Baker McKenzie.

Directors Duties in Australia

Introduction

Australian law imposes a wide range of duties and obligations on directors of Australian companies. These duties range from common law and statutory duties to act in the best interests of the company to more specific obligations such as disclosure requirements and managing environmental and cyber security risk.

Matters covered in this Guide include principal duties, financial reporting, restricted benefits, insider trading, corporate governance, contravention and other sources of liability (including anti-bribery and corruption, competition, employment and tax laws).

Being a trusted adviser to many of the top companies in Australia, Baker McKenzie is recognised for its extensive experience advising directors of Australian companies.

This Guide provides you with a broad overview of the duties of directors of Australian companies, however it is not intended to be an exhaustive analysis of all relevant legal requirements. If you would like to discuss any of the issues raised in this Guide, please contact us.

PARTNER CONTACTS

SYDNEY

Tharani Dharmaraj
+61 2 8922 5477
tharani.dharmaraj@bakermckenzie.com

Sean Duffy
+61 2 8922 5270
sean.duffy@bakermckenzie.com

Steven Glanz
+61 2 8922 5205
steven.glanz@bakermckenzie.com

Kate Jefferson
+61 2 8922 5302
kate.jefferson@bakermckenzie.com

Michael Kunstler
+61 2 8922 5333
michael.kunstler@bakermckenzie.com

Ben McLaughlin
+61 2 8922 5342
ben.mclaughlin@bakermckenzie.com

Lawrence Mendes
+ 61 2 8922 5472
lawrence.mendes@bakermckenzie.com

Antony Rumboll
+61 2 8922 5102
antony.rumboll@bakermckenzie.com

Lance Sacks
+61 2 8922 5210
lance.sacks@bakemckenzie.com

Eric Thianpiriya
+61 2 8922 5631
eric.thianpiriya@bakemckenzie.com

Lucas Tyszkiewicz
+61 2 8922 5497
lucas.tyszkiewicz@bakemckenzie.com

Leo Vellis
+61 2 8922 5745
leo.vellis@bakemckenzie.com

MELBOURNE

Arthur Apos
+61 3 9617 4461
arthur.apos@bakermckenzie.com

Lewis Apostolou
+61 3 9617 4403
lewis.apostolou@bakermckenzie.com

Adrian Chin
+61 3 9617 4415
adrian.chin@bakermckenzie.com

Simon De Young
+61 3 9617 4370
simon.deyoung@bakermckenzie.com

Liam Hickey
+61 3 9617 4221
liam.hickey@bakermckenzie.com

Peter Ickeringill
+61 3 9617 4563
peter.ickeringill@bakermckenzie.com

Andrea Kennedy
+61 3 9617 4423
andrea.kennedy@bakermckenzie.com

Richard Lustig
+61 3 9617 4433
richard.lustig@bakermckenzie.com

Rick Troiano
+61 3 9617 4247
riccardo.troiano@bakermckenzie.com

BRISBANE

Tanya Denning
+61 7 3069 6219
tanya.denning@bakermckenzie.com

Jim Peterson
+61 7 3069 6207
jim.peterson@bakermckenzie.com

Derek Pocock
+61 7 3069 6234
derek.pocock@bakermckenzie.com

Trudi Procter
+61 7 3069 6256
trudi.procter@bakermckenzie.com

Contents

1. Position as a director 4
2. Directors' duties 6
3. Delegation and reliance on others 14
4. Financial reporting 15
5. Company meetings 18
6. Continuous disclosure 18
7. Restricted benefits 19
8. Insider trading 21
9. Climate change risk 22
10. Cyber security risk 24
11. Whistleblower protections 25
12. Contraventions 26
13. Corporate governance 27
14. Insurance and indemnities 29
15. Other sources of liability 29

This Guide is current as at 30 July 2023 unless indicated otherwise.

All dollar amounts stated in this Guide are Australian dollars.

About Baker McKenzie Australia

Baker McKenzie is unique among Australian law firms in our ability to deliver the knowledge, experience and capabilities of our global network to our clients in the local market. Companies benchmark themselves against the best practice in their sectors, globally, not just domestically. We provide our clients with the innovative legal solutions they expect from the global top-tier law firm, together with commercial pragmatism and seasoned experience as leaders in Australia. Baker McKenzie has been an integral part of the Australian legal landscape since 1964.

1. Position as a director

1.1 Appointment of directors

A proprietary company must have at least one director. At least one director of a proprietary company must ordinarily reside in Australia.[1]

A public company must have at least three directors. At least two directors of a public company must ordinarily reside in Australia.

Only an individual (i.e. a natural person) who is at least 18 years of age may be appointed as a director. A person must give written consent to act as a director of a company before being appointed.

Directors may be appointed by the members of the company in a general meeting or by the other directors in a board meeting. Directors leave office if they resign, retire, are removed in accordance with the *Corporations Act 2001* (Cth) (**Corporations Act**) and/or the company's constitution, or are disqualified from managing companies.

Certain personal details of a director, such as their full name, date and place of birth and usual residential address, must be notified to the Australian Securities and Investments Commission (**ASIC**) shortly after the director is appointed. These details then become publicly available.

Also, each director of an Australian company is required to verify their identity by holding or applying for a unique director identification number. For further details, see "Director identification number regime" in section 1.7 below.

Notification must also be made to ASIC if a director ceases acting as a director within 28 days of the date that the person ceased acting as a director. If a director's resignation is not notified to ASIC within 28 days, the resignation is not effective until the date that ASIC is notified. Also, a director's resignation or a resolution of members of a proprietary company to remove a director, is generally not effective if the company does not have at least one other director remaining at the end of the day the resignation or resolution (as applicable) is to take effect.

1.2 Alternate directors

A director may generally appoint an alternate to exercise some or all of the director's powers for a specified period (for example, to attend and vote at board meetings when the director is unable to attend). The method of appointment and powers of alternate directors are usually set out in the constitution of the company. A person acting as an alternate director is subject to the same duties and liabilities as other directors. The appointment and removal of an alternate director must be notified to ASIC.

1.3 De facto and shadow directors

A person may be deemed to be a director of a company (even if they have not validly been appointed as a director) if:

- they act in the position of a director (**de facto director**); or
- the directors of the company are accustomed to act in accordance with the person's instructions or wishes (**shadow director**).

---

[1] If a proprietary company wishes to raise capital through equity crowd-sourced funding (**CSF**), it will be subject to Australia's CSF regime which requires, amongst other things, that the company have at least two directors. If the company has two directors, one of the directors must be ordinarily resident in Australia. If the company has more than two directors, a majority of the directors must be ordinarily resident in Australia.

Determining whether or not a person is a de facto or shadow director will be based on the control and influence they have over the company's affairs, including considering the duties performed by that person in the context of the particular company. However, a person will not be considered to be a de facto or shadow director merely because the directors of a company act on advice given by the person in a professional advisory capacity (for example, an accountant or lawyer), or the person's business relationship with the directors or the company.

A person acting as a de facto director or shadow director is subject to the same duties and liabilities as a formally appointed director.

1.4 Functions of the board of directors

The board's functions depend on the circumstances of the company and may include to:

- appoint and reward the company's chief executive;
- set goals, formulate strategies and approve business plans for the company;
- approve annual budgets and key management decisions (such as decisions on major capital expenditure, business acquisitions, restructuring and refinancing);
- monitor management performance and business results;
- set and review policies for member communication and provide reports to members;
- set and review budgetary control and conformance strategies; and
- monitor the company's corporate governance practices.

Although the directors of a company act collectively as a board, each director is individually subject to statutory and common law duties, including to act in good faith in the best interests of the company and with reasonable care and diligence.

1.5 The constitution

A company's internal management may be governed by the replaceable rules in the Corporations Act, by a constitution or by a combination of both.

It is common for a company to have a constitution. The constitution sets out rules by which the company is governed and regulates the relationships between the company, its officers and members. The constitution may include, amend or displace the replaceable rules in the Corporations Act.

The constitution typically includes provisions regarding:

- the share capital of the company, including procedures for issuing and transferring shares in the company;
- powers, rights and duties of members;
- appointment of officers and their powers; and
- the winding up of the company.

A company's constitution (if any) and any replaceable rules that apply to the company operate as a statutory contract that is binding on the company, each member and each director and secretary.

1.6 Responsibilities of individual directors

On a board of directors, individual directors may have distinct responsibilities to the company, depending on the nature of their particular role within the company.

Executive and non-executive directors

If there are executive and non-executive directors on a board, the executive directors will usually have greater responsibilities than the non-executive directors. The distinction between executive and non-executive responsibilities is reflected in the different standards of care applied to individual directors - a higher standard of care will apply to executive directors (see section 2.5 below).

Managing directors

The board of directors can also choose to appoint a managing director to assume responsibility for the day-to-day management of the company. Where an individual director on a board would not have the ostensible authority to act alone on behalf of the company, a managing director may be empowered to act in a way akin to the board acting as a whole.

1.7 Director identification regime

Each director of an Australian company (including registered Australian bodies and registered foreign companies) is required to hold or apply for a unique identifier known as a "director identification number" (**director ID**). A director ID will be permanently assigned to each director, regardless of what company or companies they may be involved with over time, and will remain on record even if they cease being a director.

The aim of the director ID regime is to better track directors and their relationships between individuals and entities, in an effort to identify high-risk individuals and crack down on illegal activities such as phoenixing.

