standing).

Figure 1.3
Organisation size

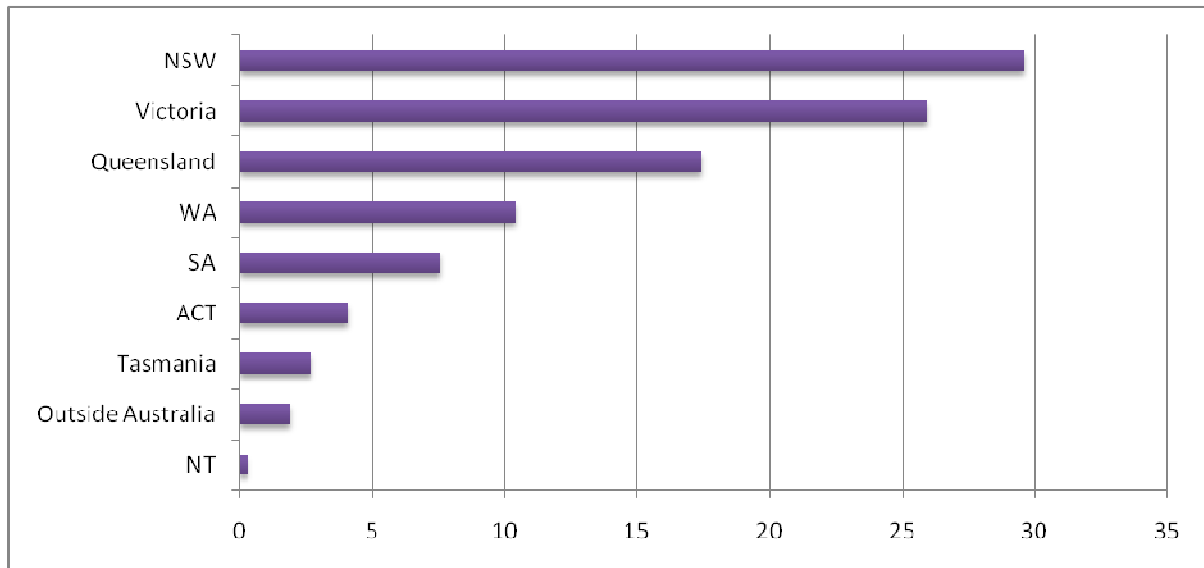


Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked to indicate the size of the organisation with which they have their primary role / directorship. N=634 (director / officer responses only)

While we have general concerns regarding the impact of legislation on directors working in organisations throughout the country, our Boardroom Burden Report Card, first released in September 2009, suggested that the impact can vary according to the jurisdiction(s) an organisation is based and operates in.

An analysis of some survey questions according to state is provided in this report.

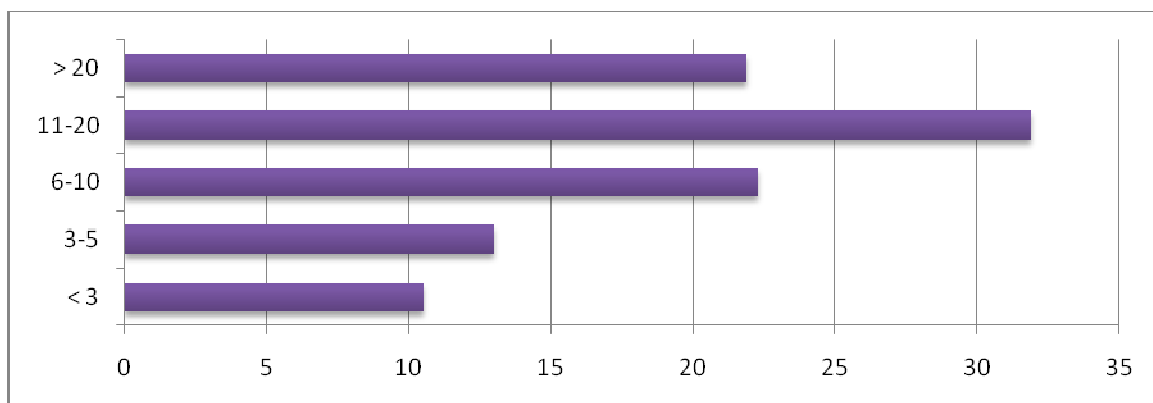
Figure 1.4
Organisation headquarters / registered



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked the state in which their primary organisation was headquartered / registered. N=632 (director / officer responses only)

The experience profile of directors / officers responding to the survey ranged from relatively new directors, to seasoned directors with more than 20 years of service (Figure 1.5). This range was reflected in number of boards that respondents held directorships with and/or reported to, as well as membership levels (grade) of respondents.

Figure 1.5
Years' experience as a director / officer

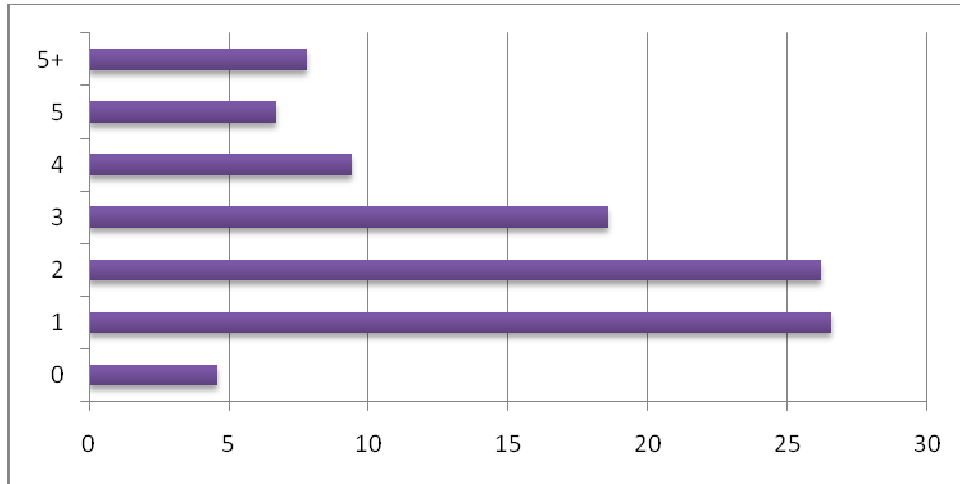


Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked how many years they had been a director or officer. N=631 (director / officer responses only)

More than 95 per cent of the respondents (directors / officers) held at least one directorship; while almost 69 per cent held more than one directorship (Figure 1.6).

More than 36 per cent of respondents were Fellows of the Australian Institute of Company Directors (post nominals of FAICD).

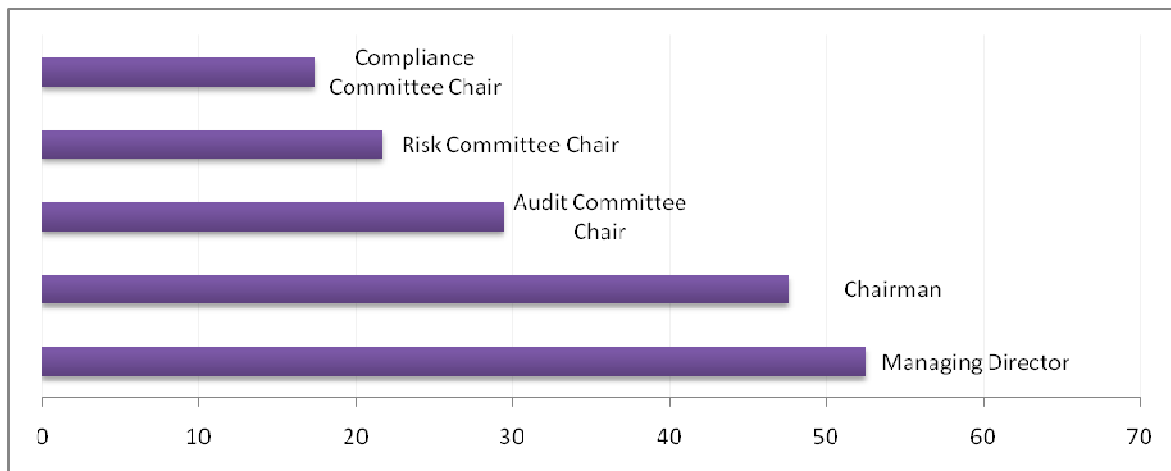
Figure 1.6
Number of directorships



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked how many boards they sit on. N=625 (director / officer responses only)

More than 80 per cent of respondents had held the position of a Chairman, Managing Director or Chairman on a board sub-committee (e.g. Audit Committee). Multiple roles were able to be selected.

Figure 1.7
Experience as a Managing Director or Chairman



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked which of the roles they had experience of. N=632 (director / officer responses only)

Part 2: Awareness of legislation imposing personal liability on directors

Overview

Most members of the Australian Institute of Company Directors have at the very least, a basic level awareness of legislation that imposes personal liability on directors. Many, of course, have detailed knowledge of the current legal environment for directors.

More than 82 per cent of respondents to the online survey stated they *were* aware of legislation that automatically imposes personal liability on directors for corporate breaches (i.e. derivative liability is where directors can be found liable simply by virtue of their position, regardless of their actions).

“I really don't feel I understand liability as well as I would like to. It appears to be quite a concern, and I'd like to know more”

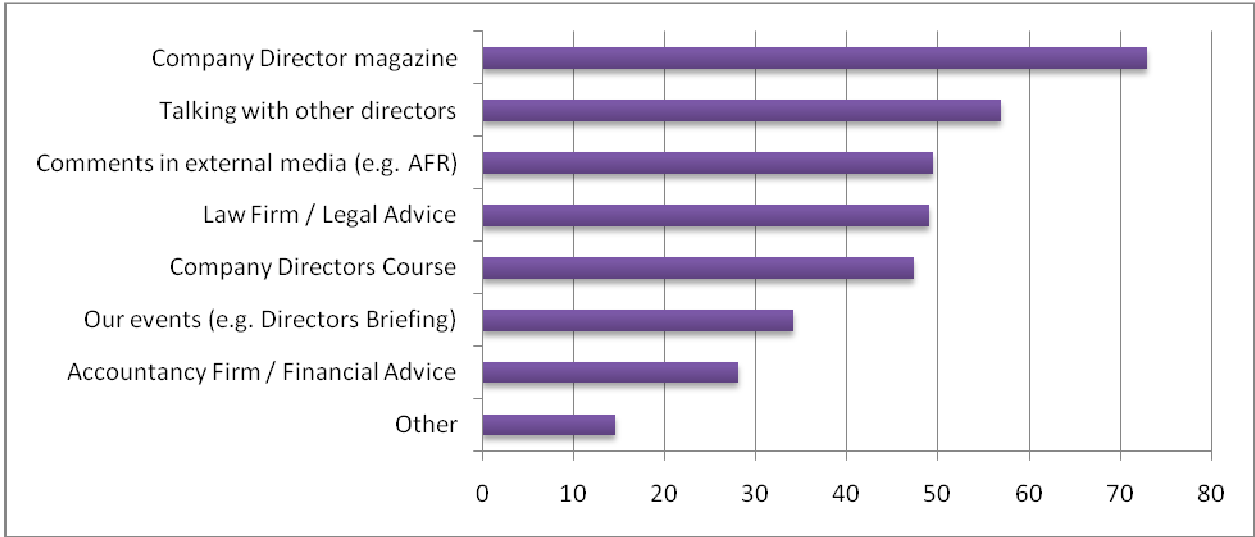
In response to a qualitative question to note any such areas of law known to impose derivative liability, the most common area highlighted was Occupational Health & Safety legislation. Other areas noted by many respondents to this question included environmental legislation, taxation and the insolvent trading provisions of the *Corporations Act 2001*.

Research previously published by the Australian Institute of Company Directors has shown that there are also more than 660 state laws imposing personal liability on directors.

More than half of respondents (56.9 per cent) had heard about personal liability from talking with other directors (Figure 2.1).

“The issues always need to be front of mind”

Figure 2.1
Sources of information on director liability



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked where they had heard about the personal liability of directors. N=506 (director / officer responses only)

The role of a director

Understanding the issue of personal liability for directors requires a good degree of understanding about the role of non-executive directors (i.e. what can be reasonably expected of someone within the position).

