Australian Institute of Company Directors

18 Jamison Street
Sydney NSW 2000
www.companydirectors.com.au
ABN 11 008 484 197

T: +61 2 8248 6600
F: +61 2 8248 6633

14 July 2020

Committee Secretary
Senate Select Committee on Financial Technology and Regulatory Technology
Department of the Senate
PO Box 6100
Parliament House
CANBERRA ACT 2600

Via email: fintech.sen@aph.gov.au

Dear Sir/Madam

Inquiry into the Financial Technology and Regulatory Technology sector

Thank you for the opportunity to appear at the public hearing before the Senate Select Committee on Financial Technology and Regulatory Technology (**Committee**) on Tuesday, 30 June 2020.

The Australian Institute of Company Directors' (**AICD**) wished to provide the Committee with the following additional evidence in response to questions taken on notice at the hearing. This additional material relates to international practice on virtual and hybrid AGMs as well as Australia's director liability settings.

1. Virtual and hybrid AGMs in foreign jurisdictions

Due to difficulties with the videoconferencing audio, the AICD was unable to provide full comment in response to a question from the Committee's Deputy Chair, regarding how foreign jurisdictions currently provide flexibility to enable companies to hold hybrid and virtual AGMs.

As outlined in the AICD's submission to the Committee on 17 June 2020, providing flexibility in the *Corporations Act 2001* (Cth) (**Corporations Act**) to enable companies to adopt the best format for their shareholder meetings (whether that be physical, hybrid or virtual) would bring us into line with other countries which allow both virtual and hybrid AGMs - such as the US, Canada, Spain, South Africa, Denmark, Ireland and New Zealand.

The ability to convene virtual and hybrid meetings under corporate law varies between countries. In the US it varies by state, and in Canada similarly by province. The relevant corporate law might expressly permit or facilitate virtual or hybrid meetings, or it might be capable of reasonable interpretation that such meetings are not prohibited.

Importantly, in most jurisdictions the legislative authority for companies to convene virtual and hybrid AGMs is accompanied by rules and conditions on the conduct and procedures of the meeting, such as:[1]

[1] Computershare, *The future of shareholder meetings is virtually here*, https://www.computershare.com/News/Virtual-Meetings.pdf

- the technology used must give all shareholders a reasonable opportunity to participate;
- the technology must be secure and must provide reasonable measures for verifying/validating those allowed to attend and vote at the meeting;
- the company must provide a digital record of the meeting; and
- in locations where only hybrid meetings are permitted, the physical meeting must be held in a specified place (e.g. the company's home country and town).

Notably, section 249S of the Corporations Act, which currently enables hybrid AGMs to be conducted subject to a company's constitutional requirements, already mandates that any technology used must give members, as a whole, a reasonable opportunity to participate.

Going forward, in the AICD's view, incorporating similar safeguards to those utilised overseas would preserve shareholder participation, while still enabling flexibility in delivery and technological neutrality.

2. Improving Australia's personal liability settings

In response to a question from the Committee's Chair, regarding the AICD's position on deregulation of the Regulatory Technology sector more broadly, we commented that there is an opportunity for a regulatory reset as a result of COVID-19 to allow directors and management to better focus on strategic growth and innovation.

As outlined in our submission to the Committee on 17 June 2020, the AICD's 2019 Innovation Study revealed that Australian boards are not prioritising innovation or disruption risks to the extent seen in overseas boardrooms, and that directors see Australia's legal settings and regulatory environment as contributing to a risk-averse corporate culture.[2]

This is underscored by Australia's uniquely burdensome director liability environment as evidenced by cross-jurisdictional legal research commissioned by the AICD in 2019 (enclosed **Appendix**).

The AICD is strongly of the view that Australia needs to actively create an environment where directors that act with integrity and commitment are free to pursue and harness new opportunities, drive recovery and create jobs without being overly focussed on personal liability concerns. At the same time, settings should ensure that individuals who do the wrong thing are held accountable. This will occur when the legal framework reflects sound underlying policy principles, and is both capable of being complied with, and appropriately targeted.

Limited nature of the Corporations Act business judgment rule

The AICD has long advocated for appropriate protections for directors who perform their roles with integrity and commitment, but who operate in a complex and compliance focused regulatory environment.

[2] AICD, 'Driving Innovation – The Boardroom Gap': https://aicd.companydirectors.com.au/-/media/cd2/resources/advocacy/research/2019/pdf/driving-innovation-the-boardroom-gap.ashx

A key issue has been the narrow operation of the statutory 'business judgment rule' in section 180(2) of the Corporations Act which applies to only one aspect of the Corporations Act, being the statutory duty of care and diligence in section 180(1) and its equivalent duties at common law or in equity.