Under the director ID regime, directors appointed must apply for a director ID before their appointment.[2] Directors must apply for their own director ID (as they need to verify their own identity). There is no application cost.

Substantial civil and criminal penalties apply for non-compliance with the requirements of the director ID regime.

2. Directors' duties

2.1 Who the duties are owed to

Directors must act for the benefit of "the company as a whole". In general, this means that directors must act in the interests of all members collectively. However, directors may sometimes be required or permitted to take other interests into account.

Individual members

In general, directors do not owe duties directly to individual members. However, in specific circumstances, a director may be found to owe a duty to an individual member. For example, a director acting as a proxy for a member at a meeting owes a duty to that member to vote according to their wishes.

Creditors

[2] For directors under the *Corporations (Aboriginal and Torres Strait Islander) Act 2006* (Cth) (i.e. Aboriginal and Torres Strait Islander persons and members of an Aboriginal and Torres Strait Islander corporation), those appointed on or before 31 October 2022 have until 30 November 2023 to apply for a director ID. For such directors appointed from 1 November 2022, they must apply for a director ID before their appointment.

In addition to the duty to prevent insolvent trading (see section 2.7 below), directors may sometimes be required to take into account the interests of creditors, particularly where the company is insolvent or approaching insolvency. The duty to take into account the interests of creditors in certain circumstances when a company is approaching insolvency has been confirmed by UK courts, providing a gateway for applicability in other common law jurisdictions such as Australia.[3]

The Corporations Act also requires creditors' interests to be considered in specific circumstances (for example, where the company is proposing to pay a dividend or undertake a capital reduction or share buy-back). In a recent case, the Federal Court found that two former executive directors of Dick Smith breached their duty of care and diligence by approving a final dividend when the information available to them suggested that doing so would cause delays in the company's payments to creditors. The directors were held liable for damages equal to the dividend of almost $12 million.[4]

Employees

Directors do not owe any general duty to employees of the company. However, directors may breach their duties to the company if their actions cause the company to breach its obligations to employees. Directors (and others) are also prohibited from entering into agreements or transactions that are intended to avoid paying employee entitlements. If the company is being wound up, a person who contravenes this prohibition is liable to compensate employees for their loss.

Corporate groups

Subject to the special case of wholly-owned subsidiaries outlined below, a director of a company owes duties to that company, and not to any related companies or any member who appointed the director. A director breaches their duty if they enter into a transaction or make a decision in the interests of a related company or appointing member if it is not also in the best interests of their company.

Wholly-owned subsidiaries

A director of a company that is a wholly-owned subsidiary of a holding company is taken to act in good faith in the best interests of the subsidiary if:

- the constitution of the subsidiary expressly authorises the director to act in the best interests of the holding company;
- the director acts in good faith in the best interests of the holding company; and
- the subsidiary is not insolvent at that time and does not become insolvent because of the director's act.

However, a director of a wholly-owned subsidiary must not disregard the subsidiary's interests entirely, and failure to identify and take into account the consequences of their actions for the subsidiary may amount to a breach of their duty of care and diligence.

2.2 Overview of directors' duties

The directors of a company are, subject to its constitution, responsible for the overall management of the company. In performing their role, directors are subject to a range of duties and obligations under the Corporations Act, the common law and the company's constitution (if it has one).

[3] In *BTI 2014 LLC v Sequana SA and others* [2022] UKSC 25, the UK Supreme Court confirmed that directors owe a duty to creditors under the general law duty to act in the best interests of the company. The creditor duty may be enlivened where there is either imminent insolvency or the probability of an insolvent liquidation (or administration) about which the directors know or ought to know. The precise nature of the duty is a question of fact and degree which needs to be balanced against shareholders' interests where they may conflict.
[4] *DSHE Holdings Ltd (Receivers and Managers) (in liq) v Potts; HSBC Bank Ltd v Abboud; Potts v National Australia Bank Ltd* [2022] NSWCA 165.

The key duties of directors are to:

- act in good faith in the best interests of the company;
- exercise their powers for the purposes for which they were conferred;
- act with reasonable care and diligence;
- avoid conflicts of interest; and
- not improperly use company information or their position to gain an advantage for themselves or someone else or to cause detriment to the company.

This Guide deals with the duties of directors, but similar duties apply to all company officers, including secretaries.

A director may rely on certain information or advice given by certain people, provided the reliance was made in good faith and after making an independent assessment of the information or advice.

Unless the company's constitution provides otherwise, the directors may delegate any of their powers to others, and are not responsible for a delegate's exercise of power if the delegation satisfies a test of reasonableness (see section 3 below).

A director who breaches any of their duties is liable to civil penalties. If the breach is reckless or dishonest, the director may also incur criminal penalties (see further, section 12 below).

Stepping stone liability

A director who unreasonably exposes their company to sanctions, civil liability or reputational damage by allowing the company to contravene the Corporations Act or another law, even if acting in accordance with the wishes of members, may be liable for a breach of their statutory duty of care to the company.[5] Any contravention of these duties may give rise to both civil penalties and disqualification as a director.

This approach is known as "stepping stone liability" - essentially, depending on the responsibilities and degree of control a director has over the company and the particular circumstances of the company, the Court may find secondary personal liability on the part of a director for allowing a primary breach by the company. Further, members of the company cannot sanction, ratify or approve any such contravention by a director. Accordingly, although section 180 of the Corporations Act does not impose strict liability on directors for breaches of the Corporations Act or other laws, directors must exercise reasonable care and take precautions to avoid foreseeable risks of harm to the company and its members.

2.3 Duty of good faith

Directors must exercise their powers and discharge their duties in good faith in the best interests of the company as a whole.

At a minimum, this duty requires directors to act in what they honestly believe to be the company's best interests. In addition, a director's conduct may be assessed objectively by reference to what a reasonable director would consider to be the company's best interests.

2.4 Duty to act for a proper purpose

Directors must exercise their powers and discharge their duties for a proper purpose.

The company's constitution may specify the proper purposes of a power, otherwise the proper purposes must be determined based on the particular circumstances and the usual function of such a power. For example, one proper purpose of the power to issue shares is to raise capital. By contrast, issuing shares for the

[5] *Cassimatis v Australian Securities and Investments Commission* [2020] FCAFC 52.

substantial purpose of diluting an existing member's voting power, is likely to be an improper exercise of the power.

It is not sufficient that a director honestly believes their actions are for a proper purpose if a court considers that purpose to be improper.

A director may have exercised a power for both improper and proper purposes. If the director would not have exercised the power "but for" an improper purpose, they may be found to have breached this duty.

2.5 Duty of care and diligence

A director must exercise their powers and discharge their duties with the degree of care and diligence that a reasonable person would exercise if they:

- were a director of a company in the same circumstances; and
- occupied the same office and had the same responsibilities within the company as the director.

The conduct required to satisfy this duty depends on the company's circumstances and the particular director's position and responsibilities. Executive directors, and other directors with special skills or experience, are held to a higher standard. For example, a finance director who is insufficiently diligent in relation to financial matters may breach this duty even though identical conduct by a non-executive director may not constitute a breach. Similarly, any special responsibilities held by the chair of the board may affect the scope of their duty of care.

However, a director's conduct will not necessarily be excused due to a lack of skills or experience. All directors are required to meet a minimum objective standard. For example, all directors are expected to take reasonable steps to be in a position to guide and monitor the management of the company.[6]

This is likely to mean that directors should not be absent from board meetings without good reason. All directors must also have sufficient financial literacy at least to understand the company's financial position and any financial statements the company is required to prepare.

Business judgment rule

A director who makes a "business judgment" is taken to satisfy their duty of care and diligence in respect of the judgment if they:

- make the judgment in good faith for a proper purpose;
- do not have a material personal interest in the subject matter of the judgment;
- inform themselves about the subject matter of the judgment to the extent they reasonably believe to be appropriate; and
- rationally believe that the judgment is in the best interests of the company.

A "business judgment" is any decision to take or not take action with respect to a matter relevant to the business operations of the company. For example, decisions to enter into transactions and matters of planning and forecasting are likely to constitute "business judgments", but not the mere performance of directors' oversight responsibilities.

[6] In December 2022, ASIC commenced civil penalty proceedings in the Federal Court against 11 current and former directors and officers of The Star Entertainment Group Limited (**Star**) for alleged breaches of their duty of care under section 180 of the Corporations Act. ASIC alleges that Star's board and executives failed to give sufficient focus to the risk of money laundering and criminal associations that are inherent in the operation of a large casino with an international customer base. This case will examine the scope of the statutory duty of care and is particularly important as this is the first time that ASIC has pursued an entire board for alleged breaches of their directors' duties in relation to non-financial risk management.

To benefit from the rule, a director must make a conscious and informed decision, even if it is a decision not to take action. A director who simply fails to turn their mind to a matter has not made a business judgment and is not protected by the rule.

This statutory business judgment rule provides a defence in relation to the duty of care and diligence only. It does not apply in relation to a director's other duties (although a court may still be reluctant to review a director's business judgments). The rule also does not apply to other potential liabilities of directors, including liability for misstatement in a prospectus or takeover document, insolvent trading or misleading or deceptive conduct.