Many respondents highlighted stakeholder confusion or a lack of understanding about what a director actually does, as one potential reason for their personal liability concerns – that is, the extent to which non-executive directors are involved in day-to-day operations, or have the capacity to influence the actions of individual employees.

Negative stereotypes and perceptions of directors are also an issue. Directors who are focused on delivering outcomes for their stakeholders feel that some egregious legislation is designed to achieve greater accountability for the problems of the minority who contravene the law.

“Our community is confused about the role of a Director. If it is to guide, overview etc, then there needs to be appropriate protections where directors act responsibly but things go wrong. If the role is to be fully accountable then the time and remuneration arrangements are wrong. Independence also becomes a factor to consider.”

“I fear the regulators are having trouble distinguishing the roles of management from those of directors/owners' representatives.”

“The liability being "automatic" is a dramatic over-reaction to a small number of incidences. It drives up exec salaries to cover the liabilities - just like the medical professions. Government can't have it both ways - restrained executive remuneration but increased liability.”

“The risk profile of Directors requires review by way of reasonableness and clarity. Also risk/reward balance needs an adjustment.”

“The degree of risk is excessive in contrast to the immediate influence a director can have in this regard.”

“I believe this potential liability is disproportionate to the level of control and remuneration.”

“Derivative liability has the potential to be unreasonable in areas such as environmental and OHS laws where non executive directors have no direct involvement.”

“I am uncomfortable as a director with the level of exposure relating to issues that may, with the best intent, be extremely difficult for a director to influence or act on.”

“The Legal System, Media and politicians are remarkably uninformed on the role and capability of NEDs [non-executive directors], who under the Aussie concept are part time and generalist with no previous link to the company of which they are a director.”

“My sense is that the real nature and role of a Board has been relegated to the background in an effort to find a way to put blame on behalf of shareholders. The response is to satisfy the concern of those with a case against a minority of those in corporate governance roles.”

“Realistically Directors, individually, can only be 'in the clear' in a 'perfect' corporation'. The role is looking more like 'the fall guy' when someone has to be held accountable rather than the people who collectively diligently strive to direct the corporation.

“Very unfair social engineering based on hatred of corporations and those that run them.”

The concept of seeking “someone to blame” is also raised in Part 3.

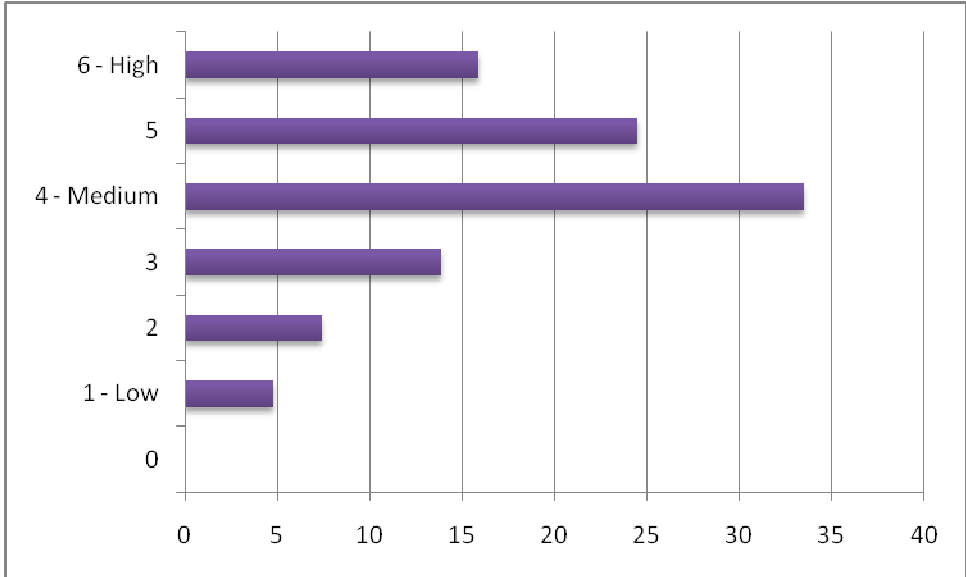
Part 3: Perceptions of personal risk exposure

Overview

More than 73 per cent of respondents believed there is a medium to high risk of directors being found personally liable for decisions they have made in good faith (Figure 3.1). This is only slightly under the finding of the 2008 Treasury *Survey of Company Directors* (78 per cent), suggesting that risk is not confined to large ASX-listed company directors alone. More than 71 per cent of those who currently hold a not-for-profit directorship also stated a medium-high risk.

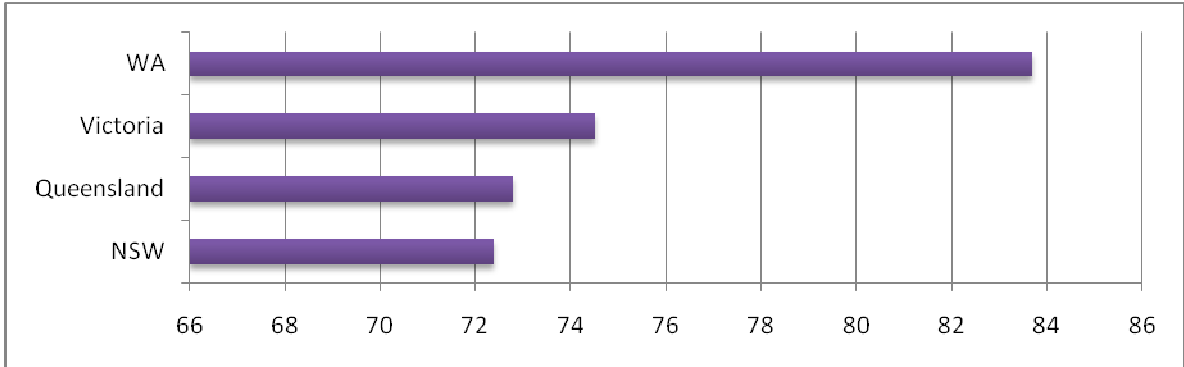
More than 83 per cent of respondents whose primary organisations were based / registered in WA responded there is a medium to high risk (Figure 3.2).

Figure 3.1
Degree of risk for decisions directors make in good faith



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked to rate the degree of risk that they considered applies to directors being found personally liable for decisions they have made (as a director or officer) in good faith (where 1 is low, 4 is medium and 6 is high). N=516 (director / officer responses only)

Figure 3.2
Medium - high risk for decisions directors make in good faith (State comparison)



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked to rate the degree of risk that they considered applies to directors being found personally liable for decisions they have made (as a director or officer) in good faith (where 1 is low, 4 is medium and 6 is high). The results were filtered based on respondents' selection of where their primary organisation was headquartered / registered (see figure 1.4). N=423 (director / officer responses from WA, Queensland, NSW and Victoria)

A complex issue

One respondent highlighted the complexity of rating the degree of risk felt in this question.

“There are at least three concepts to this question:

- 1. What is the risk of being prosecuted? Because of the lack of information as to the numbers of cases and the outcomes, I would believe many directors would believe the risk to be low.*
- 2. If a prosecution did take place, is the law perceived as loaded against the directors? I do consider this risk is high because the concept of safe harbour is not widely utilised. There appears to be in the legislators' minds a naive presumption of easily established facts, at the point of decisions, whereby the directors could determine the right or wrong course.*
- 3. As the laws stand what is the potential risk of liability? That is reflected in my answer.” [Respondent selected 5 from the scale above].*

Another respondent, who cited similar complexity, considered risk to be low on the basis of probabilities.

“It's about taking things seriously. Risk is a matter of probability of occurrence PLUS net effect or event PLUS risk of being caught. Overall that is a pretty long probability!”

Reasons given

For those who answered the question at face value, in addition to the reverse onus of proof, reasons given for the perceptions of risk exposure included:

- lack of available defences;
- the judgement of directors with the benefit of hindsight;
- the lack of influence directors have in the day-to-day running of organisations (compared to management);
- personal experience;
- unrealistic expectations of risk minimisation;
- directors can be joint and severally liable (directors can be bound by board decisions even if they oppose them individually); and
- low levels of awareness of potential liability .

“It seems unjust that if decisions were made in good faith following due diligence and all available information, personal liability shall arise. I can see that if decisions were made negligently that personal liability may be just.”

“Companies are a risk investment. Directors can make decisions in their best endeavours to generate future prosperity for shareholders. External influences and/or honest errors in judgement may make these decisions seem poor in HINDSIGHT. The ability to judge someone with the benefit of perfect hindsight is not appropriate in assessing judgemental decisions at the time.”

“Very hard to TICK ALL THE BOXES in the proper honest business judgment test where things go wrong and a scapegoat is sought.”

“Too high - It is wrong that a director who has made every effort to minimise risk yet is still liable.”

“Liability of directors is joint and several - which detracts somewhat from one's personal standards of diligence and good faith.”

“I think there is reason for concern for directors who are not fully aware of their personal liability when, with the best of intentions, join organisations e.g. Not For Profit organisations to assist them strategically and find themselves with significant legal consequences.”

“It is a concern because a NFP charity I was on invested badly Government funds and lost them in the GFC against my advice yet I potentially could have been liable for those funds when the Commonwealth demanded repayment and they could not be met.”

Depends on the circumstances

Many believe the risk depends on the particular company: its structure, size, the quality of the board and its governance / compliance practices, its visibility (i.e. public profile); the decision at hand or jurisdiction(s) in which it is based or operates.

For others, the risk is not a question of probabilities, but the negative outcomes should the risk eventuate. It was also noted that there is risk in “decisions not made” as well as “decisions made”, and one of the greatest risks is not “eliminating every risk which could impact the organisation.”

Comments relating to the impact of risk perceptions have been included throughout this report.

“The degree of risk relates predominately to the corporate governance practices of the organisation to which you are a director.”

“Depends on the size and nature of the organisation, the abilities and honesty of management and fellow directors.”

“I believe it is low-medium in a well governed company however can be high in companies with poor governance systems and awareness of directors responsibilities.”

“Recognising the risk of being called naive, I'm confident that in practical terms a court would look at the whole of relevant circumstances and take actual conduct into consideration when determining whether liability applies. I am confident that I'm 'doing my job properly'.”

“The degree of risk is dramatically reduced but not eliminated by well run boards and companies complying with the law and continual awareness and alertness by directors and snr management.”

“Understand having employees in NSW of particular concern.”

“My assessment is based on the scale and nature of the company of which I am currently a director. If that changed then my risk assessment would likely rise.”

“Incidence is low but impact both financial and reputational are extreme.”

“Numerically, most directors don't get into trouble. However the damage resulting from liability is very high.”

“Is a serious consideration when taking on a Directorship. Due Diligence will be critical.”

Appropriate risk

It should be noted that the current degree of accountability and risk is considered appropriate by some.

“The role cannot be risk free, and some risk exposure probably focuses the mind and weeds out some of the negligent.”

“Directors are liable for their actions of the company on which they sit as board members. I have no problem with the legislation as it stands. As you would also be aware that executive officers also carry some risk. The buck has to stop somewhere and it should stop with all the directors.”

“Directors have a responsibility to understand / influence the risk profile of companies they sit on the Board of. If they aren't comfortable with that risk profile, they should resign. If they are comfortable, then the risk should be low.”

“I think it is possible to manage this risk if directors take their responsibilities seriously.”

“We have organised ourselves around needing directors and somewhere for the buck to stop - so there should be some penalty at risk particularly to stop bad faith let alone criminal activity. Good arguable judgement in the light of evidence at the time - and resources reasonably available to obtain it - should be adequate defence.”

“The risk issue is exaggerated. Directors who are doing their job adequately (note - they don't even have to be doing it well) are not at risk.”

The reverse onus of proof

A fundamental legal and human rights principle is to be innocent until proven guilty. However, in some areas of legislation, there is a reverse onus of proof for directors. Directors can be found liable simply by virtue of their position, regardless of their actions.

This is considered to be one of the more egregious aspects regarding the personal liability of directors and was noted extensively in comments throughout the survey. Examples of these comments are given below.

It is also considered by some to have a negative impact on director recruitment and retention (see part 5).

“Liability with the burden of proof reversed is a huge disincentive to contribute commercially, a blight on our society”

“Seems a lot like guilty until proven innocent, with very few ways to prove your innocence.”