Notably, the 'business judgment rule' is not available as a defence to *any* other alleged contravention of the Corporations Act, and is not the broad 'catch-all' defence it is sometimes suggested to be in public discourse.

Even in its application to section 180(1) and its equivalent duties at common law or in equity, leading corporate law experts have concluded that the current business judgment rule is deficient[3].

Some of the key limitations of the rule are outlined at a high level below. With this in mind, the AICD encourages the Committee to take into account Australia's director liability settings and the limitations of the existing 'business judgement rule' as part of the Committee's broader inquiry.

(a) Only relates to active decision-making

The business judgment rule is also specifically limited to 'decisions'. A business judgment is defined in the Corporations Act as 'any decision to take or not take action in respect of a matter relevant to the business operations of the corporation'. In other words, a director must positively turn their mind to an issue in order to rely on the rule. The defence will not be available in circumstances where the director has omitted to address a particular issue, even if this occurs in good faith and for good reason.

(b) Limited application of the rule

The scope of the rule has been further limited by judicial decisions which have confined the meaning of 'business judgments'. Matters considered to be of a 'compliance' nature (such as matters relating to market disclosure) are excluded from its operation, even though commercial considerations and complex business judgments will typically underpin such decisions.

This is particularly problematic as a result of the 'stepping stones' approach to director liability under which an individual director can be liable for a breach of their duty of care and diligence under section 180 of the Corporations Act where their organisation contravenes the law, or contraventions are foreseeable or likely, (including, for example, contraventions of the organisation's disclosure obligations)[4]. In such circumstances, they will not have recourse to the business judgment rule[5].

This circumvents natural justice principles and the express accessorial liability provisions of the Corporations Act, which require the regulator to prove that the officers were 'involved' in the contravention. It also deprives officers of any defences to accessorial liability that might

[3] Du Plessis, Jean and Mathiopoulos, Jim, Defences and Relief from Liability for Company Directors: Widening Protection to Stimulate Innovation (2016). Australian Journal of Corporate Law Vol. 31; Dr Robert Austin, 'Boards that Lead Need Better Protection', Australian Financial Review, 21 March 2013.

[4] See ASIC v Cassimatis (No 8) [2016] FCA 1023.

[5] Bednall T & Hanrahan P Officers' liability for mandatory corporate disclosure: Two paths, two destinations? (2013) 31 C&SLJ 474.

Australian Institute of Company Directors

otherwise have been available in the circumstances (for example, the 'reasonable steps' defence available to individuals, such as directors and officers, in the context of continuous disclosure obligations).

(c) Balanced liability settings needed to support economic recovery

The AICD believes that the current COVID-19 crisis highlights the need for reform in this area. This could involve, for example, modifying the business judgment rule to:

- ensure that it does not operate in an overly restrictive way by excluding certain decisions seen to be of a compliance nature even where they are underpinned by commercial considerations; and
- captures positive acts and omissions by directors (provided certain legislative conditions such as "good faith" and "proper purpose" requirements are met).

It might also involve a holistic review of the director liability environment more generally, including to ensure that there are appropriate defences across Commonwealth legislation for diligent directors who have acted in good faith and for a proper purpose.

3. Next steps

We hope the above supplementary material will be of assistance to the Committee's deliberations.

Yours sincerely

Christian Gergis GAICD
Head of Policy, Advocacy

Australian Institute of Company Directors

APPENDIX: Criminal and Civil Frameworks for Imposing Liability on Directors

To strengthen the evidence base on Australia's comparatively strict director liability environment, the AICD commissioned Allens to research the frameworks for imposing criminal and civil liability on directors in Australia and comparative jurisdictions (the UK, New Zealand, Canada, Hong Kong and the USA). The research considered contraventions of key corporations, prudential, competition, consumer, taxation, environmental and workplace laws, reviewing key similarities and differences between the jurisdictions.

In brief, the research concludes that while Australia has the same general frameworks for imposing criminal and civil liability on directors as other jurisdictions (namely, direct, accessorial and deemed liability), there are several important distinctions:

- Australia regulates a relatively broad range of subject matter through the imposition of director liability;
- Australia imposes criminal liability (with harsh penalties) on directors relatively liberally, particularly in relation to dishonest or reckless contraventions of their corporate governance obligations;
- The emergent doctrine of stepping-stone liability has the potential to further expand the ambit of director conduct that may be subject to public civil enforcement; and
- Australia's civil penalties are harsh, even as compared with Australian and other jurisdiction's criminal pecuniary penalties.

Additionally, Australia has a unique corporate criminal liability model, which can compel analysis of corporate culture and expose directors to corporate criminal proceedings even when their own conduct is not impugned.