2.6 Duty to avoid conflicts of interest

Directors must not place themselves in a position where there is an actual conflict, or a real possibility of conflict, between their duties to the company and a personal interest or duty owed elsewhere (for example, to another company).

It is not necessary for the company to suffer any detriment or the director to obtain any advantage in order for this duty to be breached.

The exact scope of the duty, and the steps required to avoid a breach, may be affected by the company's constitution, as discussed below. A general requirement, depending on the nature of the director's interest or other duty, is disclosure to the company.

Disclosure of interest and other procedural requirements

A director who has a material personal interest in a matter that relates to the affairs of the company must give the other directors notice of the interest, unless an exception applies (for example, the interest relates to a proposed contract that is subject to approval by members). The notice must provide details of the nature and extent of the interest and its relation to the company's affairs and must be given at a directors' meeting as soon as practicable after the director becomes aware of their interest in the matter. Standing notice of the interest may also be given.

In addition, a director of a public company who is required to disclose such an interest may not be present at a directors' meeting while the relevant matter is being considered and may not vote on the matter, unless the disinterested directors resolve that the interest should not disqualify the director. The same restriction usually does not apply to directors of a proprietary company, depending on its constitution and the particular circumstances. However, even where a director is permitted to vote on a matter in which they are interested, they must do so with regard to the best interests of the company.

The constitution of the company, whether public or proprietary, may also impose additional restrictions regarding directors' interests or requirements regarding disclosure of interests and other procedures to be complied with by interested directors.

Dealing with the company

The duty to avoid conflicts of interest may be breached where a director enters into, or otherwise has a personal interest in, a contract or other transaction with the company, or is a director of two companies that are transacting with each other.

If the director breaches the duty (for example, by not complying with disclosure and other requirements), the company may be entitled to avoid the transaction and the director may be liable to compensate the company for any loss it suffers or account to the company for any profit made by the director.

However, under the replaceable rules in the Corporations Act, if the director of a proprietary company complies with the requirement to disclose any personal interest before a transaction is entered into, the director may retain benefits under the transaction and the company cannot avoid the transaction merely because of the director's interest. Even if a proprietary company's constitution displaces this rule, it will typically contain a provision with similar effect.

Nevertheless, an interested director is not entitled to deal freely with the company merely because they disclose their personal interest. The director must continue to satisfy all of their duties, particularly the duties to act in the company's best interests and with care and diligence. In some circumstances, those other duties may oblige an interested director to take additional action to protect the company's interests, such as disclosing further information about the transaction or actively attempting to prevent a transaction that is not in the company's interests.

Additional restrictions apply to dealings between a public company and its directors – see section 7.1 below.

Appropriation of corporate opportunities

A director must not appropriate, or divert to another person, a business opportunity which the company is considering or pursuing, or which the company could reasonably be expected to have an interest in.

A director who breaches this rule is liable to account to the company for any profit made by the director, even if the transaction was fair to the company or the company was unable to exploit the opportunity itself or unlikely to have made the profit in question.

Misuse of position or information

Overlapping with the preceding general rule, directors have a statutory duty not to improperly use their position, or information obtained by virtue of their position, to gain an advantage for themselves or someone else or to cause detriment to the company.

Such conduct is "improper" if it breaches the standards of conduct that would reasonably be expected of a person in the director's position, regardless of whether the director considers it improper.

The duty not to misuse company information continues to apply after a person ceases to be a director, provided that the person obtained the information while they were a director. The duty not to misuse company information can apply to information which is not confidential. A general duty of confidence also applies in relation to information which is confidential.

Authorisation by members

If a director has fully disclosed a personal interest or other duty, the members may authorise the director to act in what would otherwise be a breach of the above conflict rules or ratify a past breach by the director, unless the company's constitution provides otherwise.

For example, fully informed members may authorise a director to enter into a transaction with the company or to exploit an opportunity that the company does not wish to exploit.

Such authorisation or ratification typically cannot be provided by the disinterested directors unless the constitution gives them that power.

Neither the members nor the disinterested directors are able to authorise or ratify a breach of a director's statutory duties (including the duties to act in the company's best interests and for a proper purpose), so an interested director must continue to satisfy those duties even if a potential conflict has been waived. However, in the case of a director's statutory duties not to "improperly" use their position or information, an appropriate approval may have the effect of removing any impropriety so that the duty is not breached.

2.7 Duty to prevent insolvent trading

Insolvency

A company is insolvent if it is not able to pay all of its debts, as and when they become due and payable. This is predominantly a cash flow rather than a balance sheet test, requiring an assessment of whether the company's anticipated current and future cash flows will be sufficient to enable its current and future liabilities to be paid when due.

However, the company's overall financial position may also be considered, having regard to commercial realities. For example, a temporary lack of liquidity or cash reserves may not constitute insolvency if the company is able to realise assets or raise funding in a timely manner.

Duty to prevent insolvent trading

Directors have a duty to prevent the company from trading while insolvent. A director breaches this duty if:

- the director fails to prevent the company from incurring a debt;
- the director is aware that there are reasonable grounds for suspecting that the company is insolvent or would become insolvent by incurring the debt, or a reasonable person in the circumstances would be so aware; and
- the company is insolvent or becomes insolvent by incurring the debt.

A debt may be incurred not only by incurring a liability in the course of trading but also, for example, by declaring or paying a dividend or making a capital reduction.

A director who breaches this duty may be ordered by a court to pay a civil penalty and/or to pay to the company, its liquidator or the relevant creditor compensation equal to the amount of loss suffered by the creditor. In addition, a director who breaches this duty dishonestly may incur criminal penalties.

Defences

It is a defence to a civil claim for insolvent trading if:

- the director had reasonable grounds to expect, and did expect, that the company was solvent and would remain solvent even if it incurred the debt;
- the director reasonably relied on a competent and reliable person to provide adequate information about the company's solvency and, on the basis of that information, expected that the company was and would remain solvent;
- the director took all reasonable steps to prevent the company from incurring the debt; or
- due to illness or for some other good reason, the director did not take part in the management of the company when the debt was incurred.

Safe harbour

Directors have the protection of a legislative carve-out from the duty to prevent insolvent trading. Specifically, directors of financially distressed companies are protected in relation to debts that the company incurs in connection with developing and taking a course of action that is reasonably likely to lead to a better outcome for the company, than proceeding immediately to voluntary administration or winding up.

This safe harbour applies from the time the director starts developing a course of action until:

- the end of a reasonable period of time if the director fails to take the course of action within that reasonable period of time;
- the director stops taking the course of action;
- the course of action stops being reasonably likely to lead to a better outcome for the company; or

- the company goes into administration or liquidation.

Directors will not be able to rely on the safe harbour if the company is not meeting its obligations in relation to employee entitlements or its taxation reporting obligations.

Further, in order to have the protection of the safe harbour, directors bear the burden of adducing or pointing to evidence that suggests a reasonable possibility that they have been acting under the safe harbour.

Bearing the evidential burden in mind, in order to ensure that the safe harbour applies, directors should:

- obtain ongoing legal and financial advice as soon as they suspect insolvency or a risk of insolvency;
- obtain ongoing advice from a sufficiently briefed and appropriately qualified turnaround or restructuring professional;
- formulate a detailed turnaround plan that addresses operational, strategic and financial issues, including proposed courses of action; and
- carefully document the steps taken in implementing the turnaround plan through board minutes and file notes.

An independent review of the safe harbour provisions was conducted in 2021 and resulted in a number of recommendations aimed at simplifying and clarifying the wording of the provisions.[7] In its response to the final report, the former government accepted a number of these recommendations, including the development of a best practice guide to safe harbour to assist directors with understanding their obligations.[8] At this stage, it is unclear when any reforms will be enacted.

Simplified debt restructuring for small businesses

Eligible small businesses are given access to a simplified debt restructuring process. This process allows directors to retain control of their company while it develops a plan to restructure its debts with the assistance of a restructuring practitioner. While the restructuring process is under way, directors are permitted to engage in transactions that are in the ordinary course of business (or otherwise with the consent of the restructuring practitioner or the leave of the Court) and are protected from liability for insolvent trading.

To be eligible for the new process, a company must meet certain criteria, including having total liabilities that do not exceed $1 million, resolving that it is insolvency or likely to become insolvent and appointing a small business restructuring practitioner to oversee the process. To put the plan to creditors, the company must also have paid all its employee entitlements and lodged all its tax returns, notices and statements.

The restructuring process involves the directors developing a restructuring plan detailing how the company's creditors would be repaid if the plan were made, which must be put to those creditors within 20 business days of entering the process (unless extended by the restructuring practitioner). The creditors then have generally 15 business days to accept or reject the proposed plan. The plan will be accepted if more than 50% of the creditors (by value) vote in its favour. If the plan is not accepted, the directors will remain in control of the company, but are no longer protected from liability for insolvent trading.

2.8 Responsibility for administrative obligations

A company's secretary is responsible for ensuring that the company complies with certain requirements under the Corporations Act, such as the requirements to have a registered office and to notify ASIC of certain details. If a proprietary company does not have a secretary, each director is instead responsible for any contravention of such requirements, unless the director took reasonable steps to ensure the company's compliance.