“In many ways, the onus of proof of innocence lies with the director.”

“It appears that position alone is enough to indict you. A clear defence would be a much better position.”

“Reversal of onus is especially problematic and contrary to the treatment given to general public.”

“In any other area of the law many, not just the civil libertarians would call it a breach of basic human rights, especially where the derivative liability involves the reversal of the normal onus of proof.”

“This is contrary to the basis of Australian Law (the dictum "innocent until proven guilty"). It is particularly pernicious in relation to insolvent trading.”

“Automatic liability when not involved in the offending actions is wrong. Defences must allow for the exercise of business judgement in the particular circumstances.”

“There is too much emphasis on finding someone to blame. Directors are guilty until proven innocent.”

“Presumption of guilt is totally against our legal principles. It is fine to investigate boards to see whether they have an appropriate system of control and review in such important areas, but to brand them personally for failures in the system is totally unfair.”

“Presumption of guilt under ohs is unconscionable and I know people who simply will not direct any boards with operations in NSW to avoid it.”

“Qld OH&S laws are not reasonable in the assumption of 'guilt' and the burden of proof of appropriate actions taken on directors and management. This automatic liability is unreasonable and changes should be made to allow for reasonable actions, evidence, to be provided before judgement is delivered.”

“Too many provisions impose strict liability; there should be a universal business judgement/ due care & attention defence.”

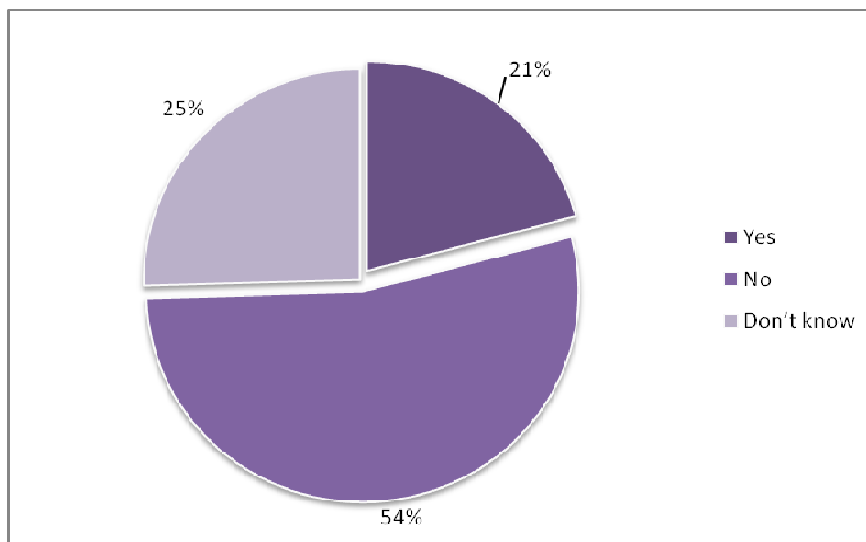
“Although there are defences, it is inappropriate that there should be a reverse onus of proof.”

Available defences

The *Corporations Act 2001* provides a business judgement rule defence under a limited number of sections. The Australian Institute of Company Directors has, on many occasions, called for a business judgement defence to be made available to other sections of the *Corporations Act*.

More than half of respondents to the survey (54 per cent) responded “No” when asked if reasonable defences exist for directors (Figure 3.3). 128 respondents offered comments on their response to this question. Examples are given below, as well as noted in other sections throughout this report.

Figure 3.3
Reasonable defences for directors?



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked whether they thought there are reasonable defences for directors under the *Corporations Act 2001* and derivative liability laws. N=501 (director / officer responses only)

“I agree with the expansion of the business judgement rule. There should be a distinction between deliberate or careless behaviour and acting as a reasonable person would in the particular circumstance.”

“There should be "safe harbour" legislation incorporated into ALL legislation which singles out directors. The only way to fix this now is to have a new act which creates "safe harbour" as a principal within all legislation (not only for directors).”

“The premise of your question suggests that derivative liability should be taken for granted; but my view is that defences should be irrelevant because derivative liability laws should be repealed. As a matter of principle a person should only be liable for harm to which he or she has personally contributed (by act or omission in dereliction of a duty).”

“I think acting in good faith, with reasonable care and diligence should be a defence. Negligent directors (especially where OH&S is concerned) belong in jail, unlucky ones don't.”

“Good faith and exercise of reasonable business judgment should be a defence. Prosecution should have onus of proving lack of these.”

“There may be reasonable defences but that does not mean that that is sufficient.”

“The defences are onerous placing an unreasonable / unbalanced demand on both the individual & the company.”

“Derivative liability is not acceptable. To show acted in good faith and with due diligence is too difficult to prove - the odds are stacked against directors.”

“I think that the law should allow for a "good faith" defence.”

“Although the defence of in good faith exists I am not comfortable with it being accepted by courts, especially in OH&S issues which can be very emotional.”

“The defences are too expensive to run and specialist tribunals do not accept them.”

While some state that effective compliance and risk management programs will provide a reasonable defence if required, there is some concern that defences are mistakenly viewed as reasonable, because of a lack of knowledge in this area. Some directors also expressed a lack of certainty regarding their knowledge in this area.

“As company secretary of an ASX listed company I observed that most directors were only vaguely aware of the deeper meaning or extent of the liability. Their common understanding was if I personally have done the right thing or it would be unreasonable to expect me to know, then that would be a sufficient defence.”

“Provided a director exercises reasonable diligence, the objective test applied by the courts will stand a director in good stead.”

“A director must enquire sufficiently to develop an informed view on issues. If that is done then generally he/she can feel protected. However when things go wrong people go searching for someone to blame and the Directors (who are part time at best) are prime targets.”

“My basic understanding is that we as Directors are responsible for our actions and decisions, so acting in accordance with our fiduciary duties and in good faith is a great start, but not too sure of detailed consequences post that.”

“Don't know enough about the "good faith" "defence" to know whether it offers "reasonable" protection.”

“Unsure whether there have been any "test" cases or precedents set yet.”

“I'm not a lawyer.”

“I would like a complete list (probably by Commonwealth and State) of the laws which do impact directors like this, what that impact is and what the legal expectations of a director

are in those situations. At least then I can know what I'm exposed to. Then I would like to be able to say that if I acted honestly etc., etc., then I have no criminal liability (even no civil liability). As a director who is neither an accountant or lawyer by profession I find it unacceptably difficult."

"It's a balancing act ... it's not that hard to develop a defence. Pendulum has probably swung a little too far, but OHS is moving back. Nothing makes you focus like personal liability!"

Other respondents commented that this is an evolving area, and one which can change according to Government reforms and interpretation of the existing law. It was also noted that the answer to this question could change according to the particular situation and circumstances.

"Up until very recently very little fall back and a lot of money could be spent defending a no-win situation. Recent court rulings may support directors' defence, although it is too early to see if the rulings stand thoughtful challenges."

"Lack of clarity around the extent of the business judgement rule and ongoing discussions about expanding the scope of application places the risk [of personal liability for decisions made in good faith] relatively high at present."

"Not sure - on the face of it there is but may be untested."

"We have seen instances where Directors acting in good faith have been penalised, and others where demonstrably liable Directors have escaped penalty - there is an imbalance and inequity in the current interpretation of the statute."

"Attracted by the more pragmatic approach to directors liability in relation to insolvency as currently being canvassed by Deputy Treasurer."

"Derivative liability is pernicious and an excellent example of Parliaments' capacity to make bad law."

"My answer is because I have no confidence that the present Government would not introduce further restrictive legislation."

Occupational Health & Safety (OH&S)

As mentioned above, Occupational Health & Safety was identified in the survey as one of the primary areas of concern in terms of personal risk exposure and availability of reasonable defences.

"Whilst I have a strong commitment to OH&S, it seems almost Catch 22 at the present when directors who have manifestly done everything right are still held liable."

"Although heartened by a higher court decision over-ruling a lower court, I am very concerned to read of the ridiculous charges laid against reasonable directors by over-zealous OHS regulators."

"Believe OH&S in particular to be totally unreasonable."

"Good faith does not protect directors in OHS situations."

"In regards the Corporation Act the defences are reasonable, but in regard to NSW OH&S this is certainly not the case."

"Particularly in OH&S liability (and particularly in NSW) the burden of proof lying with prosecuted party does not fit with other forms of legal proceedings."

"The best defence is to show that the directors have asked appropriate questions of the executive and the answers have been properly considered but even with the best intentions and safety practices accidents do happen."

“OHS laws are draconian - you can have the best safety systems in place and an excellent track record, but it only takes one idiot doing something stupid and you can be found liable.”

“The risk is high and there appears no reasonable defence because for example for serious OH&S workplace incidents in NSW:

- (i) guilt is assumed*
- (ii) hearings and appeals are held in a court that was established for the protection of workers’ rights*
- (iii) unions are able to launch actions and receive financial benefit from successful prosecutions*
- (iv) insurers covering directors and officers have a financial incentive to settle at the earliest opportunity given assumed guilt and the utterly overwhelming lack of actual successful defences*
- (v) the extremely difficult task for independent non-executive directors (and therefore high risk) to control all employees attitudes and behaviours all of the time coupled with the nature of natural systems including human beings to move to the lowest energy state thereby increasing the risk of people taking shortcuts leading to injury*
- (vi) the strong resistance of unions and employees to disciplinary action and strict accountability of front-line employees in relation to safety.*

Derivative liability for independent non executive directors should be eliminated and broad based safe harbour legislation should be introduced while maintaining significant penalties for companies which fail to protect workers safety.”

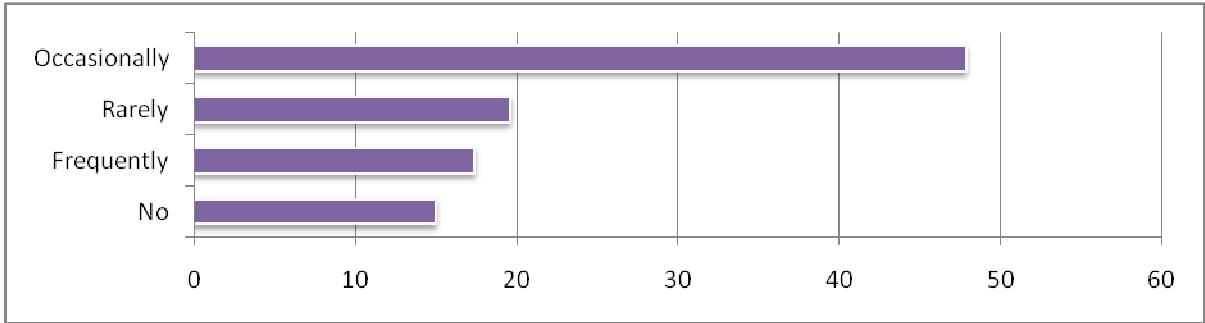
There is further discussion of OH&S in Part 4 – the impact of OH&S of legislation on decision-making.

Part 4: Impact of legislation on business decision-making

Sixty-five per cent of respondents said felt the risk of personal liability had caused them or a board on which they sit to take an overly cautious approach to business decision-making frequently or occasionally (Figure 4.1).

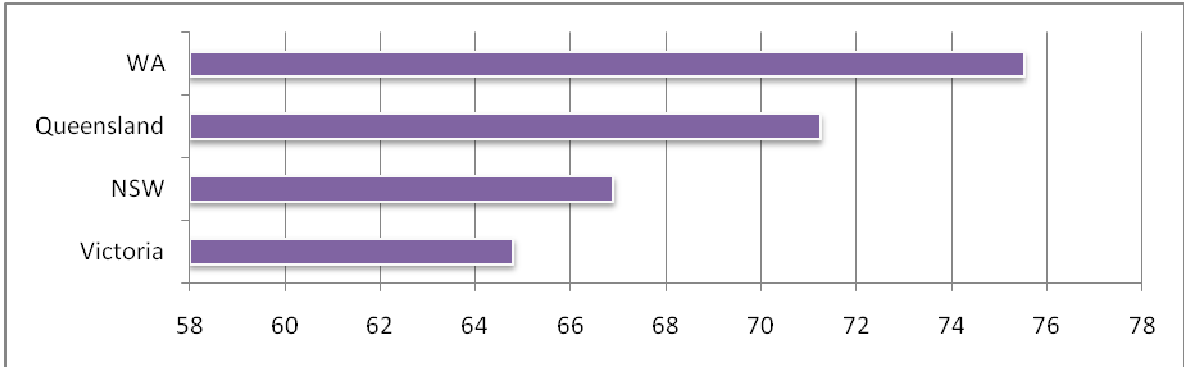
The percentage of respondents whose primary organisations were based / registered in Queensland and WA both rated above this (Figure 4.2), showing a potential correlation between decision-making and the provisions in state-based legislation.

