Resignations or Removal of Directors

This position paper addresses issues associated with director resignations and removals. A director is appointed by the shareholders of the company and can only be removed by those shareholders. Circumstances can arise which lead a director to consider resigning from the board. The decision to do so is a serious one that requires careful consideration of a number of matters.

What does the Corporations Act say?

The Corporations Act 2001 (sections 203 and 206) and a company’s constitution outline the ways in which a director can leave office. These include resigning, not being properly appointed, breaching provisions set out in the company’s constitution, being automatically disqualified from managing a corporation, becoming bankrupt, being removed by resolution in a general meeting or by death.

The FAQ, Resignation or removal of directors, looks at specific requirements of the Corporations Act including what notice to give when resigning.

When should a director consider resigning from the board?

Resignation from a board is a matter where individual directors and boards must consider their individual circumstances. In general, in order to fulfil his duty under the Corporations Act, a director must be satisfied that he has taken into account all circumstances when considering his actions and believes his proposed course of action is in the best interests of the company and its shareholders.

The effective functioning of the board is reliant on each director having confidence with one another and the group as a whole. A director might consider resigning when he has lost the confidence of the board. A director cannot be compelled to resign where he has been appointed by shareholders.

Examples of situations where it might be appropriate for a director to consider resigning include:

- where the director is the subject of litigation connected with the company;
- when his presence on the board could be seen to cause harm to the company;
- where the director cannot allocate the required time to preparation for and attendance at board meetings;
- where the director has a fundamental conflict with the best interests of a company
which arises over time, e.g. where another board on which a director serves becomes a market competitor;
• where the director has a fundamental ongoing conflict of interest;
• where the director feels he no longer adds value to the Board.

What steps could a director take before resigning?

Before resigning a director could take a number of steps to clarify whether this course of action is the most appropriate one. These steps could include raising the issue of concern with the chair of the board and privately raising the issue with other board members.

Can a board remove a director?

Under the Corporations Act directors of public companies are appointed by the shareholders of the company to act on their behalf. Therefore only shareholders can remove these directors. AICD strongly supports this fundamental principle of law and corporate governance.

AICD believes that allowing a board to remove a director could potentially compromise the independence of mind that is the objective of many corporate governance principles. For example, a director who conscientiously challenges a board’s thinking may be fulfilling his duties under the Corporations Act.

On the other hand, situations may arise where the board believes it is in the interests of shareholders to remove the director. If a director refuses to resign, AICD believes the matter must be referred to a general meeting of shareholders who have appointed the director.

In proprietary companies a director may be removed by a majority of directors if the constitution allows it. In doing this, and if the person is an executive director, the company needs to be mindful of the terms of employment for that director, unfair dismissal laws and natural justice requirements.

Should shareholders be informed of the reason for the director’s resignation?

The notice of director’s resignation is lodged with ASIC but the director does not have to state reasons for his resignation.

There has been some discussion about whether a director should make public the reason for his resignation. Some argue that this would provide relevant information to the market.
However, before a director makes that decision they must consider whether such a disclosure could breach board or company confidentiality. The material in a disclosure might also give rise to defamation proceedings or could damage the company’s reputation or interests.

These matters should all be carefully considered and evaluated before a director makes such a disclosure.

The role of board evaluations

There is increasing recognition that boards are more effective if their collective performance and that of individual directors is evaluated regularly. Such evaluation may make it clear that a particular director who is not performing, and whose term has not expired, should leave the board and make way for fresh talent. When told of this assessment, a director may leave the board of his own volition.

A change may be required at board level if the company’s business mix changes. The board may need directors with different skills.

For more information on board evaluations, please refer to AICD’s publication, *Evaluating board performance* (2007).

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