[7] Review of the Insolvent Trading Safe Harbour Report (November 2021)
[8] Government Response to the Review of the Insolvent Trading Safe Harbour (March 2022)

2.9 Liabilities of corporate trustees

If a company which acts as trustee:

- incurs a liability which it cannot discharge; and
- is not entitled to be indemnified by the trust against that liability due to the terms of the trust or because the company committed a breach of trust or acted outside the scope of the trust,

the directors are jointly and severally liable to discharge the trustee company's liability (unless any particular director is held responsible).

3. Delegation and reliance on others

3.1 Delegation

Unless the company's constitution provides otherwise, the directors of a company may collectively (but not individually) delegate any of their powers to a committee of directors, an individual director, an employee of the company or any other person.

The appointed delegate must exercise the powers delegated in accordance with the directions of the directors. Any exercise of power by the delegate is as effective as if the directors themselves had exercised it. However, each director remains responsible for the exercise of the power by the delegate unless the director believed, on reasonable grounds:

- that the delegate would exercise the power in conformity with the duties imposed on directors by the Corporations Act and the company's constitution; and
- in good faith and after making proper inquiry, that the delegate was reliable and competent in relation to the power delegated.

3.2 Non-delegable powers and responsibilities

Irrespective of the above, there are certain powers and responsibilities of directors that cannot be delegated and must be exercised by directors themselves. Some of the non-delegable powers and responsibilities include:

- becoming and remaining familiar with the operations and business fundamentals of the company;
- monitoring and remaining informed as to the company's operations (for example, by regularly attending board meetings and making inquiries as to the company's operations);
- maintaining a reasonably informed opinion of the financial status and solvency of the company;
- understanding the company's financial status including, at minimum, having a basic understanding of financial statements and the general accounting standards applicable to the company; and
- approving the company's financial statements.

Also, directors have an obligation to generally supervise and remain informed of a delegate's use of any delegated powers and responsibilities, including applying the director's own knowledge to information provided to the director by that delegate.

3.3 Reliance on information or advice

In certain circumstances, a director is entitled to rely on information, or professional or expert advice given or prepared by:

- an employee of the company whom the director reasonably believes to be reliable and competent in relation to the relevant matters;
- a professional adviser or expert if the director reasonably believes that the relevant matters are within that person's professional or expert competence;
- another director or officer in relation to matters within that person's authority; or
- a committee of directors on which the director did not serve in relation to matters within the committee's authority.

A director's reliance on such information or advice is presumed to be reasonable if the reliance was made in good faith and after the director made an independent assessment of the information or advice (having regard to the director's knowledge of the company and the complexity of the structure and operations of the company).

That is, directors must bring an independent mind to bear when considering professional or expert advice and must not simply accept the views of others. Also, directors should not automatically expect to be kept properly informed by senior management or others of all important matters relating to the company. Directors should not only exercise independent judgement on company matters, but also regularly engage with senior management and other key personnel in the company, to facilitate a healthy flow of information between the board and management (see further, section 13 below).

4. Financial reporting

4.1 Financial records

All companies are required to keep written financial records and retain them for at least seven years after the transactions covered by the records are completed.

The financial records must correctly record and explain the company's transactions and financial position and performance and enable true and fair financial statements to be prepared and audited.

4.2 Reporting obligations

Directors must inform themselves of the reporting obligations of their company depending on its size and type. Public companies, disclosing entities, large proprietary companies and certain small proprietary companies are all required to prepare annual financial reports and directors' reports.

The basic financial reporting requirements of these companies are, with limited exceptions, to:

- prepare an annual financial report and directors' report;
- arrange for the financial report to be audited;
- send the financial report, directors' report and auditor's report to members;
- lodge the financial report, directors' report and auditor's report with ASIC (or the Australian Securities Exchange (**ASX**) if the company is listed on ASX); and
- if the company is a public company, present the financial report, directors' report and auditor's report at the annual general meeting (**AGM**).

Disclosing entities (including listed companies and certain companies with 100 or more members) also have half-yearly reporting obligations, including to:

- prepare a half-yearly financial report and directors' report and have the financial report audited or reviewed by an auditor and obtain an auditor's report; and
- lodge the financial report, directors' report and auditor's report with ASIC (or ASX if the company is listed on ASX).

Companies listed on ASX have additional periodic reporting obligations under the ASX Listing Rules.

Proprietary companies that are subject to Australia's crowd-sourced funding regime and have raised over $3 million must also have their financial statements audited.

4.3 Financial report

The financial report of a company for a financial year consists of:

- the financial statements for the year;
- notes to the financial statements; and
- a directors' declaration about the statements and notes.

Financial statements and notes

The financial statements and notes must comply with Australia's accounting standards issued by the Australian Accounting Standards Board (**Accounting Standards**) and must give a true and fair view of the financial position and performance of the company (or a consolidated group, if required by the Accounting Standards).

If a company is required to prepare a financial report, it is generally also required to have the report audited and obtain an auditor's report.

Directors' declaration

As part of the financial report, the directors of a company must make a declaration about the financial statements and notes. This declaration must be made in accordance with a resolution of the directors. It must also specify the date on which the declaration was made and be signed by a director.

The directors' declaration must include declarations such as whether, in the directors' opinion:

- there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable; and
- the financial statements and notes are in accordance with the Corporations Act, including that they:
  - comply with the Accounting Standards; and
  - give a true and fair view of the financial position and performance of the company.

The directors of a listed company must only make the directors' declaration after each person who performs a chief executive function or a chief financial officer function has given the directors a declaration regarding the company's financial records, financial statements and notes.

4.4 Directors' report

The directors' report for a financial year must include information such as:

- the names of the directors;
- a review of the company's operations and the results of those operations;

- details of any significant changes in the company's state of affairs;
- the company's principal activities, and any significant changes in the nature of those activities;
- details of dividends paid, or recommended or declared but not paid;
- significant post-financial year matters, and likely developments in the company's operations for future years;
- if the company's operations are subject to any particular and significant environmental regulation, details of the entity's performance in relation to environmental regulation; and
- indemnities given and insurances paid by the company for its officers and auditor.

The directors' report for a listed company must include additional information such as:

- each director's interests in shares and other securities of the company or a related company;
- directorships of other listed companies held by a director in the current or previous two financial years;
- information to enable an informed assessment of the company's business strategies and prospects;
- details of amounts paid or payable to the company's auditor for non-audit services; and
- a report on the remuneration of key management personnel, as discussed below.

Remuneration report

The remuneration report must include details of the remuneration of each member of the key management personnel of the company (or the consolidated group, if applicable), such as details of:

- the person's short-term, long-term, termination and post-employment benefits;
- any performance conditions that apply to any part of the person's remuneration;
- equity instruments, and options and rights over them, held or controlled by the person or a close family member of the person; and
- the duration, termination notice periods and termination payments under any contract of employment with the person.

At a listed company's AGM, a resolution to adopt the remuneration report must be put to a vote of members (excluding key management personnel covered by the report and their closely related parties). This vote is advisory only and does not bind the directors or the company. However, if 25% of votes oppose adoption of the report at two consecutive AGMs, at the second AGM members may resolve to hold a "spill meeting" within 90 days at which they will vote to replace or re-appoint all directors (except for a managing director whose appointment is indefinite). If the company does not hold the spill meeting within 90 days, each director at that time commits an offence.

Further, at a listed company's AGM, the chair must allow a reasonable opportunity for the members to ask questions about, or make comments on, the remuneration report.

4.5 Directors' obligations

Directors have an obligation to take all reasonable steps to comply with, or to secure compliance with, the financial record-keeping and reporting obligations set out in the Corporations Act. A director commits an offence if they breach this obligation dishonestly.

5. Company meetings

5.1 Member meetings

Member meetings provide opportunities for a company and its directors to provide information to members and agree key decisions. A public company must hold an AGM within 18 months of its incorporation and within 5 months of the end of its financial year. There is no requirement for a proprietary company to hold an AGM, but certain actions (such as changing the company's name or its capital structure) are required to be approved by members.

Meetings of members can be called by a director or at the request of members with at least 5% of the votes that may be cast at the meeting. An unlisted company must give at least 21 days' notice in advance of a meeting and a listed company must give at least 28 days' notice in advance of a meeting, unless the constitution specifies a longer period of notice.

5.2 Director meetings

Meetings of directors are less regulated than member meetings. The rules applying to directors' meetings are typically contained in the company's corporate documents, including the constitution and members agreement (if any). Some matters, such as resolutions required for key decisions and use of technology, may need to follow Corporations Act requirements.

5.3 Hybrid or virtual meetings

From 1 April 2022, permanent changes were made to the Corporations Act to permit companies to hold hybrid meetings and, if expressly provided by the company's constitution, virtual-only meetings. The Corporations Act specifies particular requirements for companies to comply with if they convene and hold meetings using virtual technology. Generally, all meetings must allow members as a whole a reasonable opportunity to participate in the meeting. This includes, for example, holding the meeting at a reasonable time and allowing members to ask questions and make comments both orally and in writing.

6. Continuous disclosure

In addition to the periodic reporting obligations outlined in section 4 above, listed companies and other disclosing entities have continuous disclosure obligations under the Corporations Act and the ASX Listing Rules (as applicable).

An entity listed on ASX must immediately notify ASX of any information concerning the entity that would reasonably be expected to have a material effect on the price or value of its securities.

Civil and criminal penalties apply for non-compliance with the continuous disclosure requirements, and this liability extends to a director (or any other person) who is involved in a breach of these obligations (see further, section 12.2 below).[9] However, a "due diligence" defence is available if the person took all reasonable steps to ensure that the entity complied with its continuous disclosure obligations and reasonably believed that the entity was complying.