Figure 4.1
Taking an overly cautious approach to decision-making



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked whether the risk of personal liability (under any law) had caused them or a board on which they sit to take an overly cautious approach to business decision-making. N=499 (director / officer responses only)

Figure 4.2
Taking an overly cautious approach to decision-making occasionally or frequently (State comparison)



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked whether the risk of personal liability (under any law) had caused them or a board on which they sit to take an overly cautious approach to business decision-making.

The results were filtered based on respondents' selection of where their primary organisation was headquartered / registered (see figure 1.4). N=419 (director / officer responses from WA, Queensland, NSW and Victoria)

Legislation and litigation that impacts decisions

Respondents were also asked to identify the laws which had caused such an overly cautious approach.

Occupational Health & Safety was the most frequently identified individual area in qualitative commentary, along with the potential for litigation and criminal liability in some cases.

“OHS in particular, however the overall community approach to attempt to track responsibility through to the owner's representatives, regardless of their involvement - is of general concern - as it skews the interpretation of the legislation in the courts.”

“Particularly the OH&S laws. The board was forced to implement changes that would have otherwise been made in a more timely and informed manner. Hasty decisions to prevent a risk perceived or otherwise is not good business practise.”

“OH&S issues where it's almost impossible to sack someone who refuses to obey safety rules yet we can be prosecuted if he is injured.”

“It is the litigious nature of the Australian commercial landscape rather than specific laws that are the key cause of concern.”

“There are two issues; litigation funders and class action initiators are a cause of concern and, and third parties are increasingly playing the blame game. With the publicity of possible "liability" being canvassed in the press, the incidence of litigation is in my view bound to increase and certainly to be given active consideration by those parties.”

“No specific law - just a general concern that there would be some exposure through litigation.”

“Every decision has to be weighed against possible liability (as well as good governance) and we therefore decide conservatively.”

“Corps Law and threat of class action. It was the potential threat rather than the law itself.”

“Liability for life.”

“Ones which impose personal criminal liability on directors.”

Insolvent trading is another major area of concern.

“The danger of insolvent trading when trying to turn (and preserve value in) around a company that is in difficulties.”

“Directors may act in good faith to continue trading to turn the company around but could find themselves liable if their plans are not successful.”

“OH&S; insolvent trading - may be instances where directors will take the low risk approach rather than looking at what may be in better interests of shareholders - can be hard to make judgement; case law on Advance Bank case.”

“I am particularly concerned about insolvency liability. I believe the pendulum has clearly swung too far to protection of creditors such that, even if I strongly and defensibly believed a company could trade out of insolvency, I would nonetheless be obliged to recommend that a company be wound up as soon as I believed it was technically (but temporarily) insolvent. The fact is that I simply could not personally carry the company's liability. I am well aware that this breaches a fiduciary duty to shareholders since, in my hypothetical, this company could trade out of insolvency.”

Other individual laws / regulations referenced in response to this question included:

- ASX Listing Rules, including continuous disclosure
- Industrial relations, including termination of under-performing employees, bullying
- Discrimination
- Financial Reporting Standards, and the requirement in the *Corporations Act* to present accounts on a true and fair basis
- Environmental
- Taxation
- Privacy
- Trade Practices Act / Competition
- Public health
- Financial Services legislation and the issuing of product disclosure statements

It should be noted that some directors saw benefit in laws encouraging directors to be cautious in their decision-making.

“OHS, but if ‘overly cautious’ means saving lives, it’s probably worth it.”

State Legislation

Specific state laws were also referenced as influencing business decisions.

“Workplace safety ... removed all manufacturing from NSW.”

“OH&S. We have chosen to restrict the work we do to certain states and to certain activities in relation to the risk that OH&S in the mining industry brings.”

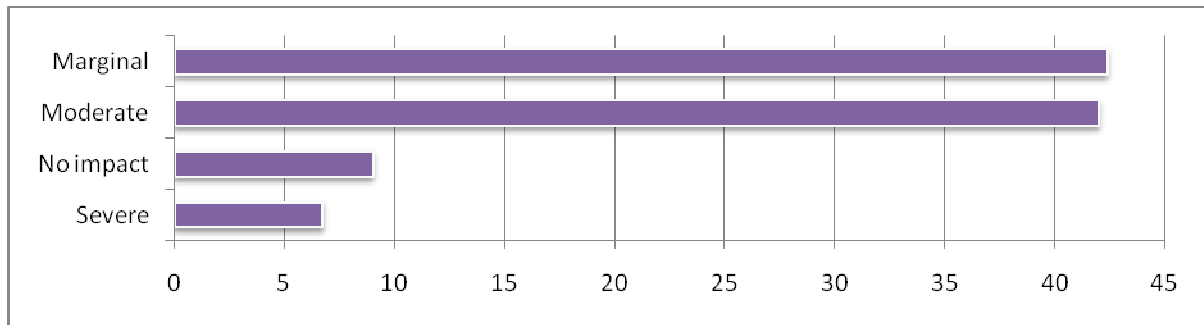
“NSW Occupational Health and Safety Law. Our company has field operations in that state.”

“Environmental laws in NSW - when constructing a new plant we spent what turned out to be excessive amounts in sound proofing due to the possibility of neighbours raising noise issues we felt were unfounded.”

Impact on optimal business decision-making or outcomes

More than 90 per cent of respondents said that the personal liability of directors has an impact on optimal business decision-making or outcomes (ranging from marginal – 42.4 per cent to severe – 6.7 per cent).

Figure 4.3
Severity of impact on businesses



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked what impact personal liability had on optimal business decision-making or outcomes. N=491 (director / officer responses only)

There was a wide range of issues raised (unprompted) in terms of how and why personal liability impacts optimal business decisions and outcomes, including, but not limited to the following:

How / Why

- Increases the time required to make decisions (as more information is required to form a decision; causes confusion);
- A focus on compliance and tactics at the expense of strategy, performance and in turn, shareholder interest;
- Negatively impacts job creation and investment in Australian / state businesses;
- Causes less optimal decisions to be made / limitation of entrepreneurial spirit;
- Increases costs and reduced revenue; insurance and legal fees were highlighted as a specific line items where cost is an issue / increasing;
- Reduces board diversity; and
- Understanding of how courts rule.

“Personal Liability compromises their [non-executive directors] ability to make informed ‘un-bias[ed]’ business decisions with calculated risk assessment. The Personal Liability risk is a major consideration and can impair judgement on what should be un-bias[ed], calculated risk decisions on behalf of Shareholders.”

“The presumption of guilt / intense scrutiny has lead to a level of documentation which itself makes it very difficult to absorb the total project plan and controls. Volume may protect in a court, but it confuses and can lead to uncertainty as the wood gets lost for the trees. It adds cost and time and therefore impacts return.”

“When the default mode is derivate liability, this drives decisions which may not be pragmatic or optimal but will be “safe” from an avoidance of liability perspective - FORM over SUBSTANCE.”

“This liability [derivative liability for decisions made in good faith] reduces inputs of directors to venture outside of the “status quo” environment in their companies and this is bad.”

“In my view the moves towards strict liability for actions that are in a director's influence but not direct control are continuing to push boards into an ineffective compliance-focused institution that does not maximise the benefit of a business for its primary stakeholders.”

“Costs have been higher due to a perhaps overly cautious approach.”

“Major investment decisions have been substantially extended by a number of years and numerous actions to reduce or transfer risk have greatly increased costs and reduced revenue.”

“It has made decision making a protracted process with a number of Directors unwilling to commit to courses of action without significant (and in my view unwarranted) investigations and voluminous reporting from management. It has resulted in the opening position being that of doing nothing and retaining the status quo is a 'safe' option and will not (erroneously) lead to personal liability.”

“We have had lawyers make a full review of all contracts which would not otherwise have been necessary and held back from an investment that may well have been successful.”

“Derivative liability laws are a competitive disadvantage which, when taken together with other Australian competitive disadvantages (e.g. multiple complex tax laws and, under the current Commonwealth Government, increasingly benighted labour laws, skew investment decisions against Australia (e.g. vis-a-vis Asia).”

“Has also caused us to not bid for work, especially in NSW.”

“The governments say that they want jobs created then they do everything within their power to stop it happening.”

“In many ways it is best to design work to eliminate people due to the added liabilities created e.g. Workers Compensation.”

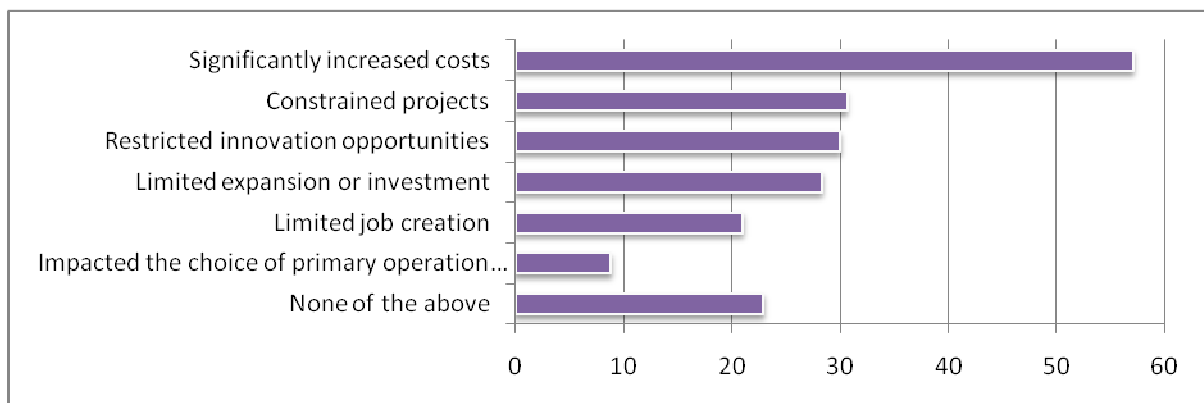
“It restricts the availability of directors. Risk-taking directors then dominate boards which seek diverse representation. It means we do not invite non-owner directors as board members. It means we do not offer ourselves to sit on other boards as the view is that the majority of board members are predominantly risk-takers. We have no wish to be a minority voice on this type of board. It reduces the diversity of boards.”

“Makes expanding the gene pool of directors difficult.”

“Courts are notoriously variable in how they rule and you tend to feel that commonsense will be lost and so you make much more conservative decisions than perhaps is needed.”

Survey respondents were also asked specifically about some of these areas mentioned above (Figure 4.4). More than 57 per cent of respondents cited personal liability had “significantly increased costs (e.g. compliance, project costs)”.

Figure 4.4
Impact on business outcomes



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked how personal liability had impacted business outcomes. N=480 (director / officer responses only)

Responsibility to the company and shareholders

Some respondents highlighted that a degree of personal accountability can result in better decision-making and/or positive business outcomes.

Other directors said that they accept the risks of personal liability as they are and do not let it impact their judgement or businesses as they discharge their duties in the best interests of the company (and shareholders) as is required by law.

It was questioned however, whether imposing personal liability on directors (to the current degree) was the best or most appropriate means or mechanism to achieve the desired outcome of *appropriate* levels of cautious decision-making (i.e. not reckless).

“If anything the issue of personal liability provides for directors to reflect carefully on their decisions and this is not bad thing to do. After all directors are responsible to their shareholders and while this sometimes slows down the decision making process it does often allow for due process to go full course and be substantially tested.”

“To some extent the caution which is encouraged might well be prudent. It is a pity however that this is being achieved through a 'big stick' approach by personally creating implied threats to directors acting to the best of their ability and intent within their boundaries of available information.”