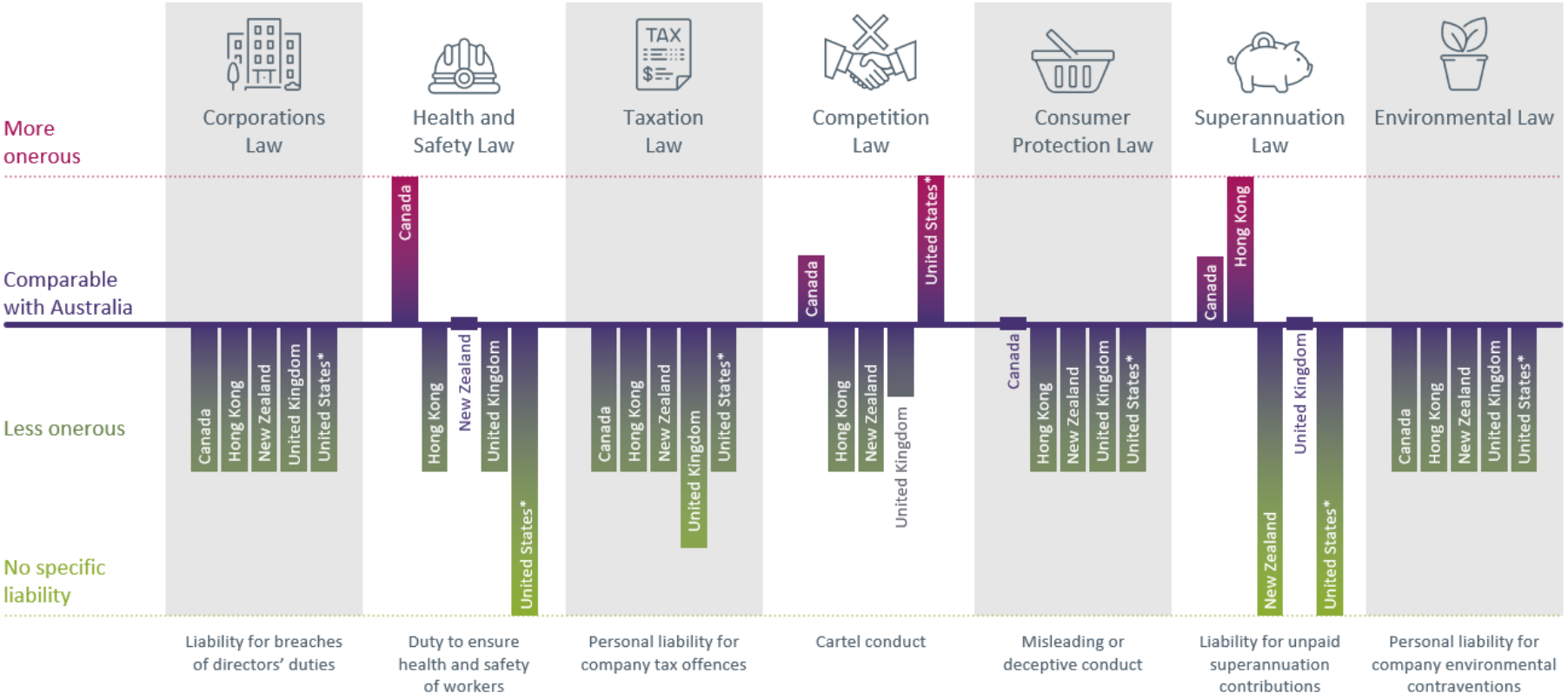
Based on the analysis, Allens considers that Australia's director liability environment is unique - and in many regards, uniquely burdensome - as compared with other jurisdictions. See diagram below which visually represents the key findings.

The full research paper can be found at https://aicd.companydirectors.com.au/-/media/cd2/resources/advocacy/policy/pdf/2020/aicd--advice-for-publication-including-organagrams.ashx.

Note: Allens' analysis is comprehensive and based on a review of key corporations, prudential, competition, consumer, taxation, environment and workplace laws across the relevant jurisdictions. Their conclusion that Australia is the most onerous overall is based on a holistic assessment of the legal environment. Certainly, core directors duties under the Corporations Act 2001 are the high-water mark as compared to other jurisdictions. However, Australia is not the most onerous across all areas considered (for example, Canada has more onerous workplace safety laws and the US more onerous competition and anti-cartel laws).

Australian Director Liability Benchmarking

Allens › ‹ Linklaters



Allens is an independent partnership operating in alliance with Linklaters LLP.

*selected jurisdictions (Federal and Delaware laws)