From 14 August 2021, permanent changes were made to the continuous disclosure laws under the Corporations Act, heightening the bar for civil contraventions of these obligations. Under the changes:

---

[9] In February 2023, the Federal Court ordered GetSwift Limited (**GetSwift**) to pay a penalty of $15 million, being the largest penalty handed down against a company for breaching continuous disclosure laws. GetSwift's former CEO and executive chairman was ordered to pay a penalty of $2 million and disqualified from managing corporations for 15 years. Two other former directors were ordered to pay penalties of $1 million and $75,000 and disqualified from managing corporations for 12 years and 2 years respectively.

- listed entities and their directors will only be exposed to civil liability for continuous disclosure breaches if there has been "knowledge, recklessness or negligence" (**Fault Test**) in updating the market with price sensitive information; and
- the Fault Test must also be established for a breach under the misleading or deceptive conduct provisions of the Corporations Act and the *Australian Securities and Investments Commission Act 2001* (Cth), meaning that a breach of continuous disclosure obligations will no longer automatically trigger misleading and deceptive conduct liability unless the Fault Test is proven.[10]

This new standard will apply both in proceedings brought by ASIC and in private proceedings, such as member class actions.

The reforms do not, however, impact:

- the existing criminal offence for failing to comply with the continuous disclosure obligations under the ASX Listing Rules and the Corporations Act;
- liability for disclosing information to the market that is misleading or deceptive or if guidance or other forward-looking statements are made without reasonable grounds; or
- ASIC's power to issue infringement notices to listed entities, if ASIC has reasonable grounds to believe that an entity has failed to disclose non-public information that a reasonable person would consider materially price-sensitive,

none of which require the Fault Test to be established.

The amended continuous disclosure provisions are permanent; however, they are scheduled to be reviewed by an independent expert in 2024.

Unlisted disclosing entities must similarly notify ASIC as soon as possible of materially price-sensitive information that is not generally available (or follow ASIC's published guidance regarding website disclosure). In both cases, there is a limited exception in relation to certain confidential information.

An entity listed on ASX must also disclose other specific information to ASX, such as the material terms of employment, service and consultancy agreements with directors or their related parties, and details of directors' interests in securities of the entity or a related entity. If details of a director's interests in securities are not disclosed to ASX by the entity, the director is personally obliged to notify ASX, and commits an offence if they fail to do so.

7. Restricted benefits

The duty to avoid conflicts of interest is supplemented by the following statutory restrictions on certain benefits that may be received by directors and others.

7.1 Financial benefits to related parties of public companies

For a public company, or an entity controlled by a public company, to give a financial benefit to a related party of the public company:

- the public company or controlled entity must obtain the approval of the public company's members and give the benefit within 15 months after approval; or

[10] A director who is found not to be liable for continuous disclosure breaches because the director did not *actually* know the information is prince sensitive information may still breach their duty to act with reasonable care and diligence if they **should** have known the information is likely to be price sensitive information (see *Australian Securities and Investments Commission v Blue Star Helium Limited (No 4)* [2021] FCA 1578).

- the giving of the benefit must fall within an exception under the Corporations Act (as outlined below).

"Giving a financial benefit" is to be interpreted broadly and includes arrangements that are indirect, informal or involve conferring a financial advantage rather than paying money. Examples include:

- providing a related party with finance or property;
- buying an asset from or selling an asset to a related party;
- leasing an asset from or to a related party;
- supplying services to or receiving services from a related party; and
- issuing securities or granting an option to a related party.

"Related parties" of a public company include:

- directors of the public company or an entity that controls the public company;
- the spouses of those directors and the parents and children of the directors or their spouses; and
- entities controlled by any of those people,

at the relevant time, in the previous six months, or if likely in the future.

There are several exceptions to the requirement for member approval. For example, if the financial benefit is:

- on arm's length terms;
- reasonable remuneration to an officer or employee of the public company or a related company;
- payment of expenses incurred by such an officer or employee in performing their duties; or
- no more than $5,000 in a financial year.

7.2 Payment for loss or retirement from office

A company (and its associates) must not give anyone a benefit in connection with a person's retirement or resignation from, or loss of, an office or position of employment in the company or a related company if:

- the office or position is a managerial or executive office; or
- the retiree has held a managerial or executive office in the company or a related company in the previous three years,

unless certain member approvals are obtained. If this prohibition is contravened, the provider of the benefit and, in many cases, the recipient of the benefit both commit an offence.

For a listed company, a "managerial or executive office" is one held by a member of the key management personnel (being persons (including directors) who have authority and responsibility for planning, directing and controlling the activities of the company, directly or indirectly). For an unlisted company, "managerial or executive office" means the office of director, or any other office or position held by a person who is also a director of the company or a related company.

The prohibition does not apply to certain benefits including:

- exempt benefits, such as certain deferred bonuses and redundancy payments; or
- benefits which are:
  - genuine payments by way of damages for breach of contract;

  - given under an agreement entered into before the person began to hold the office or position from which they are retiring; or
  - payments by way of pension or lump sum for past services to the company or a related company,

  provided the total value of all benefits does not exceed the retiree's average annual base salary (pro rata if the person held the office or position for less than a year).

7.3 Financial assistance

A company is prohibited from financially assisting a person to acquire shares (or any right or interest in shares) in the company or a holding company of the company, unless:

- the assistance does not "materially prejudice" the company or its members or the company's ability to pay its creditors;
- the company follows certain procedures involving member approvals and lodging documents with ASIC (known as a "whitewash" procedure); or
- an exception applies, for example if the assistance is given under an employee share scheme approved by members.

Subject to certain exceptions, a company is also prohibited from acquiring shares in itself or taking security over shares in itself or in a company that controls it.

7.4 Directors' bonuses

If a director receives a benefit from the company which is "unreasonable" (i.e. uncommercial from the company's point of view), and a winding up of the company begins within the following four years, a court may order the director to return some or all of the benefit and/or pay the company a fair amount for some or all of the benefit (in addition to other possible orders).

This rule applies whether the benefit is a payment, company property, securities in the company or the right to such a benefit (such as an option over shares), and whether the benefit is given to a director, a close associate of a director or another person on behalf of a director or their close associates.

8. Insider trading

Insider trading by a director, or any other person, is an offence. Insider trading occurs where:

- a person possesses "inside information", i.e. information which is not generally available and which a reasonable person would expect to have a material effect on the price or value of particular securities (or certain other financial products) if it were generally available;
- the person knows or ought to know that the information is inside information; and
- the person trades in or agrees to trade in the relevant securities (or procures another person to do so).

If the securities are listed, it is also an offence if a person communicates inside information to another person and knows or ought to know that the other person would be likely to trade in the relevant securities.

Information which is generally available is not inside information. Generally available information includes readily observable matter, information likely to have come to the attention of persons who commonly invest in the relevant kind of securities, and inferences drawn from these two types of information.

Exceptions and defences

There are a number of exceptions and defences to the insider trading prohibitions, for example where:

- a director is obtaining a share qualification;
- communication of the relevant information is required by law;
- the person being prosecuted obtained the relevant information solely because it was made known in a manner that was likely to bring it to the attention of persons who commonly invest in the relevant kind of securities; or
- the other party to the transaction knew, or ought reasonably to have known, of the information before entering into the transaction.

9. Climate change risk

With climate-related disclosure and "greenwashing" attracting attention recently, directors should be aware that these topics have become an area of increased corporate regulatory scrutiny in 2023.

ASIC Chair, Joe Longo, stated that ESG and climate-related disclosures by listed companies are a "core focus" of the Commission's 2023 corporate governance priorities.[11] Additionally, the ACCC Chair pledged in March 2023 to closely scrutinise “consumer, product safety, fair trading and competition concerns in relation to environmental claims and sustainability”.[12]

ASIC defines "greenwashing" as the practice of misrepresenting the extent to which a financial product or investment strategy is environmentally friendly, sustainable or ethical. ASIC states that labels or statements about a product's green credentials should not be misleading, emphasising that "being 'true to label' is not a nice-to-have, it's a regulatory must have". In their information sheet on how to avoid greenwashing, ASIC outlined a list of questions to consider and examples of misconduct which are particularly useful to directors in this space - notably the sheet sheds light on the importance of not using ambiguous or vague terminology or providing inadequate explanations. While the information sheet states that it "focuses on sustainability-related products issued by funds, its principles may apply to other entities that offer or promote financial products that take into account sustainability-related considerations".[13]

Importantly, ASIC recognises the recommendations made by the Financial Stability Board's Task Force on Climate-related Financial Disclosures (**TCFD**), and encourages voluntary disclosure in accordance with the TCFD framework. They expect that anyone who follows the framework will be well placed in future to transition to future disclosure standards in Australia.