“I believe 'personal liability' risk only creates a conflict of interest for Directors. The Directors consider their own personal circumstance and risk above that of the Shareholders.”

“Any impact is potentially dysfunctional to the decision-making process where the director's primary role is to the shareholders and other stakeholders where the personal liability consideration should not be a factor.”

“The effect is more to slow pace; directors should not allow personal liability risk to deflect them from the proper course of action in the interests of the company; they should manage the risk, not merely avoid the risky course.”

“If we acted to eliminate all the risks, the impact would be severe.”

“Have still taken the right decision for the business regardless of the personal liability risk.”

“Personal liability is a good thing to a point in keeping companies honest. When the law is unreasonable and onerous then it becomes counterproductive; e.g. strict liability regardless of fault.”

“Ultimately I think directors do what is right for the business and just hope unfair laws don't bring them down.”

“I have been part of board discussions on this issue, mostly to identify possible outcomes of decisions and the impact on the board members, but have not changed our decisions.”

“Personal liability is, I like to think, only a small factor in the decision making. The prime motivator is 'what is in the best interests of the company' in the current circumstances.”

“Although the personal risk is well known to all my board colleagues it is not a key factor in our decision-making. We are more concerned with doing the right things in the right way than with avoiding personal liability for our actions. Hopefully doing the right thing in the right way should be a defence.”

“Timeliness to make a decision but this has only impacted sentiment and not opportunities.”

“But in a good way - encouraging the board to take matters seriously.”

“I think the risk and the impact are over-stated.”

“All of these impacts [Figure 4.4] are couched in negative terms. Another impact might be to make directors more conscious of the effects of their decisions.”

“... I feel this is a leading question as all the possible options have not been canvassed ...”

“If there are no consequences for decisions then directors can become careless. Many are already ...”

Impact on the broader economy

Just under half of respondents who cited a negative impact of liability on decision-making or business outcomes said this has in turn inhibited their organisation’s ability to contribute to the broader economy.

In qualitative commentary on this issue, some found it difficult to determine the flow-on effects, and while others admitted they had answered “no” in this case, there was potential for an impact in the future. The negative impact on jobs and investment in Australian companies was again raised.

There was the most marked difference in responses to this question from those whose primary organisations were based / registered in Western Australian – more than 59 per cent said that the impact of personal liability had inhibited their organisation’s contribution to the broader economy (Figure 4.6).

“To some degree at this stage but much greater potential in the future”

“The opportunity for conservative businesses with a lesser risk appetite to grow through partnerships and acquisitions is reduced. This in turn expands the overall ratio of higher risk businesses within the economy. This greater representation of risk-taking businesses fuels public perceptions that businesses are poor ‘corporate citizens’ which in turn skews the interpretation of legislation and the extent that attempts are made via the legislation to ‘punish’ directors. This becomes a ‘virtuous circle’ of self-fulfilling outcomes. To impact the broader economy, a significant intervention is required.”

“Not really. It may have stopped us operating in some areas however there is no guarantee that we would be successful anyway.

“It should not if directors have done the correct thing and are compliant.”

“Any sub-optimal decisions that result from avoidance of potential derivative liability as its driving criteria will certainly limit the organisations contribution to the broader economy.”

“[Yes] Particularly with respect to employing people in NSW.”

“We operate in the area of employment of apprentices. The cost of compliance has caused us to restrict recruitment.”

“A stupid law [derivative liability] constraining business and does nothing to assist in the employment of Australians.”

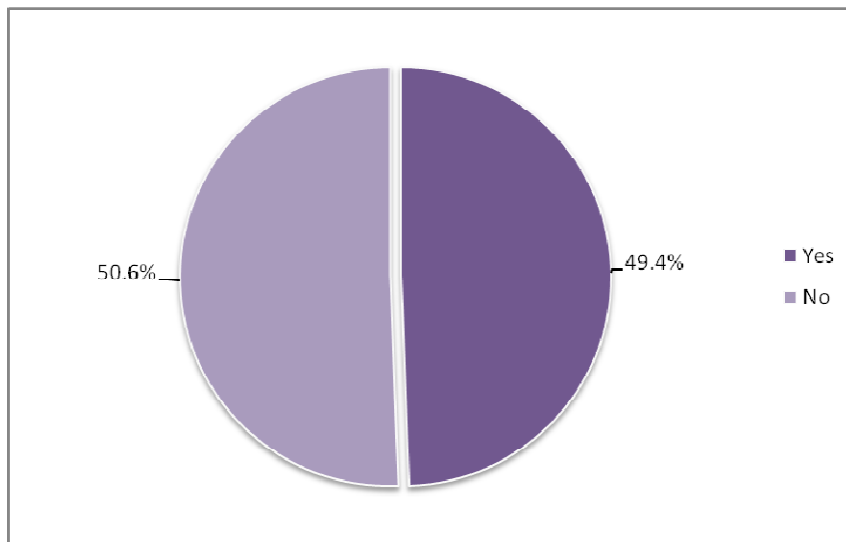
“It is just one of multiple factors which, taken together, result in choosing to invest off-shore rather than in Australia. In my personal experience this is most obvious in manufacturing.”

“Certainly companies are spending resources in this area which are being diverted away from normal business operations.”

“[No] But it has created a fearful, bullying and insecure business environment.”

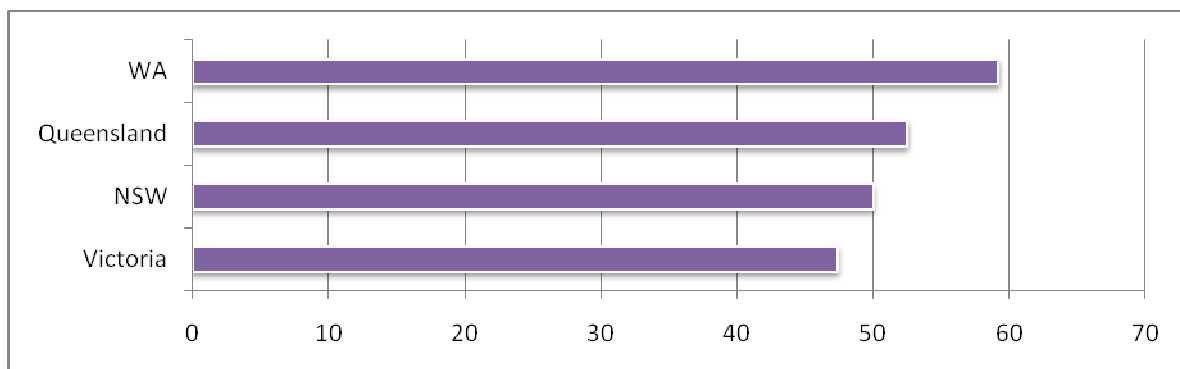
“Most of the company's I'm involved with are "too early stage" for their businesses to have a contribution to the broader community at this stage.”

Figure 4.5
Impact on organisation’s ability to contribute to the economy



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked whether this in turn (the impact of personal liability on optimal business decision-making or outcomes) had inhibited their organisation’s ability to contribute to the broader economy. N=482 (director / offices responses only).

Figure 4.6
Impact on organisation’s ability to contribute to the economy – “Yes” (State comparison)



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked whether this in turn (the impact of personal liability on optimal business decision-making or outcomes) had inhibited their organisation’s ability to contribute to the broader economy.

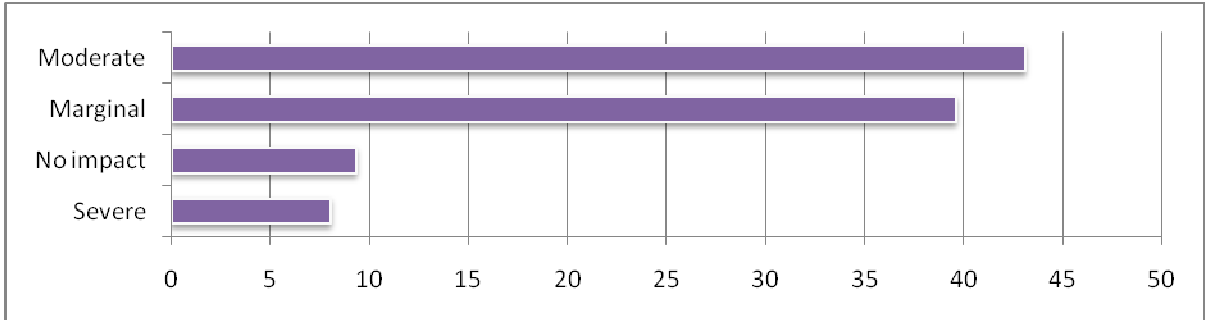
The results were filtered based on respondents’ selection of where their primary organisation was headquartered / registered (see figure 1.4). N=402 (director / officer responses from WA, Queensland, NSW and Victoria)

Impact on those who hold a Not-for-Profit directorship

More than 90 per cent of respondents who hold a not-for-profit directorship said that the personal liability of directors has an impact on optimal business decision-making or outcomes (Figure 4.5).

“As a not-for-profit director we have made decisions NOT to be involved with some marginal groups because the legislated liabilities are too high. For example: If an organisation works with people under the age of 18 there is no ability for liability to be waived or reduced (even by custodians) for incidents caused as a result of the behaviour of the minor. In essence, if a 17 year old takes a risk, that harms himself or another, the organisation is liable for his behaviour - without waiver. Who'd work with a 17 year old?”

Figure 4.7
Severity of impact according to those who hold an NFP directorship



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked what impact personal liability had on optimal business decision-making or outcomes.

The results were filtered based on respondents' selection of what type of organisations they have a directorship of (see figure 1.2). N=225 (director / officer responses, with one or more directorships in a not-for-profit organisation)

Part 5: Impact of legislation on director recruitment and retention

Director Recruitment and Retention

More than 32 per cent of respondents had declined the offer of a company directorship primarily because of the risk of personal liability (Figure 5.1). In addition, more than 22 per cent had resigned from a directorship primarily because of the risk of personal liability (Figure 5.2).

In contrast, 56.8 per cent of respondents knew of other directors who had declined the offer of a directorship (Figure 5.3), and 52.2 per cent knew of others who had resigned from a directorship primarily because of the risk of personal liability (Figure 5.4).

“I have been a director of some 30 companies including 5 public companies. Because of the legislation and what happened to colleagues I have resigned all directorships except my family company and have refused any offers.”

“Up until this stage the impact [of liability on decision making] has been negligible however going forward the consideration given to personal liability will become an overriding factor in determining my position on a Board.”

“I perceive the risks in Australia now as so high that I have been reducing my directorships and will soon have withdrawn from the final two. It's simply not worth being a director.”

“It's a wonder anyone sits on boards nowadays.”

“The increasing complexity and inherent risks for Directors "acting in good faith" will eventually drive experienced people away from taking on director roles if major prosecutions under these acts occurs.”

“Relying on backing myself to be sensible and argue so [minimise risks of personal liability] but the world is full of hidden risks frankly debatable whether risk is worth the return - modest cash or joy of public service.”

“This [the risk of personal liability for decisions made in good faith] is much too high. I have turned down directorships where I am sure my experience and integrity would be of value to the business and 'society' - but it is simply not worth the risk.”

“This [the risk of personal liability for decisions made in good faith] reduces my interest in directorships and means I do not seek directorships in companies at risk in any way.”

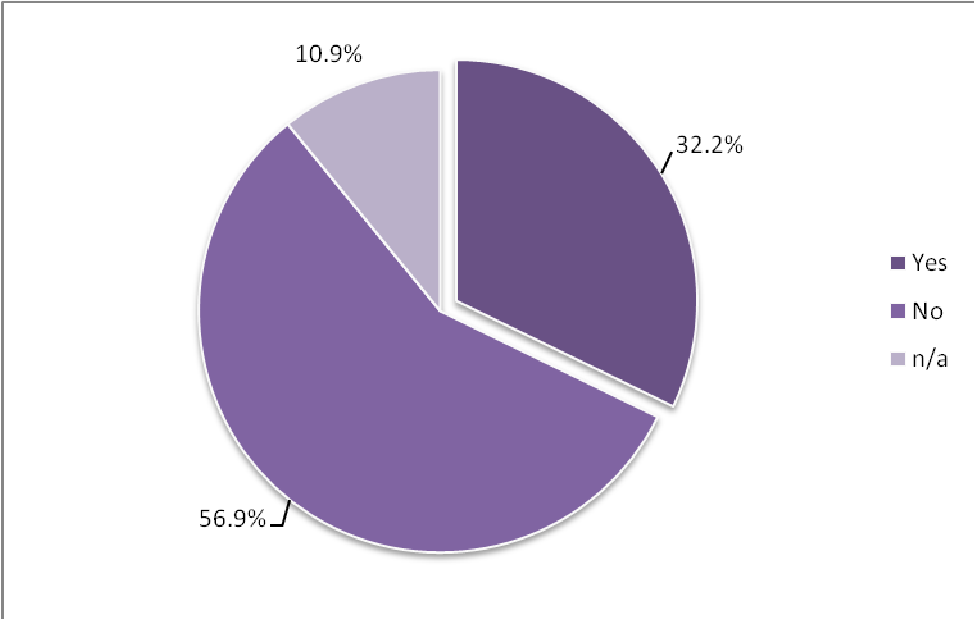
“I refuse to seek directorships outside of my personal businesses for this reason [lack of available defences].”

“A leading executive search CEO told me I would a fool to accept NED positions.”

“The impact [of personal liability] that I've seen is that experienced business folk are unwilling to take on the Non Exec Director risk.”

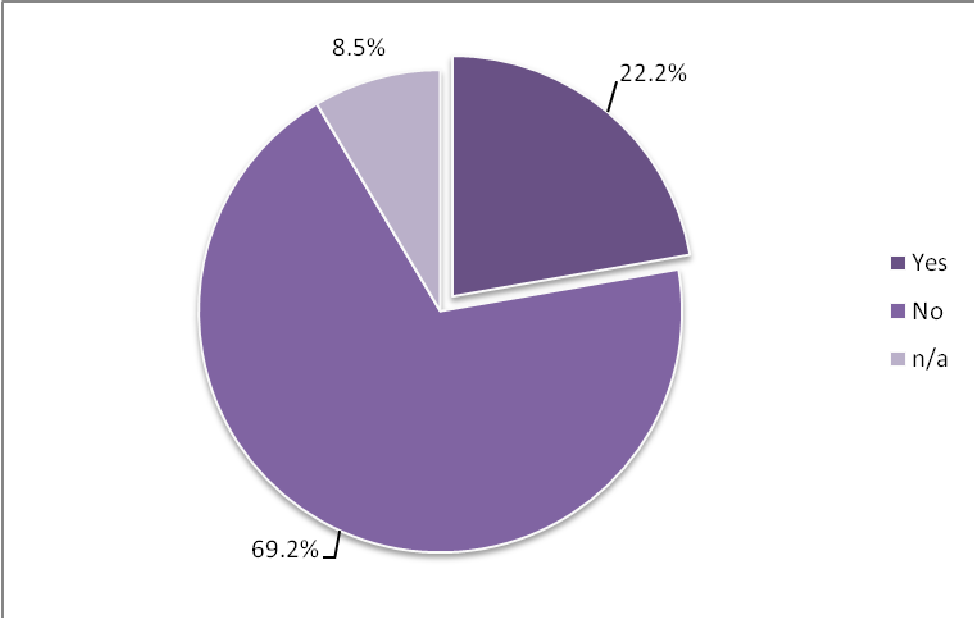
“The lack of definitive knowledge wrt [with regards to] the laws which can actually affect me in Victoria and that impact causes great concern and is leading me to consider non-director roles, e.g., advisory boards, steering committees etc.”

Figure 5.1
Declined the offer of a company directorship



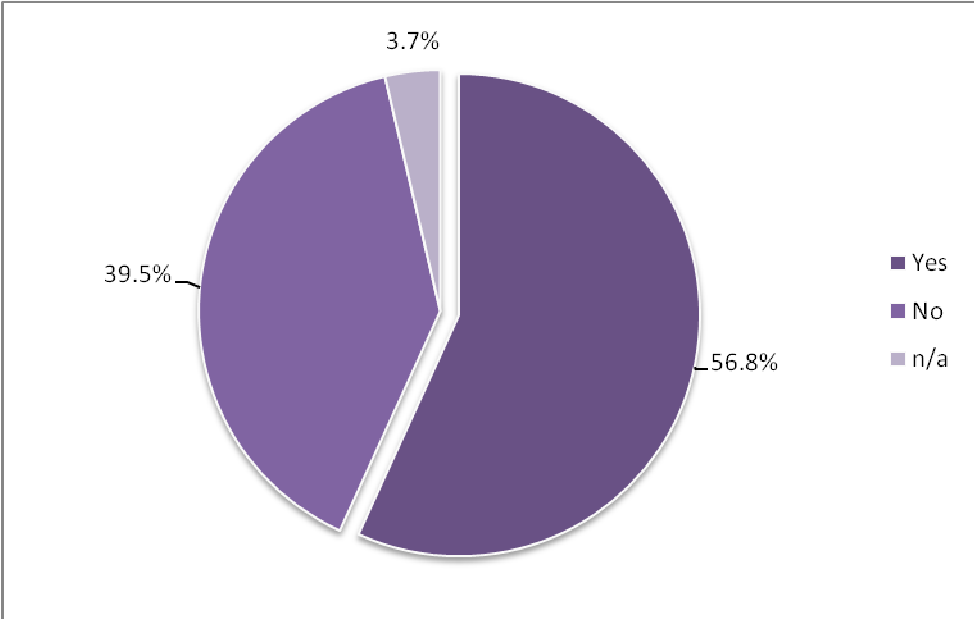
Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked whether they had declined the offer of a company directorship primarily due to the risk of liability. N=486 (director / offices responses only).

Figure 5.2
Resigned a company directorship



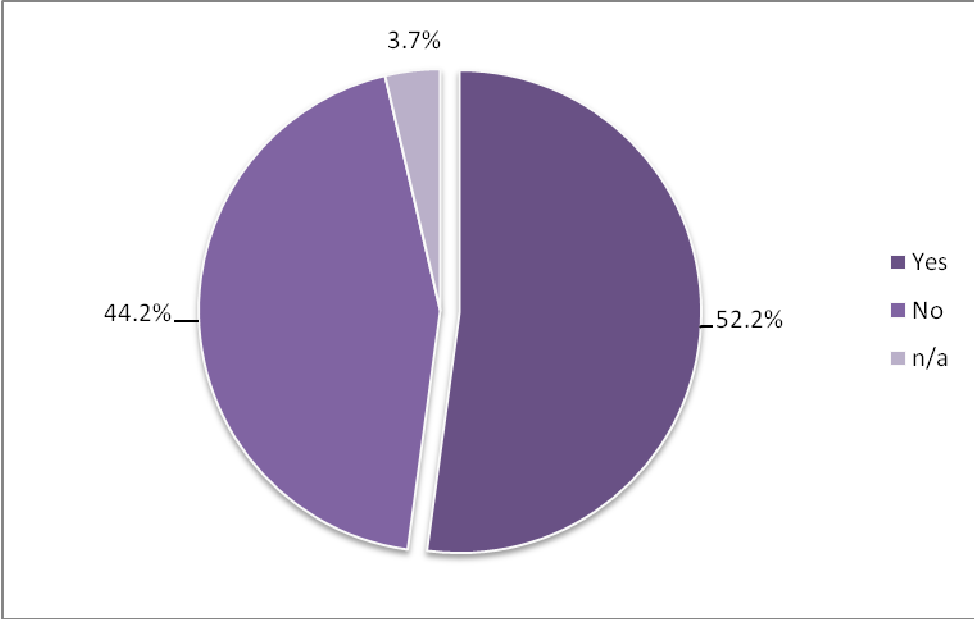
Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked whether they had resigned from a company directorship primarily due to the risk of liability. N=486 (director / offices responses only).

Figure 5.3
Know of others who have declined a directorship



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked whether they knew of other people who had declined the offer of a company directorship primarily due to the risk of liability. N=473 (director / offices responses only).

Figure 5.4
Know of others who have resigned from a directorship



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked whether they knew of other people who had resigned from a company directorship primarily due to the risk of liability. N=473 (director / offices responses only).

Impact on director recruitment and retention in the Not-for-Profit sector

Of those who currently hold a not-for-profit directorship:

- More than 34 per cent of respondents had declined the offer of a company directorship primarily because of the risk of personal liability; and
- More than 26 per cent had resigned from a directorship primarily because of the risk of personal liability.

The concern for the not-for-profit sector was also highlighted in commentary throughout the survey. The risk is considered greater by some in not-for-profit organisations because of limited financial resources to manage compliance requirements.

“Limits people wanting to be directors, as the risk is perceived to be too great, especially in Not for Profit organisations.”

“Very hard to obtain people on Charity Boards.”

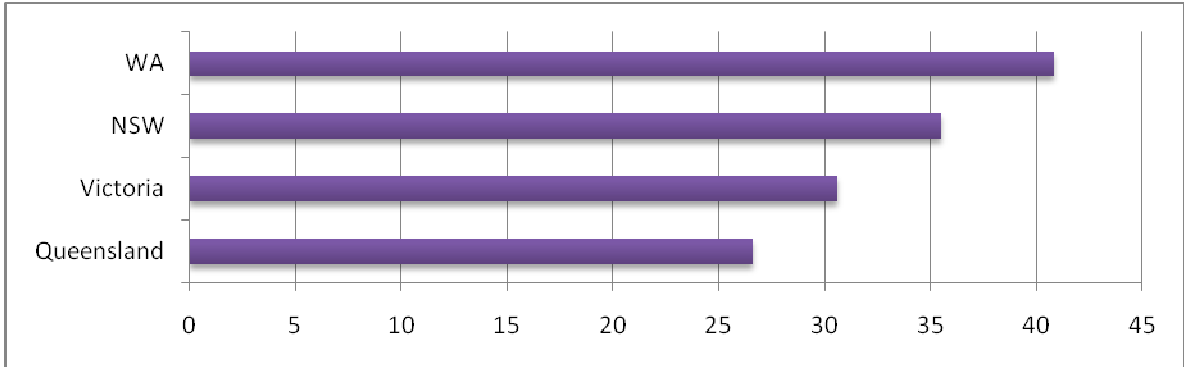
“It puts co-operative members off becoming directors and imposes unnecessary and extra considerable financial expenses onto organisations - training, insurance just to cover "red tape".”

Impact on director recruitment according to State

There was some variation in the impact of personal liability on director recruitment by state, with more than 40 per cent of respondents from Western Australia indicating they had declined an offer of directorship, compared to only 26.5 per cent in Queensland.

“The personal liability issue in our case quite simply makes it unattractive to continue as a director of a company with NSW operations when the rewards could be so far outweighed by the liabilities if anything untoward were to occur in our field operations.”

Figure 5.5
Declined the offer of a company directorship – “Yes” (State comparison)



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked whether they had declined the offer of a company directorship primarily due to the risk of liability.

The results were filtered based on respondents’ selection of where their primary organisation was headquartered / registered (see figure 1.4). N=406 (director / officer responses from WA, Queensland, NSW and Victoria)

Part 6: Concern about personal liability

When prompted with a range of potential concerns about the automatic personal liability of directors, more than 64 per cent of respondents said they were “seriously concerned” about the prospect of being subject to criminal and civil penalties. Conversely, less than five per cent said this was of no concern at all.

Almost 60 per cent were also seriously concerned about potential damage to reputation as a director (Figure 6.2).

“You have only one reputation, the other issues can be managed.”

Also of moderate to serious concern is the impact on companies and boards of the automatic personal liability of directors in terms of time, cost and long-term reputational damage (Figure 6.1).

“My concern is if personal liability leads to decisions/actions that compromise the effectiveness of a director in serving the board and organisation.”

“While defences exist, they are obviously dependent on the effectiveness of your legal counsel in framing them and of the willingness of the judge to accept those arguments – in practice things probably generally work out OK for most people, but there is considerable trauma (and expense) in working through the process and no certainty that there will be exoneration for the NEDs at the end of the process.”

“If they exist [reasonable defences] it is not clear what they are or how the courts would rule. Raises the issue of costly legal defence & no certainty of desired outcome.”