On 27 June 2023, Treasury released a second consultation paper seeking views on the implementation of standardised, internationally-aligned requirements for disclosure of climate-related financial risks and opportunities in Australia.[14] According to this paper, it is anticipated that the mandatory disclosure regime will roll out in three phases, with specified thresholds determining the year in which entities are required to commence reporting. The proposed timeline for mandatory disclosure is as follows:

- commencing in the 2024-2025 financial year:
  - entities that are required to report under Chapter 2M of the Corporations Act (**Reporting Entities**) and fulfil two of the following three thresholds: (1) has over 500 employees; (2) has $1 billion or more in consolidated gross assets; and (3) has $500 million in consolidated revenue; and

[11] ASIC’s corporate governance priorities and the year ahead (ASIC)
[12] Compliance and Enforcement Priorities for 2023/2024 (ACCC)
[13] How to avoid greenwashing when offering or promoting sustainability-related products (ASIC)
[14] Climate-related financial disclosure: Second consultation (Treasury)

- Reporting Entities that are a ‘controlling corporation’ under the *National Greenhouse and Energy Reporting Act 2007* (Cth) (**NGER Act**) and meet the NGER publication threshold;

- commencing in the 2026-2027 financial year:
  - Reporting Entities that fulfil two the following three thresholds: (1) has over 250 employees; (2) has $500 million or more in consolidated gross assets; and (3) has $200 million in consolidated revenue; and
- commencing in the 2027-2028 financial year:
  - Reporting Entities that fulfil two the following three thresholds: (1) has over 100 employees; (2) has $25 million or more in consolidated gross assets; and (3) has $50 million in consolidated revenue; and
  - Reporting Entities that are a ‘controlling corporation’ under the NGER Act.

It is proposed that the disclosure requirements will align with IFRS S2 *Climate-related Disclosures* issued by the International Sustainability Standards Board (**ISSB**) in June 2023.[15] The AASB will be responsible for developing Australian climate disclosure standards, and it is anticipated that the AASB will conduct a public consultation process in the second half of 2023.

Directors should carefully consider the kinds of governance structures which may be required to be developed now, in order to best support company disclosure and reporting in the future, having regard to the connection between sustainability reporting and financial reporting.

Regulatory enforcement powers and remedies are extensive in Australia and include monetary penalties of up to $15.65 million for companies and $1.565 million for individuals. Criminal penalties for breaches of directors’ duties carry a penalty of up to 15 years imprisonment.

Between 1 July 2022 and 31 March 2023, ASIC secured 23 corrective disclosure outcomes, issued 11 infringement notices and commenced one civil penalty proceeding in relation to potential misleading marketing and/or greenwashing by entities.[16] ASIC’s greenwashing interventions broadly related to:

- net zero statements and targets, and claims of decarbonisation, which did not appear to have a reasonable basis, or were factually incorrect;
- claims that an entity’s operations, projects or products were “carbon neutral”, “clean” or “green”, when there appeared to be no reasonable basis for these claims;
- instances where financial products or managed funds included sustainability-related terms that were inconsistent with the funds’ investment, or the investment process described; and
- instances where the scope or application of an investment screen or exclusion was vague or overstated in a product disclosure statement or on associated websites for ESG-related financial products.[17]

In addition, on 2 March 2023, the ACCC announced that it would be investigating a number of businesses for potential greenwashing following an internet sweep of 227 businesses which found more than half of the businesses reviewed made concerning claims about their environmental or sustainability practices. The

[15] *IFRS S2 Climate-related Disclosures* (IFRS)
[16] ASIC’s recent greenwashing interventions (ASIC)
[17] In February 2023, ASIC commenced civil penalty proceedings against Mercer Superannuation (Australia) Limited for allegedly making misleading statements about the sustainable nature and characteristics of some of its superannuation investment options. ASIC alleges that Mercer made statements on its website that its ‘Sustainable Plus’ investment options excluded investments in companies involved in carbon-intensive fossil fuels like thermal coal, as well as those involved in alcohol production and gambling. However, ASIC alleges that the Sustainable Plus options had investments in many companies that were involved in these industries.

ACCC stated that it “will take enforcement action where it is appropriate to do so as it is critical that consumer trust in green claims is not undermined”.

With recent extreme weather events confirming the reality of climate change, it is important that climate considerations and risk management are at the front of mind for every organisation. With this in mind, the Governance Institute of Australia have released a guide for management and boards on the path to net zero and outlining the key steps to achieving net zero. These include governance, strategy, expectations and reporting. The guide acts as a practical framework to assist senior managers and directors and aims to do communicate the immediacy of climate change and its potential impact on companies.[18]

10. Cyber security risk

In the wake of recent high profile cyber security breaches involving Optus and Medibank, cyber security risk management is now a critical issue for company boards to consider. With increasing regulatory focus on cyber incidents and data breaches, the Australian government is considering implementing stronger cyber security regulation to support Australia's growing digital economy and protect it from cyber security threats.

In July 2021, the former government released a discussion paper, *Strengthening Australia's cyber security regulations and incentives*, which sets out a number of proposed strategies, including the proposal to set minimum expectations for companies to manage cyber security risks.[19] The discussion paper contemplates two potential governance standards:

- voluntary governance standards for larger companies which sets out the responsibilities (including that of directors) and processes for managing cyber security risks; and
- mandatory governance standards requiring larger companies to achieve compliance within a specific timeframe.

Whilst it is unclear when any proposed governance standard will be implemented, directors should be aware that consideration and management of cyber security risks may fall within the scope of their duty to act with reasonable care and diligence and in good faith in the best interests of the company.

Additionally, ASIC's published best practice guidelines in relation to cyber resilience processes highlights the importance of board engagement in cybersecurity strategy and governance, suggesting that directors should:

- follow the advice of the Australian Cyber Securities Centre in identifying and managing cyber risks;
- reflect on risks relevant to the company's business;
- take ownership of cyber strategy and ensure it is reviewed on a periodic basis;
- recognise and ensure there are appropriate safeguards in place to manage cyber risks; and
- where appropriate, engage external experts to review and challenge the company's cyber risk tolerance.[20]

ASIC also recently flagged the importance for listed companies to review their continuous disclosure plans to ensure they comply with their continuous disclosure obligations in the event of a material cyber security incident, noting that "the dynamic nature of both the extent and impact of a cyberattack means planning is critical".[21]

Similarly, the Australian Institute of Company Directors and the Cyber Security Cooperative Research Centre has developed a practical framework for directors to build organisational cyber resilience, underpinned by key

[18] Guide for boards and management on the path to net zero (Governance Institute of Australia)
[19] Strengthening Australia's cyber security regulations and incentives: call for views (2021)
[20] ASIC's Cyber resilience good practices.
[21] ASIC warns on cyber incident disclosure (Corporate Finance Update, March 2023)

cybersecurity governance principles. This framework recognises that directors have a critical role to play in managing cyber security risks and must seek to enhance their own skills and knowledge on cyber security to foster a cyber resilient culture within their organisation.[22]

In a recent case, *Australian Securities and Investments Commission v RI Advice Group Pty Ltd* [2022] FCA 496, the Federal Court found that the holder of an Australian financial services licence (**AFSL**) contravened the Corporations Act's requirements for a licensee to provide financial services 'efficiently, honestly and fairly' by failing to have adequate cyber security risk management systems in place to manage cyber security risks. The company was ordered to undertake a compliance program including engaging an external expert to assess the adequacy of its cyber security risk management systems and security training. Although this relates specifically to the company's duties as an AFSL holder, the case highlights ASIC's position regarding cyber security risk management and may be extended to apply directly to directors' duties.

There may also be additional cyber security and risk management obligations which will apply in regard to a company's assets that are "*critical infrastructure sector assets*" under the *Security of Critical Infrastructure Act 2018* (Cth), which was amended in 2021 and early 2022 and covers 11 industry sectors and 22 categories of critical infrastructure assets.

11. Whistleblower protections

The Corporations Act protects corporate sector "whistleblowers" who make public interest disclosures by identifying and calling out potential misconduct of companies.

Directors, auditors and other senior people within companies must be aware of their obligations to protect whistleblowers, and those who fail to handle whistleblower reports correctly may be in breach of their Corporations Act obligations. Contravention of the whistleblower protections may result in criminal or civil penalties for any person found to be:

- causing or threatening to cause detriment to a whistleblower; or
- disclosing a whistleblower's identity or information likely to lead to their identification, unless that disclosure is authorised under the law.[23]

Public companies, large proprietary companies and corporate trustees of superannuation entities regulated by the Australian Prudential Regulation Authority (APRA) are also required to have compliant internal company policies to ensure that whistleblowers are appropriately protected, and their complaints are heard. Such policies must include, amongst other things, information setting out the legal protections available to a whistleblower, and how the company will investigate whistleblower disclosures and protect whistleblowers from detriment.

In March 2023, ASIC released a report setting out good practices when designing programs or frameworks for handling whistleblower disclosures.[24] The report recommends that Australian entities should:

- establish a strong foundation for the whistleblower program, through implementing procedures and systems to embed the program's requirements;
- foster a whistleblowing culture which actively protects and support whistleblowers who make disclosures;

[22] AICD Cyber Security Governance Principles.
[23] In March 2023, ASIC commenced civil penalty proceedings against TerraCom Limited (**TerraCom**), its managing director, chief commercial officer and former directors in relation to an alleged breach of the whistleblower provisions under the Corporations Act. ASIC alleges that TerraCom and the relevant individuals engaged in conduct that harmed a whistleblower who revealed the alleged falsification of coal quality certificates. ASIC is seeking declarations of contravention, pecuniary penalties, disqualification orders and costs in these proceedings.
[24] Good practices for handling whistleblower disclosures (ASIC)

- invest resources and training for relevant officers and employees, and in particular for eligible recipients who receive disclosures;
- conduct periodic reviews of the program and associated policies, procedures and practices;
- take steps to address the issues raised by whistleblowers and use information obtained from disclosures to address emerging areas of risk;
- embed executive accountability for the program; and
- formalise arrangements for board or board committee oversight of the policy and program.