“The money spent to obtain external advice to provide a line of defence has become a generally accepted ‘insurance policy’ expense.”

The director community is somewhat divided over whether exercising due diligence diminishes the risk of automatic personal liability.

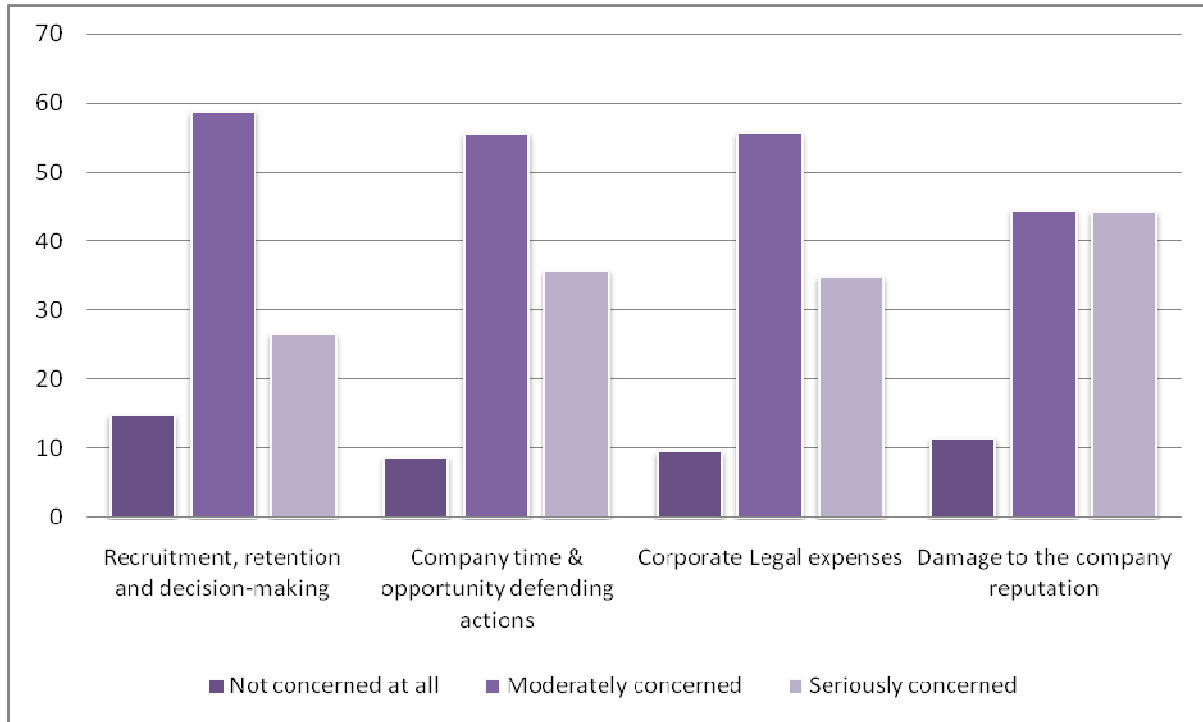
“I am comfortable with the risk appetite/profile of companies I am involved with. I am not overly concerned due to my own due diligence and cautious nature.”

“All of the above do cross the mind from time to time, however as previously mentioned, my view has been that we are doing our utmost in the key areas, then that is in itself our defence.”

One respondent interpreted “concern” not in terms of “worry”, but more a question on responsibility.

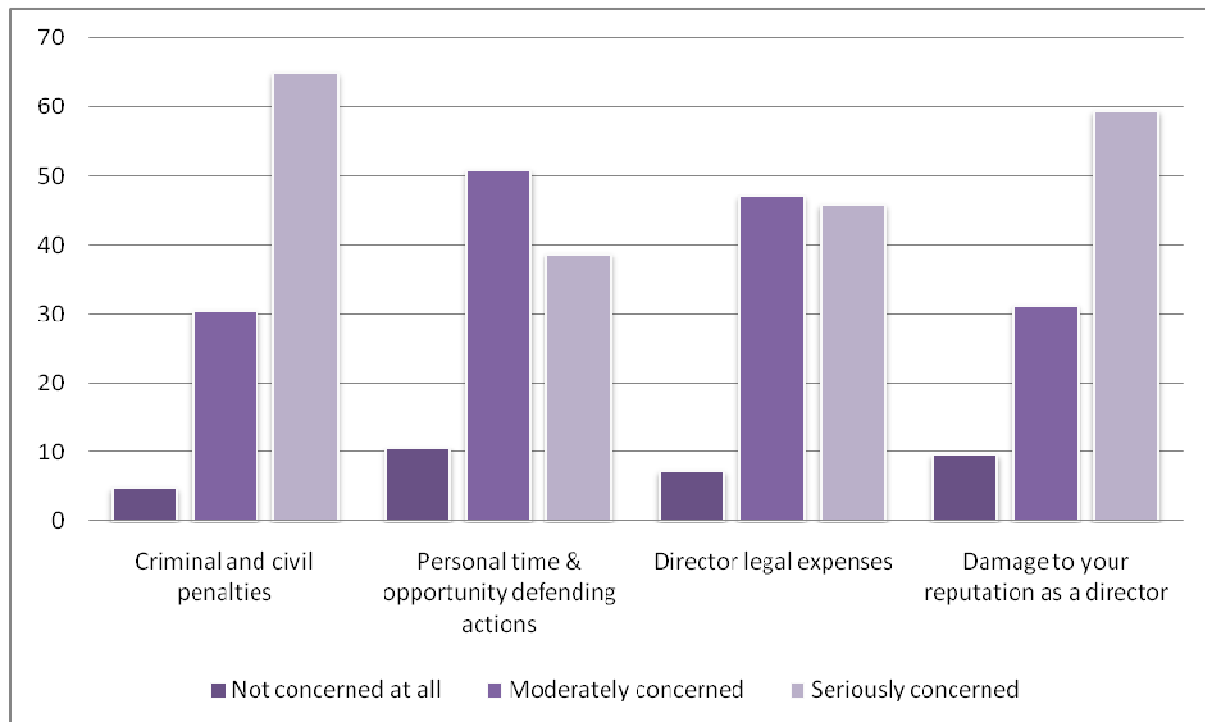
“I and all directors should be seriously concerned as the buck stops and rightly so, with us. We should always be considerate of our actions and in the back of our minds realise that we could be seriously affected by poor actions or lake of action taken by us.”

Figure 6.1
Types and degree of concern about the business (board and company) impact of personal liability of directors



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked how concerned they were about the automatic personal liability of directors when it comes to the impact on board recruitment, retention & decision-making; lost time & opportunity for the company defending actions; corporate legal expenses and damage to the company's reputation . N=486 (director / offices responses only).

Figure 6.2
Types and degree of concern about the personal impact of personal liability



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked how concerned they were about the automatic personal liability of directors when it comes to being subject to criminal and civil penalties as a director; lost time & opportunity as a director defending actions; director legal expenses and damage to reputation as a director. N=486 (director / offices responses only).

Part 7: The weight of law

Compliance

The time spent on compliance varies across organisations, from less than 10 per cent in almost a quarter of cases nominated by directors, to more than 25 per cent in 33 per cent of organisations represented in the survey responses (Figure 7.1).

Comments supplied to support the selected option indicated whether this percentage breakdown of compliance v performance activity was reasonable and appropriate, or suggested other ways in which they had sought to deal with compliance requirements.

A number also noted the time spent on compliance was, or is, expected to increase.

Some respondents also noted they had selected one of the higher options because of membership of a compliance committee (board sub-committee).

The question was based on a framework whereby compliance and performance are considered two essential, interrelated board functions, which can compete for board time and attention. As the time that a board devotes to each will rightly vary according to company circumstances, what we sought to quantify with the following question, was whether the burden of compliance is considered too great (Figure 7.2). Seventy-nine percent of respondents have some degree of concern in this regard. Several respondents rightly noted that compliance can positively impact performance outcomes.

“This question is based on the false premise that the two are completely separate. Many activities in the compliance area are simply good risk management and improve performance overall.”

“Far too much of the [board] discussion is on compliance etc. The shareholders actually want performance within a reasonable and controlled framework.”

“It hinders productivity to an alarming rate in our business.”

“It is fast becoming the main factor that is throttling competition and innovation and ensuring that the best and brightest are unlikely to become directors.”

“The overall time has to expand to match the additional workload of compliance.”

“We tend to extend the time required rather than limit time for growth. This adds a challenge when setting remuneration and, in due course, will impact when recruiting new directors.”

“The burden is so unclear - or too complicated and extensive - that I and many directors I know just go for performance and try their best to always do the right thing, unknowing of their potential liability.”

“In order for me to be satisfied regarding this risk, excessive executive time is negatively spend adversely impacting the company’s ROI [return on investment] and other KPIs [key performance indicators]”

“It is important for Boards to be aware of compliance and to be confident that the company is compliant. It is compliance with poorly thought through legislation that is an issue.”

“Excessive time spent on compliance does distract from time spent on performance as well as seriously colour risk appetite. It is clear that bureaucratically overburdened economies create less wealth and significant capital flows away or is placed elsewhere.”

“I think Boards need to take compliance very seriously and so devoting time is appropriate. It is the uncertainty and unfairness of liabilities that concerns me.”

“The time demands of compliance are extensive - however it is my view that boards must allocate whatever time is required to meet its duties. Directors are inadequately compensated for the additional time and the personal risk.”

“Essential part of NED role but could be made easier by focus on streamlining Oz legislation and unifying.”

“Total waste of my time in all reality when it does not affect the outcome of any move against me or the companies due to some petty official on a power trip.”

“Far too little time is spent in this important area, and is a matter I will be raising.”

“There has to be a balance. It is currently too far heavily weighted on the side of compliance.”

“Law are there to protect society and members of the community. We should spend a reasonable amount of time in compliance.”

“Sensible boards manage this pretty well.”

“Because of the processes I have mandated to be in place the oversight of compliance is well balanced.”

“Our focus on compliance ensures a safe and productive workplace. This enhances operational performance.”

“Compliance costs may have increased because of legislation but not directly as a result of the personal liability issue.”

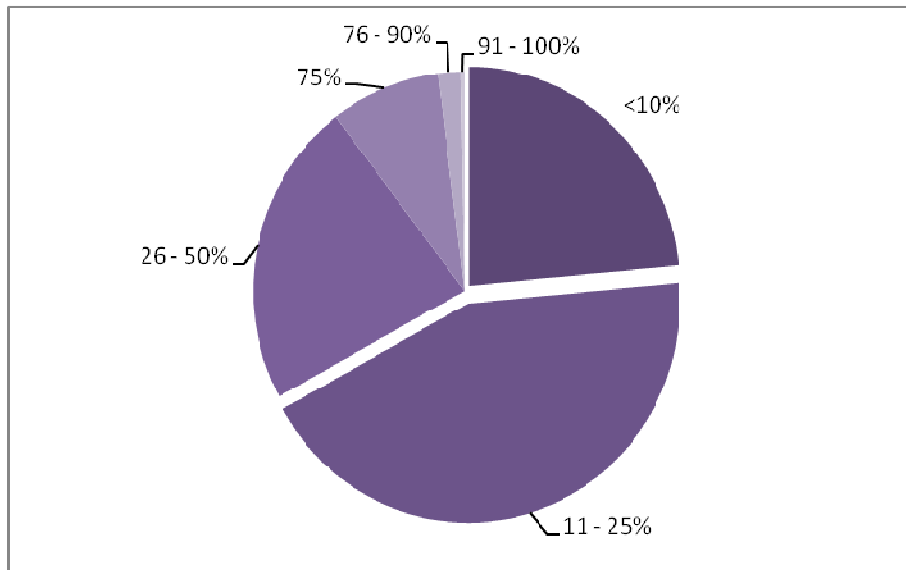
Compliance in not-for-profit organisations

“Compliance burden on not for profits is unreasonable.”

“This [concern regarding time spent on compliance] becomes more so with a NFP.”

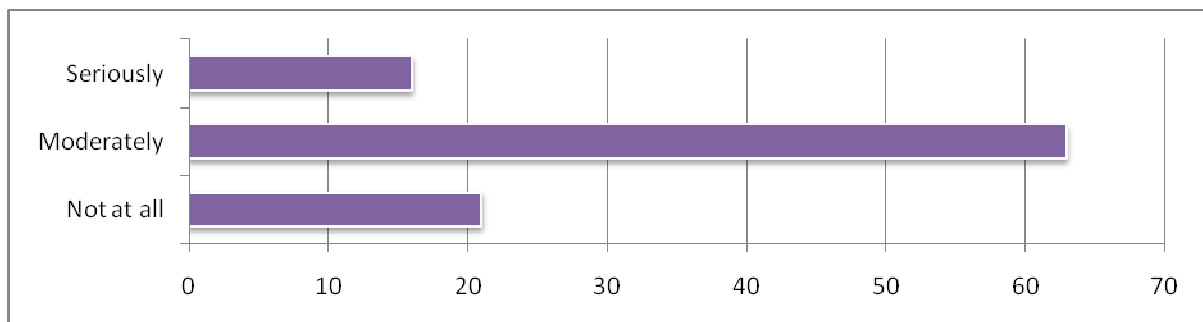
“This [cost of compliance] is a significant expense for a non-profit organisation, where our revenues should be better spent.”

Figure 7.1
Percentage of time as a director spent on compliance



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked what percentage of their time as a director on a board is spent on oversight of compliance with laws and external regulations (as opposed to performance activities). N=584 (director / offices responses only).

Figure 7.2
Degree of concern regarding time spent on compliance



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked how concerned they were that the time their board invests in oversighting compliance is detracting from time that could be spent focusing on enhancing organisational performance / productivity. N=586 (director / offices responses only).

Occupational Health & Safety

Background

Safe Work Australia, an independent statutory body, is developing model work health and safety laws as part of an initiative of the Council of Australian Governments. Safe Work Australia Members agreed on 28 April 2010 by majority to endorse the current version of the amended Model Work Health and Safety (WHS) Act and to recommend it to the Workplace Relations Ministers' Council (WRMC) to note. The model WHS Act is scheduled for commencement on 1 January 2012.

More than 87 per cent of respondents said the harmonisation of OH&S legislation would positively impact their organisations. Those that selected "Yes" highlighted the good sense of consistency and the obvious benefits of reduced cost, confusion and complexity of OH&S compliance requirements.

Some respondents that selected "No" advised that they did so because their organisations were International, did not operate across multiple states in Australia, or the nature of their organisations would mean it would have minimal impact.

Other respondents said they found it difficult to comment because of a lack of awareness of how the laws may be streamlined and the uncertainty remaining regarding the final 'result' of the WHS Act (including which current state law may be the preferred 'model').

"I very much support this development, however as Directors it will have no impact upon our day to day approach to OH&S - we give it full attention anyway."

"Yes, but only in relation to new investment in Australia, as the risk is already assumed and managed for existing businesses. However, one shouldn't have to demonstrate a positive impact to justify the repeal of bad laws."

"A streamlined OH&S system with clear duties and defences for directors allows for a precise decision making process. As it stands presently a director can be personally liable for an accident that happens completely beyond their best efforts to ensure doesn't happen in the first place."

"The current laws in NSW are very discriminatory against employers and difficult to defend. Harmonisation will only be effective if the laws remove some of the anti-employer aspects of the legislation. Every employer has to work on providing a safe workplace but there is no effective obligation on employees to work safely and the courts tend to work against employers. Having unions getting a share of the fines in some cases is obnoxious and open to abuse - this cannot be part of any harmonisation."

"There is a great deal of uncertainty about the extent, detail and application of the law that varies from state to state and targets independent non-executive directors. Harmonised law that treated the company as the responsible entity not individuals and removed the abomination of presumption of guilt would significantly assist in clarifying and streamlining decision making and remove the absurd targeting of individuals who were not directly involved in culpable behaviour. Such targeting of independent non executive directors is very inhibiting to broad based decision-making."

"We have operations in other states and territories. We have considered moving head office to a better jurisdiction but the prospect of a single, national, law is one that is far better for us than the prospect of simply being registered in the best of the current mish mash of jurisdictions."

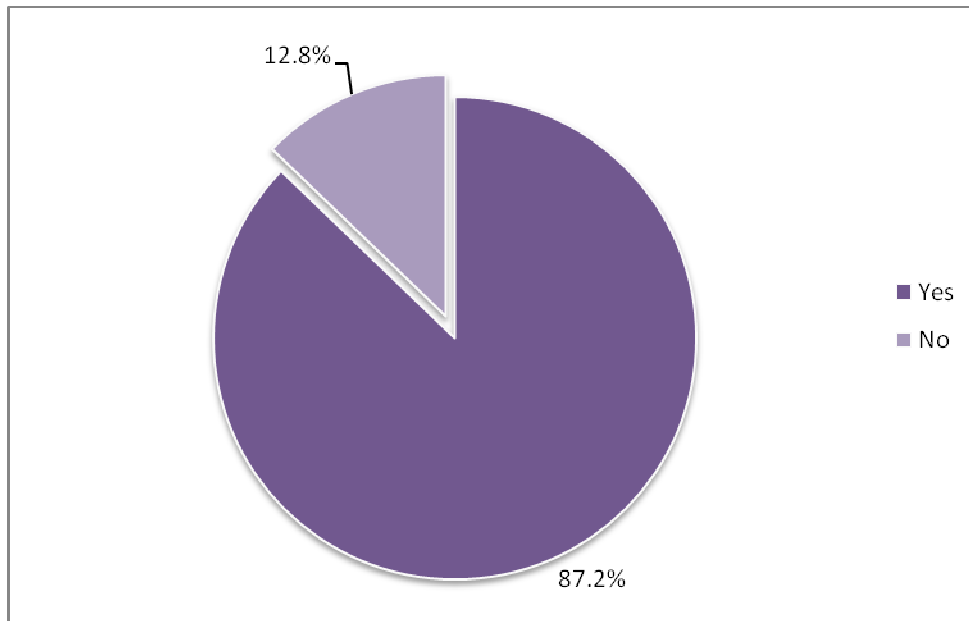
"yes, yes, yes yes. way overdue, good initiative, the sooner the better. bring on harmonised environmental legislation as well!"

"It won't be beneficial until all states harmonise."

"Hard to tell - it might make things worse."

“I don't think it would make a significant impact at this time because most of our Australian operations are in Vic and not significantly affected by diversity (and as operations are low risk on OH&S front). However, increased simplicity for compliance and a compliance approach that is 'substantive' rather than 'form' based would be advantageous in any complex regulatory area.”

Figure 7.3
Impact of harmonised OH&S legislation



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked whether the introduction of harmonised OH&S legislation would positively impact their organisations. N=483 (director / officers only).

Part 8: The Future – Emerging Directors

While a small sample, the responses from ‘aspiring directors’ were also indicative of concern regarding personal liability.

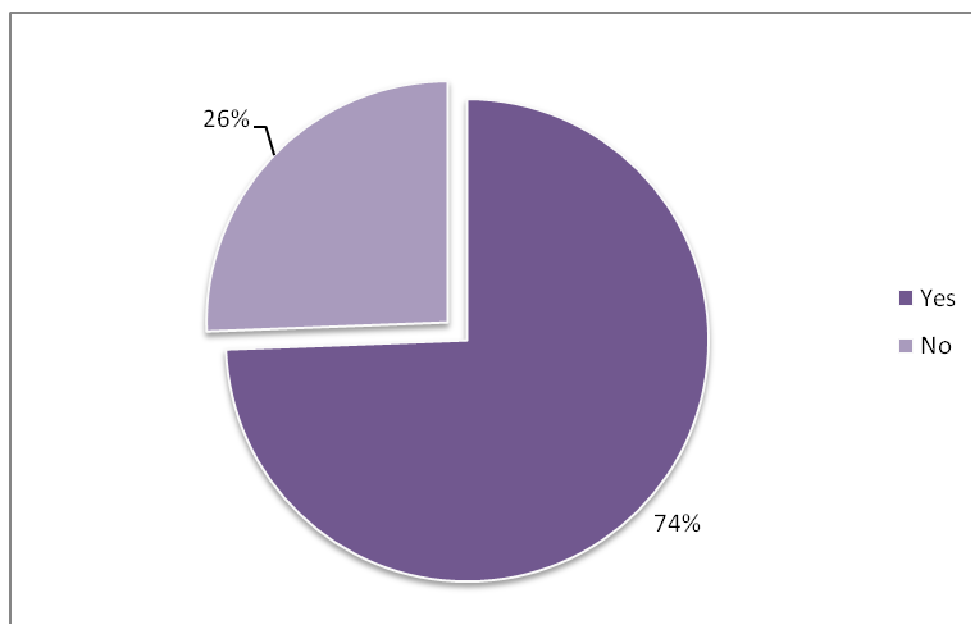
Seventy-four per cent of those who identified themselves in the survey as “aspiring directors” (when asked to nominate their primary role or interest in directorship) said the risk of personal liability had made them reconsider directorship as a career (Figure 8.1).

“Particularly in regard to Not-for-Profits, where the remuneration does not compensate for the risk and where control over employees can be more difficult.”

“The benefits derived from a role as a director - even in an NFP are severely negated by the prospect of personal liability exposure.”

“No, but I would take due regard in taking up a directorship as to the potential personal liabilities I may be taking on.”

Figure 8.1
Directorship as a career



Source: The Australian Institute of Company Directors, *Director Liability Survey 2010*, Survey respondents were asked whether the risk of personal liability had made them reconsider directorship as a career N=43 (aspiring directors only).

Part 9: The role of education

The level of education – and therefore understanding – a director has of their duties and responsibilities is an important factor underpinning awareness and perceptions of the personal liability risk.

The need for education – and experience – was highlighted in qualitative commentary with regards to board decision-making, inductions, appointments and reducing liability risk.

“In my experience inexperienced directors are unaware of their duties and go along with group think to make dumb ones so it is more a case of who one agrees to be on a board with rather than the legislation itself which is of concern.”

“Acquainting new board members with these relatively new provisions is difficult - they often seem counter-intuitive to those without a sound knowledge of governance and risk management principles.”

“It [the impact on personal liability] ought to made more widely known to directors before they are allowed to become directors.”

“There is an opportunity here to use the legislation as a driver to train and educate the workforce. This has several positive outcomes; the workforce may respond positively (the company cares), the risk of facing a liability claim is reduced as it can be demonstrated that the company is actively seeking to provide safe systems of work. In all it is a good investment in personnel and defraying exposure.”

Part 10: Comparison to the results of the 2008 Federal Treasury Survey of Company Directors

A selection of the most relevant results from the 2010 Survey – in comparison to the 2008 Federal Treasury Survey of Company Directors is provided below.

Question and summary of responses	Treasury 2008	Directors & Officers 2010	NEDs only data 2010
Which option best describes your primary role, or interest in directorship?			
Non-executive director	84.2	49.4	100
How many boards do you sit on or report to?			
4 or more	71.3	23.9	29.8
How many years have you been a director or officer?			
More than 10 years	75.3	53.8	53.3
Please indicate whether as a director you have had experience in one or more of the following roles?			
Chairman	69.3	47.6	55.2
Audit Committee (Member / then Chair)	74.3	29.4	43
Please rate the degree of risk that you consider currently applies to directors being found personally liable for decisions they have made (as a director or officer) in good faith:			
Medium to High Risk	78.2	73.9	70.4
Has the risk of personal liability (under any law) caused you or a board of directors on which you sit to take an overly cautious approach to business decision-making?			
Occasionally or Frequently (combined)	78.2	65.3	66.2
Primarily due to the risk of personal liability under any law, have you ever:			
Declined an offer of a company directorship	71.1	32.2	33.7
Resigned from a position as a company director	46.4	22.2	23.6

Question and summary of responses	Treasury 2008	Directors & Officers 2010	NEDs only data 2010
Primarily due to the risk of personal liability under any law, do you know of other people who have ever declined an offer of a company directorship (Response = "Yes")	62.9	56.8	59.9
Do you think there are reasonable defences for directors under the Corporations Act 2001 and derivative liability* laws (e.g. some OH&S laws, environmental laws)? (Response = "No")	67	53.7	54.1

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Note: The horizontal axes of all bar charts in this report show responses in percentages.

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