12. Contraventions

If a director contravenes any of their duties, or they fail to meet any of their obligations, proceedings may be brought against them. Proceedings can be brought by:

- the company;
- the company's members;
- creditors, insolvency administrators or trustees in bankruptcy;
- third parties; and
- regulatory authorities.

12.1 Regulatory authorities

The main regulatory authorities responsible for governing Australia's corporate sector are set out below.

ASIC

The Australian Securities and Investments Commission (**ASIC**) is a government body that enforces and regulates company and financial services laws through the general administration of the Corporations Act.

ASX

Alongside ASIC, the Australian Securities Exchange Limited (**ASX**) is responsible for the market regulation and compliance of Australia's listed companies.

ACCC

The Australian Competition and Consumer Commission (**ACCC**) is charged with administering Australian competition regulation through the implementation of the *Competition and Consumer Act 2010* (Cth) (**CCA**).

APRA

The Australian Prudential Regulation Authority (**APRA**) is the national regulator of the Australian financial services industry, supervising prudential institutions including deposit-takers (i.e. banks, building societies and credit unions), insurance companies and superannuation funds (other than self-managed superannuation funds).

12.2 Liability for involvement in a contravention

Where certain provisions of the Corporations Act (such as those discussed in sections 2, 3 and 6 above) are contravened, a director (or any other person) who is "involved" in the contravention may also be liable. A person is involved in a contravention if they aid, abet, counsel, procure or induce the contravention, are knowingly concerned in or party to the contravention, or conspire with others to effect the contravention.

Similarly, a director (or any other person) who aids, abets, counsels or procures the commission of any criminal offence is taken to have committed the same offence themselves.

12.3 Consequences of contravention

A director who breaches their duties or other obligations may be liable to suffer significant consequences, including:

- pecuniary penalties (fines);
- liability to compensate the company or others for loss suffered;
- liability to account to the company for profits made by the director; and
- disqualification from managing companies.

If a director's breach of duty constitutes an offence (which often, but not always, involves dishonesty), the director may also be liable for substantial criminal penalties (such as a term of imprisonment).

In civil proceedings only, the court has discretion to excuse a director from certain liabilities, if the director acted honestly and ought fairly to be excused for a contravention. Also, officers of listed entities will not contravene the civil penalty provisions of the Corporations Act if they can show that they took all reasonable steps in the circumstances to ensure that the entity complied with its obligations under the civil penalty provisions, and after doing so, believed on reasonable grounds that the entity was complying with its obligations.

The Court may also make a relinquishment order to neutralise any financial benefit that might have been gained from misconduct. Further, in making a pecuniary order, relinquishment order or imposing a fine, the Court must give priority to the compensation of victims.

12.4 Penalties under the Corporations Act

The maximum penalties, for offences committed on or after 1 July 2023, are:

- for criminal offences, 15 years' imprisonment and/or a fine the greater of:
  - $1.4085 million for an individual or $14.085 million for a body corporate;
  - three times the benefit gained and detriment avoided by the offence; or
  - for a body corporate, 10% of its annual turnover; and
- for civil breaches, a pecuniary penalty the greater of:
  - $1.565 million for an individual or $15.65 million for a body corporate;
  - three times the benefit gained and detriment avoided by the breach; or
  - for a body corporate, 10% of its annual turnover, up to $782.5 million.

13. Corporate governance

13.1 ASIC's Corporate Plan for 2022 to 2026

In its Corporate Plan for 2022 to 2026, ASIC set out its mandate to support Australia's economic recovery in the post-pandemic world, making clear that it will be taking greater action against the failure of boards to manage non-financial risk, with a focus on the individual conduct of directors.[25] It will be focusing its regulatory and enforcement strategy on four key pillars:

- reducing the risk of harm to consumers caused by poor product design, distribution and marketing, and driving compliance with new requirements;
- supporting market integrity through proactive supervision and enforcement of governance, transparency and disclosure standards in relation to sustainable finance;
- protecting consumers, with a focus on superannuation products, managed investments and financial advice; and
- focusing on the impacts of technology in financial markets and services, driving goof cyber-risk and operational resilience practices and addressing digitally enabled misconduct, including scams.

In its Future of the Board report, the Governance Institute confirmed that boards are set to come under greater scrutiny in the coming years, with higher expectations placed on directors to lead the way in terms of social and ethical matters.[26]

13.2 ASX Corporate Governance Principles and Recommendations

The ASX Corporate Governance Council's Corporate Governance Principles and Recommendations (**Principles and Recommendations**)[27] highlights the importance for directors and officers to monitor and take responsibility for culture, conduct and behaviour within companies, and an increased need for boards to engage with senior management on non-financial (as well as financial) risks. While the Principles and Recommendation are applicable to listed entities only, they are considered to be a benchmark for corporate governance in Australia generally and should also be reflected in the corporate governance practices of non-listed entities.

13.3 ASIC Corporate Governance Report

Similar to the Principles and Recommendations as mentioned above, ASIC's Corporate Governance Taskforce Report urges directors and officers to focus on overseeing and managing compliance risk, and implement better information flow between directors, senior management and risk committees.[28] This places a higher onus on directors to be pro-active in assessing and holding management accountable for non-financial risks (such as operational, conduct and compliance risks), in addition to directors' customary focus on financial risks.

13.4 ASIC's enforcement powers

The Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (**Royal Commission**) triggered a wide-spread toughening of approach by regulators to corporate governance and contravention in Australia.[29] In response to recommendations made by the Royal Commission, ASIC established an internal "Office of Enforcement", which has a broad range of enforcement powers aimed at the deterrence and punishment of wrongdoing in a targeted and proportionate way. ASIC's range of enforcement powers include issuing infringement notices, negotiating enforceable undertakings and initiating civil and criminal proceedings.

[25] ASIC Corporate Plan 2022–26: Focus 2022–26.
[26] Future of the Board (Governance Institute).
[27] ASX Corporate Governance Council's Corporate Governance Principles and Recommendations.
[28] ASIC's Corporate Governance Taskforce Report.
[29] Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry.

14. Insurance and indemnities

A director may be insured and/or indemnified against liabilities they may incur as a director, subject to a number of restrictions outlined below. In addition, a company or a related company must not exempt a person from a liability to the company incurred as a director of the company.

14.1 Restrictions on indemnifying directors

Indemnities for liabilities other than legal costs

A company or a related company must not indemnify a person against any of the following liabilities incurred as a director of the company:

- a liability owed to the company or a related company;
- a liability to pay a pecuniary penalty or compensation ordered under the Corporations Act; or
- a liability that did not arise out of conduct in good faith.

These restrictions do not apply to indemnities for legal costs, which are restricted as set out below.

Indemnities for legal costs

A company or a related company must not indemnify a person against legal costs incurred in defending an action for a liability incurred as a director of the company if:

- the director is found to have a liability for which the company may not indemnify them, as outlined above;
- the director is found guilty in criminal proceedings;
- the proceedings are brought by ASIC or a liquidator and the grounds for making the order sought are established; or
- the costs are incurred in connection with proceedings for relief to the director under the Corporations Act and the relief is not granted.

14.2 Restrictions on insuring directors

A company or a related company must not pay a premium for a contract insuring a present or former director of the company against a liability (other than for legal costs) arising out of:

- conduct involving a wilful breach of duty in relation to the company; or
- a breach of the duties not to improperly use their position or information.

15. Other sources of liability

In addition to the potential liabilities under the Corporations Act and common law summarised above, directors may incur liabilities under various other laws. Key laws of importance to directors are outlined below, but this is not an exhaustive summary.

15.1 Anti-bribery and corruption

Australia has anti-bribery laws at Commonwealth, state and territory levels, governing bribery offences relating to Commonwealth public officials, foreign public officials, and commercial or private bribery.

Directors can be personally liable for directly or indirectly giving or receiving a bribe, or if they are involved in the bribery, they may have accessorial liability. This can result in fines or imprisonment. In addition, if a director authorises a bribe, then this could result in significant financial penalties for a company.

ASIC, Australia's main corporate regulator, can be involved in investigations into corrupt conduct where an Australian corporation is involved - particularly in relation to associated offences in relation to the books and records of the company or in relation to directors' duties. Directors have been liable for breaching their directors' duties in circumstances where they "failed to join the dots" and identify corrupt conduct occurring within the company.

Baker McKenzie recommends that corporations adopt a compliance program to discourage and prevent bribery and corruption within their organisation. This program should be tailored to the corporation's geographical and operational risks, and directors should ensure that it is comprehensively and continually communicated, monitored and enforced. Directors should ensure that they receive regular reports in relation to the implementation of the compliance program and information in relation to any evidence of such conduct.

15.2 Competition

Directors may be liable for any personal contraventions of the CCA or Schedule 2 of the CCA (**ACL**), for example by engaging in misleading or deceptive conduct.

In addition, if a company breaches the CCA or ACL, any director (or other person) who was "involved" in the contravention may also be liable. A director is involved in a contravention if they aid, abet, counsel, procure, induce (or attempt to induce), are in any way knowingly concerned in or party to, or conspire with others to effect, the contravention.

A director who commits or is involved in a contravention may incur significant pecuniary penalties, liability to compensate others for loss suffered as a result of the contravention and, in the case of the prohibition on cartel conduct, substantial criminal penalties (up to 10 years' imprisonment). A director may also be disqualified from managing a corporation.

A company is prohibited from indemnifying a director for liability to pay a pecuniary penalty for breach of the CCA or ACL, or for legal costs incurred in proceedings in which they are found liable to pay such a pecuniary penalty.

15.3 Environment

In Australia environmental legislation and regulation operates at a Federal, State and Territory level.

The recently introduced *Environmental Legislation Amendment Act* 2022 (Cth) (**Act**) expands the liability and penalties that the Environment Protection Authority (**EPA**) can impose on corporations, directors and related bodies for the commission of environmental offences, both financially and criminally.

The maximum financial penalties imposed on individuals has now risen to $500,000 for failing to comply with environmental orders and $250,000 for giving false or misleading information. As an alternative to, or in addition to, the maximum monetary penalty, individuals can also be imprisoned for up to 18 months for making false or misleading statements in reports, and up to two years for repeat waste offences. Additionally, the Act also expands the offence of providing false and misleading information by including situations where it was provided unknowingly.

The Act broadens the definition of a 'fit and proper person', entitling appropriate regulatory authorities to determine whether a director of a corporation is a 'fit and proper person' based on whether current and former directors of the corporation and related bodies have contravened environmental protection legislation. Finally, the Act also widens the EPA's powers, giving them the authority to issue clean-up, prevention and prohibition notices for corporate environmental breaches. The imposition of stricter environmental obligations for corporations and directors will likely be the subject of further reforms for other States and Territories as

Commonwealth and State governments have committed to achieving net zero emissions by 2050. Similarly, the number of large Australian companies making net zero commitments has also risen. These net zero pledges, if unsubstantiated, may attract risk of personal liability for directors as acts of misleading and deceptive conduct under Australian Consumer Law.

It is important for directors to comply with new legislation and industry standards by ensuring proper strategies and implementation measures are in place. The recent scrutiny of climate-related disclosures and greenwashing further highlights the need for directors to embed climate action as a core focus for their organisation.

15.4 Employment

Directors can incur personal liability for their companies' breaches of some employment laws.

Under the *Fair Work Act 2009* (Cth) (Australia's national employment legislation) a director who was "involved in" a contravention of a "civil remedy provision" of that Act (most of the important provisions of that Act are civil remedy provisions) is deemed to have personally contravened that provision. This can happen if the director aided or abetted the contravention, induced the contravention, conspired with others to effect the contravention, or was "knowingly concerned in" the contravention.

Higher penalties apply where the company commits a serious contravention (that is, the provision was knowingly contravened and as part of a systematic pattern of conduct), and the director knew the company's contravention was a serious contravention.

From 7 June 2023, a new civil remedy provision will come into effect in relation to pay secrecy. From this date, a prohibition on including pay secrecy terms in employment contracts or other written agreements with employees that are inconsistent with the newly created "workplace right" in relation to pay secrecy will take effect. If a director is "involved in" a contravention of the pay secrecy provisions, the director could be deemed to have personally contravened that provision.

Additionally, under Victorian "wage theft" laws, directors are deemed to have committed an "employee entitlement offence" if their company has done so. An "employee entitlement offence" includes deliberately withholding wages or other employee entitlements, deliberately and dishonestly underpaying employees, falsifying employee entitlement records to gain a financial advantage and avoiding keeping entitlement records. In those circumstances, the onus will fall on the director to show that he/she exercised due diligence to prevent the occurrence of the offence. A director can still be prosecuted and found guilty even if the company is not.

Queensland has also amended its criminal code to include "wage theft" as a type of stealing. A director who aids the committing of an offence or counsels or procures a person to commit an offence will be taken to have committed the offence.

15.5 Anti-discrimination and sexual harassment

Commonwealth, state and territory legislation prohibit discrimination in the workplace and in the provision of goods and services on various grounds. These grounds include age, disability, union activity, pregnancy, breastfeeding, gender identity, intersex status, race, sex and sexual orientation. These laws also prohibit sexual harassment and, in some cases, other forms of harassment and conduct likely to humiliate or intimidate.

The *Anti-Discrimination and Human Rights Legislation Amendment (Respect at Work) Act 2022* (Cth) recently amended the *Sex Discrimination Act 1984* (Cth). These changes introduced:

- a positive duty on employers to eliminate unlawful sex discrimination. This duty applies to sexual harassment, sex-based discrimination, hostile workplace environments and victimisation;

- a prohibition against subjecting another person to a workplace environment that is hostile on the ground of sex; and
- a lower threshold for finding harassment on the ground of sex (the definition of harassment has been amended such that there is no longer a requirement for the alleged wrongdoer to have engaged in unwelcome conduct of a "seriously demeaning" nature, just that the unwelcome conduct was of a "demeaning nature").

Directors may be held personally liable under all these laws if they engage in harassment or discriminatory conduct or request, induce, instruct, encourage, authorise, or assist another person to commit a discriminatory or unlawful act.

The *Fair Work Act 2009* (Cth) also prohibits the taking of adverse action against an employee (or prospective employee) of the basis of their race, colour, sex, sexual orientation, breastfeeding, gender identity, intersex status, age, physical or mental disability, marital status, family or carer's responsibilities, pregnancy, religion, political opinion, national extraction, or social origin. This is a civil remedy provision, so a director will be taken to have contravened the provision if they aided or abetted the contravention, induced the contravention, conspired with others to effect the contravention, or was "knowingly concerned in" the contravention.

15.6 Workplace health and safety

A company which conducts business activities or undertakings in Australia, including engaging employees and contractors, has obligations under work health and safety legislation in each State and Territory. These obligations extend to workers, contractors, sub-contractors, employees of contractors, visitors, customers and any other person affected by the business activities or undertakings conducted by the company.

Directors can also be personally liable for offences under work health and safety legislation. Uniform work health and safety legislation in most States and Territories imposes positive obligations on each director and company officer to exercise due diligence to ensure the company complies with its work health and safety obligations.

Substantial penalties are imposed on companies and individuals for breach of work health and safety legislation. An individual director, officer or employee may also be imprisoned for up to five years for reckless conduct under work health and safety legislation.

A number of States and Territories have also recently introduced industrial or workplace manslaughter laws. The detail of these laws varies from place to place. In Victoria, a director who by negligent conduct causes the death of a person who is owed a duty under workplace safety legislation can, in some circumstances, be prosecuted and, if convicted, jailed for up to 25 years.

Additionally, in October 2022, NSW was the first State to pass amendments to their Work Health and Safety Regulations to provide for an explicit duty to eliminate or minimise workplace psychosocial risks. A psychosocial risk is one that arises from the design, management, environment, plant or interactions at work, that may increase the risk of work-related stress which can then lead to psychological or physical harm.

Other States and have followed suit, or have introduced Codes of Practice, reflecting a broader shift in the minimum standards expected in the management of psychosocial risks in the workplace.

15.7 Tax

Complicity in taxation offences

If a company commits a taxation offence, the directors who are concerned in, or take part in, the management of the company are deemed to have committed the same offence.

It is a defence if the director proves that they:

- did not aid, abet, counsel or procure the commission of the offence; or
- were not knowingly concerned in, or a party to, the commission of the offence.

Unremitted taxation and superannuation amounts - personal liability

Very broadly, directors are personally liable for any:

- pay as you go (PAYG) withholding amounts that are not remitted to the Commissioner of Taxation;
- superannuation contributions not made;
- goods and services tax (GST) liabilities or instalments of the company; and
- excise tax and wine equalisation tax,

unless the company:

- pays the amount in question;
- enters into an instalment arrangement with the Commissioner to remit the amounts;
- goes into voluntary administration (where an administrator of the company is appointed under section 436A, 436B or 436C of the Corporations Act);
- appoints a small business restructuring practitioner for the company under section 453B of the Corporations Act; or
- begins to be wound up.

These penalties may also apply to new directors who become directors after the due day for the amounts. New directors can incur a director penalty for the outstanding liabilities if they have not discharged the obligation (by payment, appointment of administrator or winding up) within 30 days of becoming a director.

Generally, it is a defence if a director can prove that:

- they did not take part in managing the company during the relevant time due to illness or some other reason, provided it would have been unreasonable to expect the director to take part, and the director did not take part, in the management of the company;
- either they took all reasonable steps to ensure that the company complied with its obligation, caused an administrator of the company to be appointed, the directors caused the company to begin to be wound up, or there were no reasonable steps that could have been taken to ensure that any of these things happened; or
- to the extent the penalty resulted from the company treating the *Superannuation Guarantee (Administration) Act 1992* (Cth) or the *A New Tax System (Goods and Services Tax) Act 1999* (Cth), as applying to a matter in a particular way that was reasonably arguable, if the company took reasonable care in connection with applying the relevant legislation to the matter.

Baker McKenzie helps clients overcome the challenges of competing in the global economy.

We solve complex legal problems across borders and practice areas. Our unique culture, developed over 70 years, enables our 13,000 people to understand local markets and navigate multiple jurisdictions, working together as trusted colleagues and friends to instil confidence in our clients.

bakermckenzie.com